



Issue Analysis

Reviving Regulatory Reform:

Options for the President and
Congress

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March 22, 2005

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ABOUT THE AUTHOR

I. Executive Summary

This report has a twofold purpose: reinvigorate public debate on regulatory reform, and help policymakers fashion a more affordable, effective, and accountable regulatory system. The report is organized as follows.

Section II examines the role of regulatory policy in sabotaging the 1990s economic boom. It finds that Federal Communications Commission (FCC) regulations, which subjected the telecommunications industry to a “what’s yours is mine” regime of infrastructure socialism and price control, inflicted trillion-dollar losses on an industry that was a key driver of the nation’s economic growth. Regulatory excess contributed to and prolonged the recession. The section concludes that Congress and the president, who are entrusted with stewardship of the U.S. economy, cannot afford to leave major regulatory decisions in the hands of unaccountable bureaucrats.

Section III tackles head on the opinion that regulatory reform is a pipedream—a thankless quest fraught with political peril and little chance of success. The chapter argues that although reformers in the 104th, 105th, and 106th Congresses failed to establish cost-benefit analysis and risk-assessment as touchstones of regulatory decision-making, they also achieved some notable successes. The Unfunded Mandates Relief Act (UMRA) has discouraged Congress from imposing new regulatory burdens on state and local governments. The Regulatory Flexibility Act, as amended by Small Business Regulatory Enforcement Fairness Act (SBREFA) and buttressed by President Bush’s Executive Order 13272, has, in some measure, reined in regulatory costs and agency discretion. The section recommends that future reform efforts be clearly based on three recognized principles of good government: cost disclosure, political accountability, and competition.

Section IV examines the basic flaws of the current process. Regulatory costs are large, growing, and, what is more disturbing, uncontrolled. Federal fiscal discipline is indeed weak, but federal regulatory discipline is practically non-existent. Many regulations function as implicit taxes, with far-reaching effects on consumer prices, employment, and innovation. Yet, nothing in the current process requires or even allows policymakers to make explicit choices about *how much* of the public’s resources regulatory agencies should control, or how regulatory authority should be *allocated* among alternate uses of the same resources. Moreover, most regulatory decisions are made by bureaucrats—officials over whom “We, the people” have little, if any, control. Americans live under a constitutionally dubious regime of regulation without representation.

Section V surveys initiatives reformers have proposed, adopted, or enacted during the past three decades, and identifies two main types: *policing* reforms and *checks and balances* reforms. Policing reforms aim via rules of rulemaking and centralized review to *regulate the regulators*. Checks and balances reforms seek to increase Congress’s responsibility for regulatory decisions, create inter-agency competition, or foster competition between agency experts and outside experts. Both types will be needed to make the regulatory system more affordable, effective, and accountable.

Section VI outlines steps to liberate the telecom industry from infrastructure socialism. Congress should amend the Telecommunications Act to phase out forced access regulation and price controls as quickly as possible.

Section VII discusses several near-term, mid-term, and long-term options for improving the regulatory process. Because of its complexity and controversial character, the most ambitious long-term reform—regulatory budgeting—is discussed separately, in section VIII.

The most important recommendations for policymakers presented in sections VII and VIII may be summarized as follows:

(1) *Make agencies compete for the right to score the costs and benefits of their regulatory proposals.* Agencies enjoy an exclusive right to determine which estimates of costs and benefits inform the rulemaking process. This creates a classic conflict of interest, because agencies have an obvious incentive to skew regulatory analyses in favor of their policy preferences and agendas. The Office of Management and Budget (OMB)—and the General Accounting Office (GAO), if Congress approves—should hold a contest to determine which analysis of each major regulatory proposal is best, reviewing the rulemaking agency’s cost-benefit estimates plus those submitted by experts in industry, state agencies, and the non-profit sector. To win the contest, the agency’s analysis would have to be more plausible than those submitted by competitors. At a minimum, agency analysts would have to visibly conform to OMB’s best practices and information quality guidelines or lose credibility as regulatory experts.

(2) *Require congressional approval before rules are effective.* Congress would have much greater motivation to insist that agencies consider low-cost and non-regulatory alternatives if it had to approve final agency rules before they could go into effect. Congressional review initially could be limited to “economically significant” rules—those likely to have an annual effect on the economy of \$100 million or more. The *Unified Agenda of Federal Regulatory and Deregulatory Actions* shows a total number of 127 economically significant rules at various stages of development in 2003, including 22 “completed actions.” Congress unquestionably could review 22 or even several dozen economically significant rules per year without shortchanging other important business. As it gained experience, Congress could lower the threshold and review rules likely to impose, for example, \$50 million in annual costs on state and local governments or the private sector, or \$25 million in annual costs on small business.

Making Congress accountable for regulation is a radical idea, but its radicalism lies in its fidelity to American principles of self-government. “No regulation without representation” clearly echoes the words and philosophy of those who signed the Declaration of Independence. No other general reform proposal has as great a potential appeal to common-sense populism. Regulations are implicit taxes that have the force and effect of law. If asked whether anyone other than their elected representatives should exercise the power to make laws or raise taxes, most Americans would unhesitatingly answer no. Paradoxically, this bold regulatory reform may ultimately be the most politically viable.

(3) *Undertake pilot projects to explore the feasibility of regulatory budgets.* Congressional review of regulations informed by competitive analysis would be a dramatic improvement over

the status quo. Nonetheless, we would never accept such a regime as adequate for making tax and spending decisions. In the fiscal arena, we do not ask Congress and the president to maximize the net benefit of each program, one at a time, in isolation from decisions about other programs, and without regard to the effects of total spending on the economy. Yet that is roughly what the current regulatory system asks agencies to do—assure the wisdom of each rule, without regard to the costs imposed by other rules, or to the cumulative burden of all rules on the economy.

Regulatory costs are, in a word, *unbudgeted*. Nothing resembling a budget framework requires or even allows elected officials to make explicit choices about how much of the nation's economy should be devoted to regulatory purposes, or about how resources should be allocated among the multitude of regulatory objectives. This fundamental flaw would persist even under a system of congressional review based on rigorous cost-benefit analysis.

Ideally, regulatory costs should be capped just like taxes and spending. However, no country has implemented this approach, and it is uncertain whether policymakers can develop the information and tools needed to reasonably estimate, accurately track, and credibly enforce limits on regulatory expenditures. Experimentation will be needed to assess the feasibility and desirability of establishing regulatory cost caps.

The potential benefits of regulatory budgets include limiting the growth of government, encouraging agencies to target resources on the most serious risks, and making agencies compete based on the effectiveness of their rules in saving lives and advancing public welfare. The potential perils of regulatory budgets include intensifying agencies' incentives to distort cost and benefit estimates, loss of political capital needed to secure other more attainable reforms, and increased paperwork burdens on regulated entities. Congress should authorize pilot projects to test the feasibility and advisability of setting regulatory budgets.

II. The Recent Recession: Was Regulatory Excess a Factor?

The beginning of the Bush presidency coincided with a sharp downturn in the U.S. economy. Predictably, Democrats blamed Bush for the ensuing recession and the loss of nearly 2.8 million manufacturing-sector jobs.¹ Such criticism is undeserved, and the 2004 *Economic Report of the President*, authored by the President's Council of Economic Advisors (CEA), implicitly provides a convincing rebuttal.

A. Council of Economic Advisors' Analysis

The downturn started before Bush took office, and events unrelated to Bush's economic policies—corporate and accounting scandals, the terrorist attacks of September 11, the dot.com collapse, and the Iraq War—weakened consumer and investor confidence, making the recovery “slow and uneven.”² More fundamentally, CEA traces the recession and slow recovery to “capital overhang”—a “structural imbalance” consisting of an excess of capital stock relative to the actual business opportunities for productive use of high tech equipment. Firms in mid-2000 sharply cut back purchases of software, computers, and other business equipment, and as a consequence, in the same year, high-tech stock prices plummeted. According to CEA:

The sharp break in investment occurred in parallel with an apparent reevaluation of future corporate profitability among financial market participants...The NASDAQ index of stock prices dropped nearly 50 percent from its peak in March 2000 to the end of the year. The prices of technology, telecommunications, and Internet shares fell particularly sharply, along with near-term earnings estimates.³

Manufacturing output declined substantially in mid-2000, mirroring the decline of business investment in equipment and software, and CEA speculates that the two developments are linked. Another source of weakness in the manufacturing sector, according to CEA, was “lackluster demand” for U.S. exports, due partly to slow economic growth in Europe and Japan.⁴ Exports fell sharply in the fourth quarter of 2000—again, prior to the Bush presidency.

To revitalize the economy, Bush sponsored legislation to end double taxation of dividends, to increase the level of capital investment small businesses are allowed to “expense” or immediately deduct in calculating taxable income, and to reduce family tax burdens. CEA attributes the economy's rebound in 2003 to the combination of Bush's tax policies and the Federal Reserve's expansionary monetary policy.⁵ But CEA offers no persuasive theory of why high-tech purchases nose-dived in the first place, and does not suggest that high taxes or tight money were to blame.

