The Paperwork and Regulatory Improvements Act of 2003

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Thank you, Mr. Chairman, and members of this Committee, for the opportunity to present testimony on H.R. 2432, the "Paperwork and Regulatory Improvements Act of 2003." I'm Fred Smith, President and founder of the Competitive Enterprise Institute (CEI), a free-market public policy group focusing on regulatory issues.

I commend you for holding this hearing on a perennially important but increasingly urgent issue. Put quite simply, federal regulatory spending is uncontrolled and, therefore, out of control.

Economist Clyde Wayne Crews, Jr., formerly an analyst with CEI and now director of technology studies at the Cato Institute, produces an annual survey of regulatory trends called *Ten Thousand Commandments*. The just-released 2003 edition estimates the annual cost of federal regulation at $860 billion. That is larger than the Gross Domestic Product (GDP) of Canada ($701 billion), and easily exceeds the combined pre-tax profits of all U.S. corporations ($699 billion). Federal regulatory costs equal 42 percent of federal on-budget outlays ($2,011 billion), and dwarfs the federal budget deficit.[1]

Although federal fiscal discipline is far from perfect, federal regulatory discipline is practically non-existent. Consequently, regulation has long been the preferred tool of both special interests seeking to manipulate public policy for competitive advantage and ideological groups pursuing their particular visions of the public interest. For example, government can promote wind-, solar-, and biomass-generated electricity not only through on-budget tax breaks and subsidies but also through renewable portfolio standards—regulatory schemes imposing un-funded mandates on electricity producers and, thus, hidden taxes on electricity consumers.

With the federal deficit once again seen as a major fiscal and political liability, policymakers will increasingly be tempted to use off-budget regulatory spending to achieve their goals. That is why this hearing is so timely. Congress must begin to discipline federal regulatory spending.

CEI strongly supports the "Paperwork and Regulatory Improvements Act of 2003." Although the bill is by no means a cure for the defects of the regulatory process, it is a positive step in the right direction. Of particular importance, by directing the Office of Management and Budget (OMB) to designate at least five agencies as pilot projects in regulatory budgeting, the bill requires the Executive Branch to experiment with an essential component of fundamental reform.

My testimony has three main parts. Part 1 will discuss why federal regulatory spending is uncontrolled. There are two main reasons. First, nothing like a coordinated, unified federal budget exists to discipline regulatory spending. Second, Congress has little incentive to enact regulatory budgets because it does not take responsibility for the cost and quality of regulatory decisions. Rather, Congress delegates the authority not just to develop and propose but also to adopt

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[1] Clyde Wayne Crews, Jr., *Ten Thousand Commandments: An Annual Snapshot of the Federal Regulatory State*, 2003 Edition, Cato Institute, available at http://www.cato.org/tech/pubs/10kc_2003.pdf.

regulations to bureaucrats—non-elected officials who are not accountable via the ballot box to the public they supposedly serve. Part 2 will briefly discuss steps both big and small Congress and OMB should take to discipline the regulatory state. Part 3 will address three questions raised in the Chairman's letter of invitation.

1. Power without Responsibility

A. Regulation without Representation

The current regulatory process suffers from two major, related defects. First, it is a system of "regulation without representation." Congress passes and the President signs into law the broad regulatory statutes that govern the activities of various industries and sectors. Well-known examples include the Clean Air Act, the Occupational Safety and Health Act, and the Food, Drug, and Cosmetic Act. However, Congress and the President delegate to non-elected bureaucrats the tasks not only of developing and proposing the implementing rules, but also of enacting those rules. The original regulatory law lacked specificity—the implemented regulation creates real costs and benefits. Thus, the legislators largely escape responsibility—they only passed the law, not the regulation. Consumers and taxpayers—those who ultimately bear the costs and reap the benefits of regulation—cannot readily reward or punish anyone at the ballot box for good or bad regulatory decisions.

This system of non-accountability exists, because it provides incumbency protection for elected officials. Elected officials get to claim credit for the real or alleged benefits of regulatory statutes, and yet are free to blame someone else—the bureaucrats—when the implementing rules turn out to be controversial, costly, or unreasonable. New York University Law School Professor David Schoenbrod calls the regulatory state a regime of "power without responsibility." Elected officials exercise and enjoy the power to create regulatory programs but take no responsibility for the associated costs and red tape.