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B. Telecom Crash

Conspicuously absent from both Democrats' criticism and CEA's apologetics is any awareness of the part played by regulatory excess in sabotaging the 1990s economic boom. That is strange, because it is well known that the information technology (IT) sector, which includes the telecommunications industry, was the main engine of growth in the 1990s, and it is well documented, even if not widely known, that botched regulatory policy has literally cost the telecom industry trillions in shareholder losses, debt, and reduced investment.

An assortment of data published by the Commerce Department confirm and illustrate the vital importance of a healthy IT sector to a healthy economy:

- From 1989 to 2000, IT-intensive industries accounted for *all* growth in U.S. productivity (GDP per full time equivalent employee).⁶
- Between 1995 and 1999, IT producing industries contributed 30 percent of total real annual U.S. economic growth.⁷
- Total U.S. R&D investment leaped from an anemic 0.3 percent real annual growth during 1989-1994 to a robust 6 percent during 1994-1999. IT industry investment accounted for 37 percent of this growth.⁸
- Employment in IT producing industries jumped from 3.9 million in 1992 to 5.6 million in 2000, with average wages roughly twice the national average for all workers in non-farm industries.⁹
- By boosting productivity, IT investment increased wages generally. During 1996-1999, computer hardware investment alone contributed 24 percent of all labor productivity growth.¹⁰

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If IT firms propelled the 1990s boom, then it stands to reason that the IT sector's financial reverses in 2000 had strong ripple effects on output, employment, and growth in several industries. Telecommunications analyst Stephen Posciask, in a June 2003 report for the Competitive Enterprise Institute and the New Millennium Council, described the staggering magnitude of the IT sector's reverses, and the implication for the economy at large:

Over the past two years, telecommunications capital spending has fallen over forty percent. One-half million jobs have been lost in the IT sector during that time. The telecommunications industry has experienced an increase of \$800 billion in corporate debt and a two trillion dollar decrease in market valuation. As a result, the market valuation for telecommunications equipment manufacturers alone fell one trillion dollars in one year. The poor condition of the telecommunications industry, by correlation, provides one very compelling reason for the weak economy.¹¹

The much-decried loss of manufacturing sector jobs is linked to the telecom meltdown. The wave of telecom bankruptcies—the WorldCom crash being the most

spectacular—produced a surge in the availability of used telecom equipment as failing firms liquidated their assets. This used equipment competes with new equipment and holds down demand for manufacturers’ products.¹²

A question CEA should be asking, then, is what caused the telecom crash? Are the industry’s woes due to some mysterious “business cycle,” or are more specific causes at work? Detailed analyses of the crisis offered by credible observers, including Pociask, Scott Cleland of The Precursor Group,¹³ John Wohlstetter of the Discovery Institute,¹⁴ Peter Huber of the Manhattan Institute,¹⁵ Robert Crandall of the Brookings Institute,¹⁶ and Adam Thierer and Wayne Crews of the Cato Institute¹⁷ identify regulatory policy as a root cause of the industry’s travails.

C. Infrastructure Socialism

Supposedly, forced access would foster competition. However, coercive sharing is not competing, it is “infrastructure socialism.”

The Telecommunications Act of 1996 directed the Federal Communications Commission (FCC) to implement a regime of mandatory open access, or forced sharing of telecommunications networks. Specifically, the Act required “incumbent local exchange carriers” (ILECs)—the Bell companies that had built local telephone networks at their own expense—to share components of those facilities with new entrants, called “competitive local exchange carriers” (CLECs). Supposedly, forced access would foster competition, enabling new firms to enter the field despite the incumbents’ advantages. However, as Thierer and Crews point out, coercive sharing is not competing, it is “infrastructure socialism.” The Telecom Act set in motion a “what’s yours is mine” regime of legal plunder.

Price control is an inescapable feature of forced access. Incumbents must receive some compensation for sharing their facilities (known as “unbundled network elements,” or UNEs) with rivals. However, because the transfer is due to political coercion rather than voluntary exchange, government by default must set the price. Thus, although nominally a blueprint for “deregulation,” the Telecom Act spawned a gigantic, convoluted system of price controls. Thierer and Crews comment:

The FCC’s now-fabled August 1996 Local Competition Order...weighed in at an amazing 737 pages and contained more than 3,200 footnotes. The edict, which ranks as one of the most convoluted rules in the history of regulatory policymaking in America, contained a long list of specific elements owned by incumbent local exchange carriers (ILECs) that were to be subject to unbundling requirements under FCC-determined price regulations, including local loops, local switching capability, packet-switching capability, interoffice transmission facilities, databases and signaling systems, operator services, and directory assistance services. This long list of items subject to sharing mandates and open-access price

controls proved so contentious that it produced a stream of litigation that continues today.¹⁸

Although Congress intended open access to be a transitional regime, a halfway house between regulated monopoly and genuine facilities-based competition, the Act created a large class of clients with a vested interest in expanding and perpetuating their “right” to “share.” CLECs naturally wanted a free ride in perpetuity, and the FCC seemed happy to oblige, as this would entrench its control over the industry.

Worse yet, the FCC set the price for leasing network elements substantially below incumbents’ costs. ILECs not only had to allow CLECs to appropriate their facilities and customers, they had to subsidize them to boot. An incumbent can lose 60 percent of its revenues when it shares a line with a CLEC, while retaining 95 percent of the costs.¹⁹ The economic effects were predictable. Forcing incumbents to subsidize competitors attracted vast numbers of new entrants into the marketplace, creating a classic bubble characterized by too many companies chasing too few customers.²⁰ At the same time, as in any socialized system, the lazy got lazier, and the industrious saw little reason to build and innovate, since the lazy would just grab the fruits of their labor.

Using FCC data, Pociask calculated the extent to which CLECs opted to share incumbents’ facilities at discounted rates rather than build—or simply maintain—their own. In December 2000, 37 percent of CLEC telephone lines were leased network elements. By June 2003, 80 percent of all new CLEC lines were leased. Moreover, during the previous six months, CLECs had abandoned 231,000 of their own telephone lines. “Thus,” Pociask concludes, “the decline in CLEC-owned lines and the coincident increase in CLEC UNE-P [leased] lines demonstrates the stark end of CLEC investment” in telephone network infrastructure.²¹

By the same token, mandatory sharing at below market rates deters incumbents from investing in new facilities and upgrades, because they “fear that the application of unbundling and line-sharing mandates on new services will prevent them from recovering the exorbitantly high fixed costs of network service.”²²

The Telecom Act not only assumed that coercive sharing is competition or leads to competition, it also assumed that new firms cannot compete unless government manages the marketplace. The second assumption is as false as the first. As Thierer and Crews note, “The most credible facilities-based competitors that have arisen to challenge the hegemony of incumbent local telephone giants have been wireless cellular providers, which are unregulated and were almost completely ignored by the Telecom Act.”²³

D. Other Regulatory Blunders

Another major problem with the Telecom Act was that it perpetuated an archaic regulatory structure, imposing separate legal standards on telecommunications services, broadcast services, and cable services. This tripartite scheme may have

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made sense in the 1970s, but bears little relationship to market realities today. “Broadcasting, telephone, cable, and satellites are all heading in the same technological direction and competing for the same customers,”²⁴ and many companies are or seek to become integrated information, broadband, or network services providers, offering “the full range of communications services, including voice telephony, wireless cellular, data communications, and Internet access.”²⁵ Multiple regulatory standards artificially limit competition, discourage investment in integrated firms, and inequitably subject similar enterprises to dissimilar requirements.

Although the Telecom Act was flawed, both in its provisions and premises, it is fair to say that the FCC took a bad law and made it worse. Nothing in the law forced the FCC to set the lease rates for incumbents’ network elements at predatory prices. Nothing in the law allowed the FCC to delegate unbundling (access-sharing) decisions to state regulators.²⁶ If ever there was a national market transcending state and local boundaries, telecommunications is it. The FCC’s delegation of regulatory decisions to state commissions impedes the building of national networks, and robs the industry of regulatory certainty—a basic objective of the rule of law. Without predictable rules, investors cannot make plans. The certainty investors needed years ago will not come from the slow and uncoordinated machinations of 50 state commissions.²⁷

E. Implications for Policymakers

The telecom debacle has at least three broad implications for the wider debate on regulatory reform. First, the cost of regulation may be much greater than official estimates suggest. Even if the FCC’s forced access rules are responsible for only one-fifth the loss of telecom shareholder value and just one-tenth of the economic downturn of 2001, the cost exceeds by an order of magnitude OMB’s estimate of the combined annual cost (\$34 billion to \$39 billion) of all major rules promulgated during the past decade.

Second, Congress’s habit of authorizing agencies not just to develop and propose but also to enact market-structuring rules gives too much power over the nation’s economic life to non-elected bureaucrats and special pleaders. Instead of saving time, punting to the FCC the task of deciphering vague provisions of the Telecommunications Act merely set the stage for years of litigation and regulatory uncertainty. Congress should have to approve economically significant rules before they go into effect. That would encourage Congress to (a) write clearer laws in the first place, and (b) ensure that the implementing rules do as little economic harm as possible, because members would be accountable at the ballot box for the final regulatory product.

Third, in some important cases, regulatory reform cannot be separated from statutory reform. No general procedural regulatory reform can fix what ails the Telecom industry. What’s needed is a new Telecom Act, one that phases

out forced access as soon as possible, and sets a clear schedule for rolling back price controls and coercive subsidies.

III. Does Regulatory Reform Have a Future?

This report seeks to put federal regulatory reform back on the agenda of American politics. That goal may strike some as quixotic or foolish. In the 104th Congress, Republicans took a political beating for attempting to enact new cost-benefit, risk-assessment, and judicial review criteria for federal regulation. Reformers wanted agencies to have to demonstrate that the health, safety, and other benefits of proposed rules, expressed in dollars, would likely exceed the financial costs and economic impacts of those rules. They also wanted agencies to have to show that estimates of regulatory benefits were based on scientific assessments of the health, safety, and environmental risk factors to be addressed. Finally, they wanted to secure the right of regulated parties to sue agencies for noncompliance with the proposed cost-benefit and risk-assessment requirements. Because those proposals would apply broadly to multiple agencies and programs, proponents proudly described their agenda as *comprehensive* reform.

With an orchestrated unity that stunned reformers, scores of self-styled public-interest groups accused Republicans of seeking to gut essential “public protections,” and “roll back 25 years of environmental legislation.” Such slogans quickly framed the terms of debate. Competitive Enterprise Institute President Fred Smith hardly exaggerated when he described the dominant media spin on regulatory reform as: “Mad-dog Republican ideologues collude with robber-baron capitalists to regain the right to put poison in baby food bottles.” Even scaled-back versions of the reformers’ proposals crashed and burned in the 105th and 106th Congresses.

The “comprehensive” regulatory reform bills of the late 1990s were based on a grand political miscalculation. Few Americans have ever cast a ballot or joined a party, much less marched in the streets or gone to war, in the name of cost-benefit analysis and risk assessment. Such analytic techniques have zero populist appeal and are easily caricatured as a greedy, green-eye-shaded plot to “price the priceless.”²⁸ In hindsight, it is amazing that anyone believed an agenda centered on cost-benefit analysis could survive a battle with pressure groups claiming to fight for children’s health, worker safety, and a clean environment.

Although the debate is less acrimonious today, its terms have changed little since the 106th Congress. Business groups and many Republicans still complain that agencies exaggerate risks, low-ball costs, and inflate benefits to prop up unreasonable rules not justified by sound science and economics. Opponents still accuse regulatory reformers of seeking to use centralized review and ostensibly neutral analytical requirements to tie agencies’ hands and weaken essential public safeguards.

Both viewpoints have merit. An agency’s cost-benefit analysis is a public justification of what the agency wants to do. Consequently, every agency has an incentive to exaggerate the risks it seeks to address, overestimate the benefits of its

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proposed intervention, and underestimate the costs. By the same token, the White House and industry groups may seek to use OMB review and cost-benefit analysis to delay or weaken the implementation of statutes they lack the political muscle to attack openly.²⁹

However, neither side readily states the obvious: Regulation is inescapably a political process. The Progressive Era ideal of neutral agencies acting out of pure respect for law, science, and the public interest is fiction. Centralized review does inject politics into the rulemaking process, putting pressure on agencies to advance the president's priorities and policies. On the other hand, lack of centralized review allows "iron triangle" politics—insider negotiations among agency officials, congressional committee members (and staff), and lobbyists—to dominate regulatory outcomes.³⁰ Unsurprisingly, public interest group and agency criticism of centralized review diminished during the Clinton administration, when OMB shared their political agendas.³¹ Business groups, for their part, cling to the hope that regulators can be legislated or managed into practicing sound science and economics.

Since regulation is an inherently political process, reforms endeavoring to require agencies to be apolitical are bound to fail.

Regulations derive from laws. Regulations are necessary because laws inevitably lack the specificity required to address the manifold circumstances to which they apply. Even if agencies did nothing more than fill in the gaps, the proverbial devil often is in the details, enabling regulators to engage in discretionary lawmaking. Congress sometimes deliberately enacts vague provisions to avoid making tough choices on controversial issues, thereby punting to the agencies (and the courts) the job of defining what the law means. This creates additional space for bureaucratic lawmaking. And when agencies legislate, partisan agendas, organizational interests, and external lobbying pressures all come into play.

Since regulation is an inherently political process, reforms endeavoring to require agencies to be apolitical are bound to fail. This is not to say that sound science and economics are not valid normative concepts. Of course, the better the analysis that informs regulatory decisions, the better those decisions are likely to be. But sound science and economics cannot simply be produced by presidential edict or legislative fiat.

Agencies quickly learn to game almost any requirement that presidents and legislatures impose on them. For example, the Unfunded Mandates Relief Act (UMRA) requires agencies to prepare a regulatory impact analysis (RIA) for any rule likely to cause lower-level governments to increase their aggregate annual expenditures by \$100 million or more. The U.S. Environmental Protection Agency (EPA) estimated that the cost to states, territories, and tribal governments of its Total Maximum Daily Load (TMDL) Clean Water Act rule would not exceed \$25 million annually—and thus exempted itself from having to conduct an RIA.³² EPA's estimate seems contrived. According to state water pollution control

administrators, the TMDL rule's annual cost could range from \$670 million to \$1.2 billion.³³

One reason agencies can evade even statutory requirements is that courts are reluctant to second-guess regulators in their areas of expertise. Most judges are unwilling to reverse an agency's action just because they might draw different policy conclusions from the same (or better) evidence. An agency's analytical methods must be flagrantly sloppy to place a rulemaking in legal jeopardy.

Even when courts do strike down a rule, the agency normally suffers no penalty beyond possible adverse publicity. The agency may simply repackage a vacated or remanded rule and hope for better luck in the next round. Telecom provides a telling example. The Supreme Court once and the D.C. Circuit Court of Appeals twice have struck down portions of the FCC's forced access rules requiring incumbent local carriers to lease their networks to rivals at discounted prices.³⁴ Nine years after Congress enacted the 1996 Telecommunications Act, the regulatory framework of the telecom industry remains in litigation limbo. Judicial review may sometimes be a necessary last resort, but it is seldom a high road to regulatory certainty.

Nonetheless, regulatory reform need not be a pipedream. Reformers have achieved some successes, and greater victories may yet be won. For example, as is discussed in section V, UMRA and a suite of small business regulatory reforms have had some constraining effect on agency discretion and regulatory costs. UMRA's point of order provision enables any member to force the House or the Senate to debate and vote on whether to consider a bill with intergovernmental mandates estimated to cost \$50 million a year or more. Although UMRA has had little impact on agencies, it has had a chilling effect on the number and size of new regulatory mandates emanating from Congress.

The Regulatory Flexibility Act (RFA), as strengthened by the Small Business Regulatory Enforcement Fairness Act (SBREFA) and President Bush's Executive Order 13272, requires the Small Business Administration's (SBA) Office of Advocacy to play a wide-ranging role in regulatory development. This series of reforms enables SBA, in some measure, to check and balance other agencies. Advocacy reports that, in FY 2003, its multi-stage interventions in numerous rulemakings saved small entities more than \$6.3 billion.³⁵

UMRA has had limited success because it embodies two key principles: cost disclosure and congressional accountability. UMRA not only requires the Congressional Budget Office (CBO) to estimate the cost of mandates in new legislation, it also allows Congress to take some responsibility for those costs. That is critical, because members of Congress, unlike agency personnel, are accountable to the regulated public at the ballot box.

The RFA-related reforms have had limited success because they embody another key principle: competition. The RFA, as amended by SBREFA and buttressed by E.O. 13272, gives SBA's Office of Advocacy means and motives to scrutinize agency

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Three principles should guide general regulatory reform in the twenty-first century: cost disclosure, political accountability, and competition.

No budget mechanism forces Congress to make explicit choices about the size of the regulatory burden relative to the economy as a whole, or about the appropriate allocation of resources among different regulatory objectives. Regulatory costs are unbudgeted or hidden.

analyses and offer real alternatives. SBA's interventions provide partial relief from the monopoly each agency otherwise maintains over its own rulemaking process. As in any market, competition tends to improve quality and lower cost.

Three principles then should guide general regulatory reform in the twenty-first century: cost disclosure, political accountability, and competition. Those principles are pillars of good government, transcending party labels and ideological biases. Although the status quo has many defenders, they may find it difficult to oppose reforms clearly based on good government precepts. If even a few policymakers have the courage to champion disclosure, accountability, and competition, regulatory reform may yet have a political future.

IV. Uncontrolled Costs, Unaccountable Decisions

Regulatory reform may be possible, but why is it desirable? What are the basic flaws or defects of the regulatory state, and how serious are they? Section IV attempts to answer these questions.

The regulatory state as it has evolved saps the nation's economic vigor and undermines the political accountability essential to democratic self-government. The costs of federal regulation are large, growing, and, what is more disturbing, uncontrolled. No budget mechanism forces Congress to make explicit choices about the size of the regulatory burden relative to the economy as a whole, or about the appropriate allocation of resources among different regulatory objectives. Instead, regulatory decisions are made by bureaucrats—officials over whom “We, the people” have little if any control.