The result is a system of "regulation without representation." Elected officials are accountable to voters for the costs and benefits of tax and spending decisions, but not for the costs and benefits of regulatory decisions.

A key consequence of this non-accountable system is that Congress and the President feel little pressure to establish in the regulatory arena the kind of budget coordination, discipline, and oversight that everybody acknowledges to be indispensable in the fiscal arena.

B. No Budget and Accounting Act for Regulatory Spending

It is instructive to compare the early 20th century struggle to create the unified federal budget with current efforts, like H.R. 2432, to discipline regulatory decision making. This perspective is valuable, Mr. Chairman, because it clarifies that your bill is not partisan, nor indeed anti-regulation, but rather an important step to ensure that OMB examines regulation—a form of off-budget spending—as carefully as it examines federal spending programs.

The early 20th century struggle to reform federal expenditure policy was complex, took many decades to conclude, and encountered much opposition. However, eventually, both Democrats and Republicans came to realize the necessity for a unified budget and enacted the Budget and Accounting Act of 1921. The following account by the House Committee on Rules reveals striking similarities between that earlier struggle and your current reform effort:

> [Prior to the Budget Act, federal spending was] … a hodge-podge of overlapping efforts compounded by a similar lack of coordination in the executive branch. Executive departments submitted their requests for funds ***directly*** to the various committees with spending jurisdiction, sometimes making ***duplicate or overlapping requests*** to more than one committee. Although the Treasury did begin compiling the requests of the

> various departments into a single “Book of Estimates” in 1878, there was ***no authority for the President to submit a single, coordinated budget proposal, or for Congress to consider one***. The President was thus limited in his ability to influence or coordinated the efforts of nominally subordinate cabinet members.
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> Budgeting in the 19th century was thus quite different from the way it is understood and practiced today … A leading reform advocate, Charles Wallace Collins, wrote that ***“no one knows in advance of action, what the government proposes to spend in the coming year.*** This can be arrived at only at or near the close of a session by summing up the various bills that have been acted on.”
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> The result was a pattern of increased Federal spending which caused House Appropriations Committee Chairman James A. Tawney to conclude in 1910 that “the division of jurisdiction and responsibility in the matter of initiating appropriations ***has contributed more than any single cause to the enormous increase*** in appropriations during recent years.” This increase, as well as the rising incidence of deficits, inevitably resulted in a renewed call for reforms to pose better spending control.[2]

One could readily substitute “regulations” for “expenditures” in the foregoing account. Agencies directly translate legislative mandates into regulatory expenditures with little or no supervision by OMB or Congress. There is no authority for the President to submit a single, coordinated regulatory spending budget, or for Congress to consider one. Agencies are free to propose duplicative and overlapping regulations. No one knows in advance of agency actions what the total price tag for American businesses and consumers will be. The absence of coordinated oversight contributes to the never-ending increase in regulatory spending.

2. How to Discipline Regulatory Spending

A. End Regulation without Representation

Two themes should guide reform efforts: accountability and disclosure. Congress and the President would have much greater motivation to insist that agencies consider low-cost alternatives and non-regulatory alternatives if elected officials had to approve final agency rules before those rules become binding on the public. Politicians could no longer blame “rogue agencies” or “high-handed bureaucrats” when things go awry, because the buck would stop where the Constitution intended it to stop—with the people’s elected representatives.

The 1996 Congressional Review Act, which provides procedures for Congress to disapprove final rules, reflected Congress’s growing recognition that it should take more responsibility for regulatory decisions. However, the CRA has severe limitations. To stop an unwise regulation, somebody must expend the effort and political capital to organize legislative majorities in both chambers. Moreover, if the President vetoes the resolution of disapproval, then opponents of the rule must assemble super-majorities in both chambers to prevail.

What is needed is a mechanism that deters agencies from proposing bad rules in the first place, not one that makes it almost impossible to stop bad rules after agencies have finalized them. The Congressional Responsibility Act, sponsored by Rep. J.D. Hayworth (R-AZ), would require that Congress sign off on significant agency rules before they can become binding. Under this arrangement, a simple majority in each chamber could stop an ill advised rule just by declining to vote for it.