A. Regulatory Costs: Off-Budget or Unbudgeted?

Nobody knows exactly how much Americans spend every year to comply with federal regulations. Most firms do not maintain accounts for the expenditures they make to comply with federal rules. They have no reason to do so, because Congress does not set statutory limits on the costs regulatory agencies may impose on them. The federal government makes no effort to track regulatory expenditures through the kinds of budget and accounting systems it uses to track fiscal expenditures and tax receipts. Consequently, most firms do not monitor regulatory costs as a category separate from other business costs.

Regulatory costs are often described as *off budget*, but that is somewhat misleading. Social Security outlays and revenues and Postal Service cash flows are off budget—excluded from the totals in both the president's annual budget submission and Congress's budget resolution. However, both Social Security and the Postal Service operate within budget frameworks and their expenditures are tracked as carefully as those of any other federal program or agency. Thus, it would be more accurate to describe regulatory costs as *unbudgeted* or *hidden*. Hidden costs are, of course, difficult to estimate, much less control.

Even if regulated entities maintained accurate, consistent, auditable accounts for regulatory compliance expenditures, we would still not know the total cost of federal rules. As James Gattuso of the Heritage Foundation points out, some regulatory costs “are by their nature unknowable”:

For many economic regulations, the major cost may not be any direct burden on consumers or businesses, but constraints on innovation. Assessing such losses is impossible because inventions that never existed cannot be measured. In today’s 21st century economy, these un-measurable costs are perhaps more harmful than the measurable burdens.³⁶

The total cost includes a variety of indirect effects on consumer prices, employment, output, competitiveness, and innovation—effects that cannot be inferred from companies’ balance sheets. Yet indirect regulatory costs may dwarf the direct costs. The FCC’s telecom access regulations, for example, had trillion-dollar economic repercussions.

The telecom debacle aside, numerous proxy measures indicate that regulatory costs are substantial and growing.³⁷

- The total number of *Federal Register* pages per decade has increased dramatically, from 170,325 in the 1960s, to 450,821 in the 1970s, to 529,233 in the 1980s, to 622,368 in the 1990s, to 713,920 in the 2000s (based on a four-year average).
- The *Code of Federal Regulations* has grown from 22,877 pages in 1960, to 102,195 pages in 1980, to 144,177 pages today.
- In constant (real) 2000 dollars, federal spending on regulatory agencies has increased from \$2.5 billion in 1960, to \$5.7 billion in 1970, to \$13.4 billion in 1980, to \$16.5 billion in 1990, to \$24.6 billion in 2000, to an estimated \$36.2 billion in 2005.³⁸
- The 2003 *Federal Register* contained 22,670 pages devoted to final rules, more than any other year during 1994-2003 except 2000.
- The average number of annual regulations for the current decade (2000-2004) is 4,190, slightly lower than the 1990s average of 4,596. However, annual output remains consistently above 4,000 final rules.
- Agencies take many more regulatory actions than deregulatory actions. From 1997 through the end of the Clinton administration, 78 percent of major final rulemakings increased rather than decreased regulatory burdens. From the start of the Bush Administration to the end of 2003, 75 percent of major final rulemakings increased rather than decreased regulatory burdens.³⁹

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We turn now to two widely discussed efforts to estimate federal regulatory burdens.

B. Regulatory Costs: OMB's and Hopkins's Estimates

The most comprehensive “guesstimate” of federal regulatory costs is a 2001 study prepared for the Small Business Administration by economists W. Mark Crain of George Mason University and Thomas D. Hopkins of the Rochester Institute of Technology.⁴⁰ The Crain-Hopkins study builds on an earlier study Hopkins conducted for SBA in 1995.⁴¹ OMB criticized that study in some detail in its first (1997) annual report to Congress on the costs and benefits of regulation, reaffirmed those criticisms in the next edition,⁴² and has not retracted them in later editions.

Since transfers redistribute wealth rather than directly reduce it, OMB's 1997 report views such burdens as having no “net” social cost. By OMB's logic, socializing the means of production would have no net social cost.

Crain and Hopkins estimated and aggregated the costs of tax compliance (time spent rather than taxes paid), workplace rules, economic regulation (constraints on pricing, entry, and investment), environmental protection, and transfer rules (regulations such as farm price supports that shift money from one group to another). They estimated year 2000 regulatory costs at \$843 billion.

Since transfers redistribute wealth rather than directly reduce it, OMB's 1997 report views such burdens as having no “net” social cost, and therefore regards their inclusion in an estimate of total regulatory costs as inappropriate.⁴³ Crain and Hopkins argue that transfers should be included because interest group competition impels rivals to keep spending on political activities until the expenditures are “commensurate” with the transfer at issue, and every dollar so spent is diverted from other, more productive activities, placing “a real resource burden on the economy.”⁴⁴

Crain and Hopkins's basic point surely has merit. Coercive wealth transfers impair economic performance and thus burden the economy. As one witness at a recent hearing put it, “Regulations involving ‘mere’ transfers alter people's behavior, either by directly prohibiting or mandating certain activities or by altering prices and costs. The value forgone when resources are thus redirected represents real costs to society, which economists refer to as ‘deadweight losses’ or ‘excess burdens.’”⁴⁵ The telecom crash demonstrates the inappropriateness of regarding transfers as an economic wash. Coercive wealth transfers from ILECs to CLECs created a bubble while stifling investment and innovation. Legal plunder makes societies poorer. By OMB's logic, socializing the means of production would have no net social cost.

Even apart from their incentive effects, regulations that rob Peter to pay Paul should be included in estimates of regulatory burden. After all, to those who foot the bill, the costs of regulatory transfers are every bit as real as the costs of tax transfers. Nobody would say, for example, that taxes spent on military programs should not be included in estimates of total tax burden because the programs provide monetary benefits to defense contractors, service personnel, and Pentagon bureaucrats. By OMB's logic, tax hikes do not really increase tax burdens, because the government inevitably spends the tax dollars it collects.

In any event, for perspective, Crain and Hopkins estimated that, if transfers are excluded, year 2000 regulatory costs drop to \$495 billion, with businesses paying \$295 billion and others (individuals and state and local taxpayers) paying \$201 billion.

Table 1. Billions of dollars in 2000

Types of regulation	Business pays	Others pay	Total
Tax compliance	70	59	129
Workplace	24-82	0	24-82
Economic	72-217	72-217	145-435
Environmental	128	69	197
All Regulation	295-497	201-346	495-843

Source: Thomas D. Hopkins, Testimony, *Regulatory Accounting: Costs and Benefits of Federal Regulation*, Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs, March 12, 2002, p. 58, [http://reform.house.gov/UploadedFiles/Printed%20Hearing_03-12-02_Reg%20Acct%20\(107-155\).pdf](http://reform.house.gov/UploadedFiles/Printed%20Hearing_03-12-02_Reg%20Acct%20(107-155).pdf).

OMB also objected to including tax-related paperwork in an estimate of total regulatory costs. The tax code and its complexities—not the derivative IRS rules—are what make tax preparation complicated, difficult, and time-consuming. Tax reform, not regulatory reform, is the cure for tax-related paperwork, and citing such burdens as a reason for regulatory reform, “especially when the tax numbers are so large relative to social and economic regulatory costs, just confuses the issue.”⁴⁶

OMB’s criticism has merit, but misses a larger point. All rules—not just IRS rules—derive from an underlying statute. Consequently, if the costs of a regulatory program are excessive, the first order of business may be to reform the statute. As OMB observes elsewhere: “...when we speak of the costs or benefits of ‘regulations,’ we are, in reality, speaking of the costs and benefits of legislation as well as regulation, for it is usually impossible, and not always productive, to try to allocate costs and benefits between the authorizing statute and its implementing or interpreting regulations.”⁴⁷ Congress would have more incentive to reform the tax code if it had to take responsibility for Treasury’s implementation and the associated paperwork.

Crain and Hopkins’s cost estimates for environmental regulation build on a 1995 study by Hopkins, which in turn was “based on individual studies that were published, for the most part, between 1975 and 1990,” according to OMB.⁴⁸ In other words, the Crain-Hopkins estimates derive from old analyses of even older data—analyses that would not reflect subsequent reductions in compliance costs due to technological advances and learning by doing.

Surprisingly though, despite those criticisms, OMB’s own “guesstimate” of total regulatory burdens is in the ballpark with Crain and Hopkins’s.

OMB’s 2003 final report estimates the annual costs of 107 major rules adopted during FYs 1992-2002 to be between \$36.6 billion and \$42.8 billion, with total annual benefits ranging from \$135 billion to \$218 billion.⁴⁹ However, the 107 major rules OMB reviewed comprise less than one percent of all rules issued by federal agencies

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during that ten-year period. OMB acknowledges that, “the total costs and benefits of all Federal rules now in effect (major and minor) could easily be a factor of ten or more larger than the sum of the costs and benefits reported [above].”⁵⁰ In other words, the total cost of all federal rules could exceed \$366 billion to \$428 billion per year. If we subtract from Crain and Hopkins’s total (\$843 billion) the estimated costs of transfers (\$348 billion) and tax-related paperwork (\$129 billion), we get \$366 billion—the *low end* of OMB’s guesstimated range.

Similarly, OMB’s 2004 draft report estimates the annual cost of major rules promulgated during FYs 1993-2003 at \$34 billion to \$39 billion, and once again OMB acknowledges that the total cost of all rules in effect during that period could easily be ten times larger or more.⁵¹

In short, even if transfers and tax-related paperwork are excluded, annual federal regulatory costs range in the hundreds of billions of dollars. And, since federal agencies issue about 4,000 new rules a year, taking many more regulatory than deregulatory actions, it stands to reason that federal regulatory costs are growing.

C. OMB’s 2003 Report: Do Benefits Justify Costs?

OMB’s 2003 report indicates that the 107 major rules issued during FYs 1992-2002 generated three to five times more benefit than cost. Some might conclude that regulation more than pays for itself, hence there is no reason to worry about cost. That would be a mistake.

Even if regulations do produce net benefits, the costs may still be excessive. For example, suppose welfare expenditures were ten times the size of current outlays. If the benefits include preventing hundreds of thousands of people from starving, total benefits arguably would still exceed total costs. However, no reasonable person would regard such a program as an efficient or prudent investment of the nation’s resources.

Furthermore, even if total regulatory benefits exceed total regulatory costs, many individual rules may do more harm than good (produce more cost than benefit). According to OMB, the bulk of the benefits—\$101 billion to \$119 billion—come from just four of the 107 major rules it reviewed: sulfur dioxide limits established by the 1990 Clean Air Act Amendments, regulations limiting particulate and nitrogen oxide emissions from heavy duty truck engines, and the Tier 2 rule limiting emissions from light duty vehicles.⁵² Those four EPA rules alone may be responsible for 88 percent of the estimated benefits. At the very least, that should raise questions about the efficiency of the other 103 major rules.

The proposition that federal rules produce three to five times more benefit than cost has little credibility. Agencies have an obvious incentive to downplay the costs and exaggerate the benefits of the programs they administer, and, as OMB’s 2003 report acknowledges, “OMB has not made any changes to agency monetized estimates other than converting them to annual equivalents.” Thus, says OMB, “our citation of, or reliance on, agency data in this report should

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not be taken as an OMB endorsement of all the varied methodologies used to derive benefits and cost estimates.”⁵³ In other words, OMB’s role in estimating the aggregate costs and benefits of federal rules was that of a mere compiler rather than that of an independent auditor.

For example, OMB did not question the assumptions on which EPA based its benefit estimates for the four rules noted above. According to OMB, EPA assumed that: (1) inhalation of fine particles is causally associated with premature death at concentrations near those experienced by most Americans on a daily basis; (2) all fine particles, regardless of chemical composition, are equally potent in causing premature mortality; and, (3) the concentration-response function is approximately linear (i.e., there is no threshold beneath which adverse health effects do not occur).⁵⁴ All those assumptions are controversial.⁵⁵ For example, a recent peer-reviewed paper in the respected *Journal of Environmental Economics and Management* finds that uncertainties in air pollution-mortality models are “so large as to question the plausibility of previously measured links between air pollution and mortality.”⁵⁶

Finally, OMB’s cost-benefit tally takes no account of the trillion dollar losses induced by botched telecom rules. OMB’s 2003 report says nothing about the role of forced-access regulation in stifling investment, output, and employment in the telecom industry, or the economy-wide repercussions. What little information OMB has about the costs and benefits of rules issued by the FCC and other independent regulatory commissions it gets second-hand from GAO studies, which are also just compilations of agency estimates, not independent audits. According to OMB’s 2003 report, the FCC “did not prepare cost-benefit analyses” for any of the rules it issued in FY 2002,⁵⁷ and previous editions reveal the same lack of information.⁵⁸ OMB’s 2004 draft report does not even mention the FCC.

In summary, although the total cost of federal regulation is unknown and even unknowable, it is reasonable to assume that regulated entities spend hundreds of billions of dollars annually to comply with federal rules, and that the indirect cost of recent-year FCC rules is even larger. Although agencies routinely claim high benefit-cost ratios for their rules, OMB does not—and due to resource constraints cannot—validate such claims. Given the substantial (and very likely growing) cost of federal regulation, to say nothing of regulation’s role in undermining the economic recovery, regulatory improvement should figure prominently in policymakers’ efforts to spur growth and expand opportunity.

D. Regulation without Representation

The current regulatory process is a system of *regulation without representation*. Elected officials enact 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 Telecommunications Act. However, Congress and the president delegate to non-elected officials the tasks not only of developing and proposing the implementing rules, but also of enacting those rules. The original regulatory law typically lacks specificity. The implementing rules are the proximate cause of the associated costs. Thus, elected officials largely escape responsibility for those costs—they only approved the law, not the regulation.

Although the total cost of federal regulation is unknown and even unknowable, it is reasonable to assume that regulated entities spend hundreds of billions of dollars annually to comply with federal rules.

Consumers and taxpayers—those who ultimately bear the burdens and reap the benefits of regulation—cannot reward or punish anyone at the ballot box for good or bad regulatory decisions.

One explanation for this system of non-accountability is that it provides incumbency protection for elected officials. Lawmakers get to claim credit for the real or alleged benefits of regulatory statutes, 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 process a system of “power without responsibility.”⁵⁹ Elected officials wield the power to create regulatory programs, but they take no responsibility for the consequent costs and red tape.

Congress’s delegation of legislative power to administrative agencies and regulatory commissions flouts the letter and spirit of the U.S. Constitution. “After a single perambulatory sentence,” observes former OIRA Administrator and Federal Judge Douglas Ginsburg, “the Constitution begins with this simple proposition: ‘All legislative powers herein granted shall be vested in a Congress of the United States.’”⁶⁰ Article I §1 vests “all legislative powers” in Congress—not in non-elected bureaucrats. And nowhere does the Constitution give Congress the power to delegate legislative powers to other branches or bodies.

In the political theory underpinning our Constitution, governments derive “their just powers from the consent of the governed.”⁶¹ This means that all powers—legislative, executive, and judicial—originate in the people, and legitimate government arises from a compact whereby the people agree to delegate certain powers to certain offices or institutions. In a regime of delegated powers, officials are the *stewards*, not the owners of power. Just as legislatures have no right to seize powers the people have delegated to the executive, so they also have no right to transfer to the executive powers the people have delegated to them.

The English philosopher John Locke succinctly explained what later came to be called the *non-delegation doctrine*:

The legislative cannot transfer the power of making laws to any other hands, for it being but a delegated power from the people, they who have it cannot pass it over to others. The people alone can appoint the form of the commonwealth, which is by constituting the legislative, and appointing in whose hands that shall be. And when the people have said, “We will submit, and be governed by laws made by such men, and in such forms,” nobody else can say other men shall make laws for them; nor can they be bound by any laws but such as are enacted by those whom they have chosen and authorized to make laws for them.⁶²

The proposition that legislatures may not transfer the power to make laws is a necessary implication of the compact theory of government, and it informed

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U.S. jurisprudence for more than a hundred years. For example, in 1892, the Supreme Court in *Field v. Clark* declared: “That Congress cannot delegate legislative power to the President is a principle universally recognized as vital to the integrity and maintenance of a system of government ordained by the Constitution.”⁶³

How then did the modern regulatory state arise? In the crisis atmosphere of the Great Depression, Congress enacted President Franklin Roosevelt’s New Deal economic agenda, which called for sweeping delegations of legislative power to administrative agencies. The Supreme Court initially struck down the New Deal programs as unconstitutional, but Roosevelt’s proposal to enlarge the Court cowed the justices, effectively suspending the non-delegation doctrine. David Schoenbrod and Jerry Taylor of the Cato Institute explain:

Shortly after taking office, Congress in 1933 granted Roosevelt virtually unlimited power to regulate commerce through passage of the Agricultural Adjustment Act (which authorized the president to increase agricultural prices via administrative production controls) and the National Industrial Recovery Act (known as NIRA), which authorized the president to issue industrial codes to regulate all aspects of the industries they covered.

The Supreme Court, however, temporarily arrested the tide in 1935 in its unanimous opinion in *A.L.A. Schechter Poultry Corp. v. United States*. The Court overturned the industrial code provisions of the NIRA, and, in a separate opinion, Justice Benjamin Cardozo termed the NIRA—and thus the New Deal—“delegation running riot.” That same year, the Court struck down additional NIRA delegations of power in *Panama Refining Co. v. Ryan*.

Largely because of the *Schechter* and *Panama Refining* decisions, President Roosevelt decried the Court’s interference with his political agenda and proposed legislation enlarging the size of the Court so that he could appoint additional justices—the so-called Court-packing plan. He lost that battle but won the war. Although the Court never explicitly reversed its 1935 decisions and continues to articulate essentially the same verbal formulas defining the scope of permissible delegation—indeed, *Schechter* and *Panama Refining* theoretically are good law today—it would be nearly 40 years before the Court again struck down business regulation on delegation grounds.⁶⁴

Some would argue that the regulatory state would have developed even if Roosevelt had not intimidated the Court, because Congress’s delegation of legislative power to regulatory agencies was an inevitable consequence of the rise of big, activist government. But the opposite is more likely the case. Big, activist government is a consequence of delegation. Schoenbrod and Taylor comment:

Perhaps the ultimate check on the growth of government rests in the fact that there is only so much time in a day. No matter how many laws Congress would like to pass, there are only so many hours in a session to do so. Delegation, however, dramatically expands the realm of the possible by effectively “deputizing” tens of thousands of bureaucrats, often with broad and imprecise

missions to “go forth and legislate.” Thus, as Jacob Weisberg has noted in the *New Republic*, “As a labor-saving device, delegation did for legislators what the washing machine did for the 1950s housewife. Government could now penetrate every nook and cranny of American life in a way that was simply impossible before.”⁶⁵

Some would argue that delegation fosters good government, because it puts regulatory decisions in the hands of experts, and thus at some remove from the special interests that wield undo influence in legislative bodies. But both theory and observation suggest that concentrated interests are at least as well represented in regulatory as in legislative proceedings. Regulators are susceptible to “capture” by the industries, or elements of the industries, they regulate. Without question, the general public has less understanding of the regulatory process than it does of the legislative process, and less access to regulators than to legislators.