Critics may complain that Congress could not manage the increased workload if it had to approve regulations. But there are various ways Congress could streamline the review process. For

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[2] *Evolution of the Budget Process—Federal Budgeting Prior to 1921*, emphases added; accessible at http://www.house.gov/rules/jcoc2v.htm

example, administrative and other non-controversial rules could be bundled together and approved by a voice vote. Congress could approve each agency's minor rules as a non-amendable package through an up-or-down vote—the procedure used to close and consolidate obsolete military bases.

My recommendation is to start with "economically significant" rules (those estimated to cost the economy more than $100 million annually), and then gradually roll back this cap as the agencies, OMB, and Congress become more familiar with the process. Within some phased-in period, each agency would face hearings on the Hill to review the agency's regulatory impact analysis for each major rule. The hearing record, including the committee of jurisdiction's recommendations, would then inform the wider congressional debate and vote on the rule. Such a process would work as well—and no better—than current fiscal policy. But, at least, Congress would be responsible for regulations promulgated under the laws it enacts, and agencies would be more careful to develop sensible, cost-effective rules.

B. Towards a Budget Accounting Act for Regulation

As Congress assumes more responsibility for regulation, it will come under increasing public pressure to control regulatory costs, just as it faces public pressure to control tax and spending burdens. Sunshine statutes like the Paperwork Reduction Act, the Regulatory Right to Know Act, and the Chairman's Paperwork and Regulatory Improvements Act are indispensable to build support for increased oversight and discipline of regulatory spending.

The long-term reform goal should be to establish regulatory budgets for each agency and, ultimately, for the federal government as a whole.

In the fiscal arena, debate swirls around the question of whether an agency's objectives (say, the Department of Defense, or DOD) would be better advanced by spending more in category A (say, a new air mobile division) than in category B (say, a new battleship). An agency will, of course, fight for the highest possible budget, but it does so within the context of a larger debate over whether the Defense budget as a whole is too high, too low, or just about right. It is clear in advance to defense planners that they must make some effort to economize and make tradeoffs among competing programs. They are not free to pretend that the sky is the limit and money is no object.

In contrast, the regulatory debate focuses on the merits of each specific regulation. There is no budget cap because regulatory costs are off budget and therefore largely ignored. Moreover, the absence of any cap means that neither the regulatory agency, nor the Office of Information and Regulatory Policy (OIRA), nor Congress has much incentive to consider less costly or non-regulatory alternatives, let alone significant changes in program design or administration. Agencies fight for all regulations individually without regard to their cumulative cost.

I commend the Chairman for including in H.R. 2432 a provision to establish regulatory budgets in at least five agencies as pilot projects. Only stale and dull habit keeps us from being astonished that regulatory spending—equivalent to 42 percent of the federal fiscal budget—is off budget and subject to no formal constraints.

C. Regulatory Report Card

There are several types of information OMB could and should publish right now to build awareness of uncontrolled nature of regulatory spending, and the need for regulatory budgets. Wayne Crews, in each edition of his annual *Ten Thousand Commandments* report, has recommended that OMB publish a simple "Regulatory Report Card" that consolidates vast amounts of regulatory data already provided but scattered across government agencies. Such information includes, but is not limited to:

- Total numbers of economically significant and minor rules;

- Number of rules costing more than $500 million, $1 billion, and $10 billion;
- Available cost tallies for the current year's rules;
- Major rules required by statute;
- Rules that are deregulatory rather than regulatory;
- Major and minor rules that are discretionary;
- Rules facing statutory or judicial deadlines;
- Rules for which cost calculations are statutorily prohibited;
- Top rule-making agencies; and,
- Percentages of rules reviewed at the OMB and action taken.

Wayne suggests, and I concur, that the Report Card should be published annually as part of the Budget of the United States, and be supplemented with easy-to-read historical tables reviewing trends in the same types of information over the past five years. Congress and the interested public would be able to see at a glance, for example, whether the number of rules affecting small businesses and localities is going up or going down, whether any significant deregulation is occurring, whether regulatory activity at the top rule-making agencies is primarily driven by statute or agency initiative.

When regulatory cost information like this gains wider currency, and becomes part of the annual debate on the Budget of the United States, many in Congress, the media, and the interested public will see the need for a new Budget and Accounting Act to discipline regulatory spending.