The telecom fiasco illustrates the power of special interests in regulatory proceedings. FCC’s forced access rules favor CLECs at the expense of ILECs. If required to vote on the issue, Congress might still have approved rules forcing incumbents to share their networks at drastically discounted prices—but then again, it might not have. ILECs could have put substantial pressure on Congress via political action committee spending, lobbying, and public outreach to reject the FCC’s proposals.

Because Congress delegates legislative power to agencies, it has little incentive to consider cost when drafting regulatory statutes, and almost none to insist that regulators develop economically sensible rules. Schoenbrod and Taylor explain:

Congress delegates power for much the same reason that Congress ran budget deficits for decades. With deficit spending, members of Congress can claim credit for the benefits of their expenditures yet escape blame for the costs. The public must pay ultimately, of course, but through taxes levied at some future time by some other officials....Just as deficit spending allows legislators to appear to deliver money to some people without taking it from others, delegation allows them to appear to deliver regulatory benefits without imposing regulatory costs.”⁶⁶

Elected officials not only escape blame for regulatory burdens, they have a positive incentive to create them. After all, the more expensive, convoluted, and litigious a regulatory program becomes, the more opportunities elected officials have “to do ‘casework’ on behalf of constituents beleaguered by the federal bureaucracy to which the legislators have delegated the hard choices.”⁶⁷ Casework generates campaign contributions and other forms of political support.

Only stale and dull habit prevents us today from seeing the enormity of this problem. Regulations are rules of conduct with the force and effect of law. Regulations are also implicit taxes, increasing the cost to consumers of goods

Because Congress delegates legislative power to agencies, it has little incentive to consider cost when drafting regulatory statutes.

and services. If asked whether bureaucrats should have the power to make laws and raise taxes, most Americans would unhesitatingly say no. Yet bureaucratic taxing and lawmaking has been a pervasive feature of American politics ever since the New Deal. Section VII of this report calls upon policymakers to end regulation without representation.

V. Previous Regulatory Reform Efforts

Previous regulatory reform initiatives seldom directly addressed the basic structural flaws of the regulatory state: the delegation of lawmaking power to politically unaccountable bureaucrats, and the absence of anything like a budget process for making explicit choices about overall regulatory costs and the allocation of scarce resources among regulatory objectives.

Most previous reform initiatives have sought to police agencies' actions. Such reforms typically have two components: (1) rules of rulemaking—the procedures agencies are to follow and the criteria rules are to meet—and (2) centralized review by OMB/OIRA to watchdog agencies' compliance with those procedures or criteria. Leading examples include the Paperwork Reduction Act, the Regulatory Flexibility Act, executive orders requiring cost-benefit analysis and centralized review, the Risk Assessment and Cost-Benefit Act, the Regulatory Improvement Act, and the Data Quality Act. Such reforms sometimes include judicial review provisions authorizing regulated parties to sue when agencies fail to perform the requisite analyses or follow the specified procedures.

In contrast, some initiatives aim to inject checks and balances into the regulatory process, either by increasing Congress's responsibility for regulatory decisions, creating inter-agency competition, or fostering competition between agency experts and outside experts. Notable examples include certain provisions of the Unfunded Mandates Relief Act, elements of the Regulatory Flexibility Act as amended and strengthened by the Small Business Regulatory Enforcement Act and Executive Order 13272, the Mandates Information Act, the Congressional Review Act, and the Truth in Regulating Act.

Section V reviews major initiatives policymakers have proposed, adopted, or enacted during the past three decades.

A. Policing Reforms

1. Paperwork Reduction Act

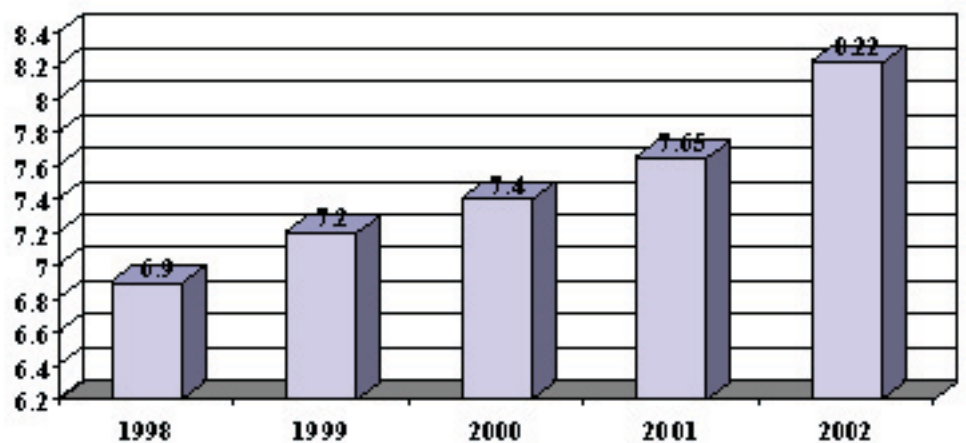
Since at least 1942, when Congress enacted the Federal Reports Act (FRA), reformers have sought to rein in federal paperwork burdens. The FRA required the Bureau of the Budget (which became the Office of Management and Budget, or OMB, in 1970) to review and approve each agency's information collection requests. In 1980, the Paperwork Reduction Act (PRA) replaced the FRA and established, within OMB,

Regulatory reform initiatives seldom directly addressed the basic structural flaws: the delegation of lawmaking power to unaccountable bureaucrats, and the absence of a budget process for making explicit choices about the size and distribution of regulatory burdens.

an Office of Information and Regulatory Affairs (OIRA), charged with minimizing paperwork.⁶⁸ The Act has been a persistent failure.

As OIRA's April 2001 (FY 2002) report to Congress acknowledged: "In most years since the PRA was first enacted in 1980, Congress has called on agencies to meet government-wide paperwork burden reduction goals of either five or ten percent. In all but one year, the Government did not meet the statutory goal. In fact, overall paperwork burdens on the public continue to increase each year."⁶⁹ For example, overall paperwork burden increased from 7.65 billion hours in 2001 to 8.22 billion in 2002, an increase of nearly 8 percent.⁷⁰

Figure 1. Federal Paperwork Burdens, FYs 1998-2002, Billions of Hours



Sources: OIRA, Managing Information Collection and Dissemination, reports for FYs 1999, 2000, 2001, 2002, and 2003, <http://www.whitehouse.gov/omb/infoereg/infocoll.html>.

In its defense, OIRA argues that most increases in paperwork burden are driven by statutory changes beyond its or the agencies' control. OIRA Administrator John D. Graham notes that, in the 15 years following the 1986 Tax Code revision, Congress passed 84 tax laws. "These laws required IRS to create and/or revise reporting and record-keeping requirements, which in turn increased taxpayer burden."⁷¹ Even changes that reduce tax liability can increase reporting requirements, creating more paperwork.

Elected officials do, indeed, directly or indirectly cause most government burdens, including IRS regulations and the associated paperwork. But this strengthens the case for increasing congressional responsibility for regulatory decisions. If Congress had to approve agency information collections before they become binding on the public, elected officials would face more public pressure to "scrap" the tax code and replace it with a simpler alternative.

2. Regulatory Accounting and Centralized Review

a. Presidential Initiatives

Since the early 1970s, every president has required agencies to undertake some form of regulatory accounting, and implemented some type of central review.⁷² In 1971, President Nixon established a Quality of Life Review program,⁷³ which became the foundation for all later presidential initiatives to institute and strengthen centralized review. Under this program, executive departments and independent agencies submitted drafts of all significant health, safety, and environmental rules to OMB, which then circulated them to other agencies for comment. In their submissions, agencies were to provide a summary of their proposals, including their principal objectives, the alternatives they considered, and a comparison of the expected benefits and costs of those alternatives. Agencies were also to submit a schedule showing estimated dates of proposed and final significant rules.

In 1974, President Ford created, within the Executive Office of the President, the Council on Wage and Price Stability (CWPS), to review regulations with potential inflationary impact. He also issued Executive Order 11821, which required agencies to prepare inflation impact statements before they adopt costly new rules.⁷⁴ Because CWPS believed that a rule would not be inflationary unless its cost exceeded its benefits, inflation impact statements developed into economic impact statements, i.e., cost-benefit analyses.