3. Chairman Davis's Questions

I will now address three questions raised by Chairman Davis in his letter to me of July 8, 2003.

> **A. Should the General Accounting Office have a permanent staff devoted solely to evaluating certain regulations for the purpose of providing Congress an independent perspective on the value and effectiveness of these regulations?**

Given that we want to move towards a regulatory budget, and considering the Congressional Budget Office's superior resources in budgetary analysis, I would recommend creating a special unit or department within CBO. However, as I understand, CBO fears it would lose its clear mission and organizational identity if required to devote significant resources to regulatory analysis.

The Government Accounting Office (GAO) is a multi-purpose investigative agency, so enhancing GAO's capability to respond to congressional requests for analysis of economically significant rules may be reasonable. However, as Congress begins to take more responsibility for regulation, and as OMB begins to implement regulatory budgets, Congress may want to establish a separate congressional agency for regulatory review, or more strongly urge the Congressional Budget office to assure this responsibility. GAO's regulatory review team might develop and analyze alternative means of reaching their goal.

> **B. Should Congress require agencies to submit annual estimates of the costs and benefits associated with federal rules and paperwork for each of their agency's programs?**

Congress should require OMB to compile and submit annual *cost estimates* of federal rules and paperwork for each agency's program, but it is neither necessary nor desirable to require benefit estimates. Indeed, the push for cost-benefit or net-benefits analysis has diverted attention from more effective ways of prioritizing regulation. Moreover, such analyses are of little or no value in containing regulatory costs.

Cost-benefit analysis is designed to enhance the wisdom of each specific regulation, one at a time. Although largely based on the common sense notion that government interventions should do more good than harm (that is, produce more benefit than cost), cost-benefit analysis is easily caricatured as a corporate plot to put price tags on human life, children's health, and unique eco-systems.

More importantly, cost-benefit review has relatively little restraining effect. As long as the regulatory agency can argue that a rule has more benefit than cost, it is home free. OIRA already requires agencies to estimate net benefits for many rules. Most agencies soon learn to employ creative accounting or soft science to ensure high benefit-cost ratios. That is hardly surprising, because agency cost-benefit assessments are "inherently self-serving." As economists Randall Lutter and Richard Belzer explain:

> The same agencies that evaluate performance also design and administer the very regulatory programs they are evaluating. It is hard to understand why anyone should expect self-examinations to be objective and informative. Investors want businesses to be audited by analysts without financial conflicts of interest. Scientists reject research that cannot be replicated independently. Consumers flock to independent testing organizations rather than rely exclusively on sellers' claims. Only in the public sector, where bureaucracies are protected from the discipline of market forces, do we rely on self-evaluations of performance.[3]

The Environmental Protection Agency's Section 812 Report to Congress on the costs and benefits of the Clean Air Act is a prime case in point. In 1997, EPA's first report on rules issued from 1970 to 1990 presented a "best estimate" of net benefits of $22 trillion—roughly the aggregate net worth of all U.S. households in 1990. "We know of no professional economist who takes that estimate seriously," Lutter and Belzer comment. Indur Goklany, formerly chief of the technical assessment division of the National Commission on Air Quality, points out several bizarre implications of EPA's net-benefits estimate:

> One such implication of EPA's estimate is that in 1990 the nation would be willing to pay 20 percent of its GDP for just the health-related benefits of air pollution control despite the fact that it spent only 12 percent of GDP on all health care that year—an amount many [including Bill and Hillary Clinton] thought excessive. Another implication is that the nation is or should have been willing in 1995 to spend 60 percent of its GDP on eliminating all existing cases of chronic bronchitis. A third implication is that the nation should pay hundreds of thousands of dollars to eliminate the loss of one life-year because of air pollution even though there are many underused medical procedures that could provide the same benefit at a tenth or a hundredth of that cost. That would be a recipe for poor public policy and wasteful spending.[4]

Imagine what would happen if we took the same approach to spending agencies. Fiscal restraint would go out the window. For example, what is the monetary benefit of preventing a full-scale nuclear attack on the United States? Surely, whatever it is, it is larger than any expenditure we might make on defense programs. So if we relied solely or mainly on net-benefit analysis to control military spending, the defense budget could easily be two or three times what it is today.