President Carter, also to combat inflation, created the Regulatory Analysis Review Group to review regulatory proposals. Carter championed several reform initiatives including the Paperwork Reduction Act (1980), which centralized review of agency information collection requests in OIRA, and laws deregulating the trucking, airline, and railroad industries.⁷⁵ In March 1978, Carter issued Executive Order 12044, requiring each non-independent agency to publish a semi-annual agenda of regulations to give the public adequate notice of planned regulatory actions, establish procedures for identifying which regulations are “significant,” and prepare analyses for rules with potentially major consequences for the economy, individual industries, and specific regions or levels of government.⁷⁶

President Reagan elevated the role of economics in regulatory oversight. Executive Order 12291, issued in February 1981, less than one month after Reagan took office, directed agencies, to the extent permitted by law, to refrain from issuing rules unless the “potential benefits to society...outweigh the costs,” to choose regulatory objectives that “maximize net benefits to society,” and to select the alternative approach to a given regulatory objective that involves “the least net cost to society.”⁷⁷ James Eads, the Chairman of Carter’s Regulatory Analysis Review Group, correctly notes that Reagan was the first president to establish a cost-benefit test for regulatory proposals:

Reagan was the first president to establish a cost-benefit test for regulatory proposals.

The Carter administration always took pains to stress that its requirements should not be interpreted as subjecting rules to a “cost-benefit test.” Instead, agencies were to identify costs and benefits, to quantify them insofar as possible, and either to choose cost-effective solutions *or* to explain why they had not. Moreover the burden of proving that proposed rules were not cost-effective lay not with the agencies but with senior White House officials...Reagan’s program goes much further. Except where expressly prohibited by law, the new executive order requires that a cost-benefit test be applied and met. An agency may not even propose regulatory action unless it can demonstrate that the potential benefits to society outweigh the potential costs.⁷⁸

E.O. 12291 also took centralized administration to a new level, designating OIRA as the body responsible for review, and requiring agencies to submit drafts of rules and cost-benefit analyses to OMB/OIRA for clearance. Eads describes the significance of this change:

The two Reagan executive orders were complementary, enabling OMB/OIRA to intervene at both ends of the rulemaking process and all points in-between.

Under Carter, the various oversight functions were parceled out among many offices. OMB monitored compliance with the regulatory analysis requirement and, beginning in late 1979, became increasingly important in monitoring regulatory paperwork as well. The Council on Wage and Price Stability (CWPS) and, in the case of particularly important regulations, the interagency Regulatory Analysis Review Group (RARG) maintained quality control of agency analysis by filings for the public record. The Regulatory Council compiled calendars of future proposed regulations, spotted and resolved regulatory conflicts, and encouraged the adoption of innovative regulatory techniques...The Reagan executive order consolidates most White House oversight functions in OMB’s Office of Information and Regulatory Affairs. In effect, OIRA has become the gate through which all-important regulations must pass—not just once, but twice—on their way to becoming law...It can overrule agency determinations on whether a proposed rule is to be considered “major”...If it finds the analysis weak or believes that important alternatives have been neglected, it can delay publication of the Notice of Proposed Rulemaking until the agency has adequately responded to its concerns.⁷⁹

Reagan’s Executive Order 12498, issued in 1985, established a process for developing and publishing an annual *Regulatory Program of the Administration*. E.O. 12498 directed agencies to prepare draft programs describing their planned regulatory actions for the coming year, required OMB to ensure the consistency of agencies’ draft programs with the administration’s policies and priorities, and tasked OMB to compile the final versions into an annual report. Except for rules responding to emergencies, the order prohibited agencies from taking regulatory actions not included in the *Regulatory Program*, unless approved by OMB.⁸⁰ The two Reagan executive orders were complementary, enabling OMB/OIRA to intervene at both ends of the rulemaking process and all points in-between. As Professor James Blumstein explains:

Whereas the centralized review process set up under Executive Order 12991 was retrospective, the regulatory planning process envisioned by Executive Order 12499 was prospective... The regulatory review procedures established under Executive Order 12991 typically reflected after-the-fact oversight by OMB. That type of ex post review maximized interagency conflict and, at the same time, constrained the ability of OMB to influence regulatory and deregulatory agendas “[t]o assure consistency with the goals of the administration.” In contrast, the regulatory planning process contemplated by Executive Order 12498 allowed OMB to exert its influence earlier in agency decision-making. It also provided an important vehicle for necessarily involving political appointees at the agencies in the process of developing a regulatory or deregulatory agenda within the agencies themselves.⁸¹

President George H.W. Bush continued the Reagan regulatory review program, although the action shifted from OIRA to the Council on Competitiveness, partly because Senator John Glenn (D-OH), Senate Governmental Affairs Chairman, would not allow a vote on the confirmation of James Blumstein, President Bush’s nominee to serve as OIRA administrator.⁸² The Council, created by Bush in March 1989 and chaired by Vice President Quayle, had a small staff and was able to review only a handful of rules in any given year. Partly for this reason (but also because of laws Bush signed, such as the 1990 Clean Air Act Amendments and the Americans with Disabilities Act), the total length of the *Federal Register*, after declining from an all-time high of 87,012 pages in President Carter’s last year to 53,376 pages in President Reagan’s last year, shot up to 67,716 pages in 1991.⁸³ Stung by criticism that he was a “re-regulator,” Bush in his 1992 State of the Union Address announced a 90-day regulatory moratorium, which he subsequently extended for an additional 120 days. During this period, federal agencies submitted regulatory proposals and cost estimates to the Council for review.⁸⁴

Assessments of the Council’s ability to shape regulatory outcomes vary. According to former EPA Administrator William Reilly, “the specific impact of the Competitiveness Council on [environmental] regulations... came down to two or three, not more.”⁸⁵ According to OMB Watch, on the other hand, the Council “interfered in, stalled, or killed dozens of regulatory programs.”⁸⁶ One fact is beyond dispute: the Council “did not keep records of discussions with lobbyists or of its own internal proceedings,” provoking criticism that it was subverting the public notice and comment process established by the Administrative Procedure Act (APA).⁸⁷

President Clinton abolished the Council upon taking office, and his Executive Order 12866,⁸⁸ issued in September 1993, required OIRA and the agencies to maintain public records of all communications with outside individuals or groups pertaining to rulemaking. It also established time limits for OIRA review and the resolution of inter-agency conflicts to prevent the review process from being used as a delay tactic.

Although Clinton's E.O. revoked both Reagan executive orders, it preserved intact the basic structures Reagan had put in place—both a forward-looking regulatory planning process and after-the-fact review of agencies' work products.

The “return letter” is an extremely popular tool until one has to take the responsibility for exercising it.

Although Clinton's E.O. revoked both Reagan executive orders, it preserved intact the basic structures Reagan had put in place—both a forward-looking regulatory planning process and after-the-fact review of agencies' work products. Indeed, according to Professor Elena Kagan, a former member of Clinton's White House domestic policy staff, “presidential control of administration, in critical respects, expanded dramatically during the Clinton years, making the regulatory activity of the executive branch agencies more and more an extension of the President's own policy and political agenda.”⁸⁹ Consistent with this interpretation, in ten places E.O. 12866 directs agencies to promote or ensure the consistency of their actions with “the President's priorities.”

However, Clinton's priorities arguably included launching a new era of regulatory activism. Significantly, although E.O. 12866 acknowledged the “legitimacy” of centralized review by OMB/OIRA, it “reaffirm[ed] the primacy of Federal agencies in the regulatory decision making process.” E.O. 12866 stipulated that the benefits of regulation should “justify” the costs—not “outweigh” the costs, as in Reagan's E.O. 12291. Perhaps most important, E.O. 12866 limited OMB/OIRA review to “economically significant” rules, a small subset of the 4,000-plus rules issued each year by federal agencies.

OIRA under Clinton reviewed less than half the number of rules it reviewed under Reagan. According to Clinton's OMB, reviewing fewer rules freed up limited staff resources to concentrate on significant agency actions, resulting in a “higher percentage of changes to the rules reviewed.”⁹⁰ Not all observers share this less-is-more interpretation. Regulatory analyst Steve Milloy warned during Clinton's first term that OMB had become a rubber stamp: “As of mid-1995, the number of regulations issued by EPA that were reviewed by OMB under the Clinton Executive Order totaled 45 out of 510, and none of these 45 were returned by OMB to EPA for failure to comply with the Executive Order.”⁹¹ Five years later, former OIRA official and Heritage Foundation analyst Angela Antonelli similarly concluded that OMB's scaled back review program “allowed agencies to be increasingly slow, sloppy, and secretive about providing justification for their rules.”⁹² Current OIRA Director John Graham observed that, in the last three years of the Clinton Administration, OMB sent “exactly zero return letters to agencies for poor quality analysis.”⁹³

When Dr. Graham took office, he vowed to revive the return letter as a stick to prod agencies into compliance with presidential criteria for cost benefit analysis. However, the revival turned out to be short-lived. Richard Belzer, a former OIRA economist, observes:

It appears that the “return letter” is an extremely popular tool until one has to take the responsibility for exercising it. In 2001 the Administration signaled that, contrary to what it considered the overly tolerant approach of its predecessor, it intended to insist on high-quality regulatory analysis. Moreover, the Administration promised it would not shy away from

exercising its authority to return draft regulations if they were supported by inadequate or substandard analysis. By my count, OMB returned 16 draft regulations from July 1 through December 31, 2001. But OMB returned only five draft regulations in all of 2002 and just two more regulations in all of 2003. Yet there is no evidence of a quantum leap in the quality of agency analysis since 2001.⁹⁴

As of February 2005, OMB's Web site shows the following number of return letters: 14 in 2001, five in 2002, two in 2003, and one in 2004.⁹⁵

The spotty record of centralized review by OMB/OIRA is not hard to explain. As AEI-Brookings scholars Robert Hahn and Erin Layburn point out, the agency heads, the OMB director, and the OIRA administrator all work for the same administration and are appointed by the same president. No administration welcomes the airing of internal criticism or policy disputes. There is an inherent conflict between OMB/OIRA's duty to police agency actions and its interest in advancing the president's political and policy agendas.⁹⁶

b. Regulatory Right to Know Act

Congress, for its part, has directed OMB to report on the costs and benefits of federal rules since 1996, and made that requirement permanent when it enacted the Regulatory Right to Know Act (Section 624 of the Treasury and General Government Appropriations Act of 2001). The Act requires OMB, in an annual accounting statement and associated report, to estimate the costs and benefits of federal rules in the aggregate, by agency, by program, and by major rule. The report is also to include an analysis of federal regulatory impacts on lower level governments, small business, wages, and economic growth, and recommendations for reform.