Benefit assessments tend to be more subjective than cost estimates, because frequently benefits are in areas for which markets are weak or non-existent (for example, air quality), often because regulation preempts the evolution of private risk management arrangements. Thus benefit estimates tend to have such a large range as to be useless in guiding policy change. For example, OMB reports that, "health, safety and environmental regulation produces benefits

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[3] Randall Lutter and Richard B. Belzer, "EPA Pats Itself on the Back," *Regulation*, Vol. 23, No. 3, 2000, www.aie.brookings.org/admin/pdffiles/epa.pdf

[4] Indur Gokany, *Clearing the Air: The Real Story of the War on Air Pollution*, Cato Institute, 1999, p. 153.

between $30 billion and $3.3 trillion of net benefits per year."[5] That vast range makes it difficult if not impossible to draw any policy conclusions other than to be skeptical of agency benefit assessments.

Reliable cost information is, by comparison, easier to obtain. The Department of Interior (DOI) may not be able to put a price tag on the benefits of saving a population of spotted owls, but economists can probably estimate the impacts of DOI logging restrictions in the Pacific Northwest on timber sales, employment, industrial concentration, tax revenues, and the like.

Leaving out a requirement for benefit estimates would help OMB and the agencies devote more resources to cost estimation and disclosure. That's what we want, because regulatory budgets—the long-term objective of our efforts—are cost budgets, not net-benefits budgets. Agencies already do a reasonable job assessing costs for $100 million rules in the preparation of Regulatory Impact Assessments, on which many individuals and organizations submit public comments.

Focusing on costs doesn't mean benefits should be ignored. Rather, benefits should be addressed in the same way Congress and the President address them in on-budget spending programs. In both regulatory and spending programs, elected officials should make the "grand judgments" about whether the benefits are worth the costs. Presumably, they do this every time they enact, amend, or re-authorize such programs. The aim of reform should not be to require agencies to claim a net-benefit for every rule. Rather, the goal should be to encourage each agency to seek that mix of regulatory activities that would best advance their mission—and fall within their regulatory budget ceiling. Of course regulatory agencies would seek larger budgets by arguing the value of their programs—just as do spending programs. Greater cost disclosure combined with regulatory budgets would create the framework and incentives for such healthy competition. Ultimately, this dynamic would allow Congress to reallocate regulatory authority based on results achieved or not achieved.

Again, though, Congress will have a stronger incentive to link regulatory budgets to regulatory performance if Congress assumes responsibility for approving and disapproving agency final rules.

C. Should Congress integrate OMB's regulatory accounting statement into the President's Budget and make this statement cover the same time period as the President's Budget?

Yes, of course. What matters to the economy is the total burden of federal intervention. Consolidating the presentation of tax, spending, and regulatory cost information would help clarify the big picture for Congress and the public. Federal regulatory costs of $860 billion combined with on-budget outlays of $2,011 billion bring the federal government's share of the economy up to 27 percent. That is the total cost of the federal government, and that is what must be contained to preserve the dynamism and growth of the U.S. economy.

Furthermore, since our long-term objective is to establish regulatory budgeting, OMB should begin as soon as possible to integrate the presentation of regulatory cost information with its annual presentation of tax and expenditure information.

Conclusion

CEI strongly supports the "Paperwork and Regulatory Improvements Act of 2003." The bill is by no means a complete cure for the defects of the regulatory process, as the sponsors surely know. Moreover, CEI questions the wisdom—both on political and policy grounds—of attempting through net-benefit requirements to make regulatory agencies police themselves. Instead, the

[5] OMB, *Report to Congress*, 1998, p. 16.

Committee should put its emphasis on cost estimation and disclosure. The bill should require OMB to produce an annual Regulatory Report Card, with easy to read historical tables, so that Congress and the public can see at a glance the scope and scale of off-budget regulatory spending. Concentrating on cost-information and disclosure will also help set the stage for future regulatory budgets, which address the costs of regulatory spending, not the net-benefits thereof.

H.R. 2342, like the regulatory budgets it envisions, should be seen as complementary to accountability reforms designed to end “regulation without representation.” In the final analysis, the purpose of regulatory budgeting and of congressional review of agency actions is one and the same: to make the regulatory state more obedient to Congress and the President and, thus, more accountable to the American people.

Thank you.