While disclosure of such information is critical to sound decision-making, OMB's report has serious shortcomings (as noted earlier) and is quite useless either as an accounting statement or as a tool of regulatory cost control. A February 25, 2004 House Government Reform Committee hearing on OMB's 2004 draft report spotlighted several critical problems.

OMB's 2004 draft report estimates that major rules issued in 2003 "added \$1.6 billion to \$4.5 billion in annual benefits compared to \$1.9 billion in annual costs."⁹⁷ In other words, benefits could exceed costs by a factor of more than 2 to 1; but costs could also exceed benefits by \$300 million. This is guesstimating, not accounting. Moreover, OMB's numbers are based on individual agency estimates for only six major regulations out of a total of 37 reviewed by OMB. "These six comprise less than one percent of all the final rules that were established by the U.S. government during the preceding 12-month period," notes William Kovacs of the U.S. Chamber.⁹⁸ Even if the agency estimates for those six rules were accurate, the draft report would still provide a very incomplete picture of FY 2003 regulatory costs and benefits.

There is an inherent conflict between OMB/OIRA's duty to police agency actions and its interest in advancing the president's political and policy agendas.

The draft report estimates that total rules cleared by OMB during the 10-year period from October 1, 1993, to September 1, 2003 produced annual benefits ranging from \$62 billion to \$168 billion, with annual costs ranging from \$34 billion to \$39 billion.⁹⁹ However, neither OMB nor the agencies made any significant attempt to re-assess initial cost-benefit projections used to compute those figures. OMB's reported information "is not benchmarked against what actually occurred after the regulations were implemented."¹⁰⁰

OMB excludes cost and benefit estimates for all minor rules, yet some of these might have substantial impact. Agencies determine which rules are to be classified as major and thus merit a regulatory impact analysis under executive orders or UMRA. "How," asks Kovacs, "is the public to have any confidence in the assessed impacts? Are some agencies 'gaming' the system, for example, by purposely understating costs or benefits of proposed regulations to avoid having to perform a regulatory impact analysis?"¹⁰¹ As a case in point, he describes how EPA avoided UMRA's \$100 million trigger for a regulatory impact assessment by claiming its Total Maximum Daily Load Clean Water Act rule would cost no more than \$25 million annually.

The 2004 draft report acknowledges that agencies use "different methodologies and valuations in quantifying and monetizing" costs and benefits.¹⁰² But, this means that, "OMB finds itself in the difficult position of comparing apples and oranges, again making the public highly suspect of reported aggregated cost-benefit estimates."¹⁰³

As with previous editions, the draft 2004 report offers no independent assessment of the accuracy of agencies' cost and benefit assessments. "The reported benefits and costs are based on agency estimates, without independent verification or any assurance that assumptions and methods are consistent across programs and activities," notes Susan Dudley of the Mercatus Center. "There is little value added in simply compiling the unverified representations of agency management."¹⁰⁴ Indeed, argues economist Richard Belzer, OMB's aggregation of costs and benefits takes bad information and makes it worse:

If errors were random, estimates of aggregate costs and benefits might be highly imprecise but they would be unbiased. However, there is both persuasive theory and consistent evidence that agency cost estimates are biased downward and agency benefit estimates are biased upward. When OMB aggregates dozens of downwardly biased cost estimates and upwardly biased benefit estimates, the total cost of federal regulation is understated by a lot and the total benefit of federal regulation is overstated by a lot.¹⁰⁵

Belzer also notes that, "huge areas of formal regulation are missing" from OMB's 2004 draft report, such as rules issued by independent commissions exempt from OMB review, including the FCC, Securities and Exchange

OMB's aggregation of costs and benefits takes bad information and makes it worse.

Commission (SEC), and Federal Trade Commission (FTC). He observes: “For a number of years telecom regulation by the FCC may have been the hottest area of federal regulation measured in terms of the number of lobbyists and analysts making a living from it. OMB’s report discloses nothing significant about telecom regulation.”¹⁰⁶

Another problem is that “over 75 percent of the reported upper-bound benefits” in OMB’s aggregation “derive from reductions in exposure to one pollutant—particulate matter.”¹⁰⁷ Yet as OMB acknowledges, “the degree of uncertainty in benefit estimates for clean air rules is large.”¹⁰⁸

c. OMB Circular A-4

In September 2003, OMB published Circular A-4, an agency guidance document on best practices in regulatory analysis. OMB’s 2004 draft report says Circular A-4 will strengthen “the role of science, engineering, and economics in rulemaking,” fostering regulatory decisions that are more “competent,” “credible,” and “consistent.” The draft report further comments: “OMB expects that as more agencies adopt our recommended best practices, the costs and benefits we present in future reports will become more comparable across agencies and programs.”¹⁰⁹

However, it is difficult not to view these claims as the triumph of hope over experience. After all, Circular A-4 “refines” OMB’s best practices document of 1996, itself an effort to clarify E.O. 12866, issued in 1993.

For years, researchers have reported that agencies often fail to follow not only best practices of regulatory analysis but minimal standards. American Enterprise Institute scholar Robert Hahn and colleagues examined 72 final rules promulgated from 1996 through February 10, 1998, and found that agency analyses often lack critical information called for in Clinton’s E.O. 12866 as well as in OMB’s 1996 best practices guidelines:

The study of regulatory impact analyses shows that agencies only quantified net benefits—the dollar value of expected benefits minus expected costs—for 29 percent of forty-eight rules...The agencies also did not adequately evaluate alternatives to the proposed regulation, another element of the Executive Order. Agencies failed to discuss alternatives for 27 percent of the rules and quantified the costs and benefits for only 31 percent.¹¹⁰

GAO found similar deficiencies in economic analyses of 20 rules issued by five agencies (the Departments of Transportation and Agriculture, the Environmental Protection Agency, the Food and Drug Administration, and the Occupational Safety and Health Administration) between March 1996 and July 1997. Five of the 20 analyses did not discuss alternatives to the proposed regulatory action, five did not discuss uncertainty associated with the agencies’ estimates of benefits and/or costs, and only one of the 20 analyses received independent peer review.¹¹¹

For years, researchers have reported that agencies often fail to follow not only best practices of regulatory analysis but minimal standards.

More recently, Hahn and a co-author examined 55 regulatory impact analyses (RIAs) issued by EPA. They found that 21 percent of RIAs under Reagan and 26 percent under Clinton did not discuss any alternatives. Only 32 percent of RIAs under Reagan, 31 percent under Bush, and 9 percent under Clinton calculated the cost-effectiveness of proposed rules.¹¹²

According to OMB's 2004 draft report, six of the 12 economically significant social regulations OMB reviewed in FY 2003 "did not include monetized estimates for either costs or benefits."¹¹³ Independent agencies provided even less quantitative information: "only 1 of the 7 rules finalized by independent agencies reported monetized benefits." Moreover, "OMB does not know whether the rigor and the extent of the analyses conducted by the independent agencies are similar to those of the analyses performed by agencies subject to the Executive Order, since OMB does not review rules from independent agencies."¹¹⁴ As already noted, OMB does not audit or vouch for the accuracy of analyses subject to its review.

One conclusion emerges: agencies cannot simply be mandated or managed into providing competent, credible, and consistent analyses of regulatory costs and benefits.

In summary, despite three decades of executive oversight and eight years of congressionally mandated reports, regulatory accounting as practiced by federal agencies remains an unreliable and misleading enterprise. Absent a basic change in the incentives agencies face, it is difficult to believe that Circular A-4 will succeed where previous presidential directives and OMB guidance documents have failed.

To its credit, OMB has acknowledged from day one that its estimates of aggregate regulatory costs and benefits are not useful for making specific regulatory decisions or reforming regulatory programs.¹¹⁵ OMB's annual reports do not inform regulatory planning and development, and play no role in OIRA's review of agency actions. Apart from creating an annual occasion for policymakers to discuss regulatory costs, and for soliciting public nominations of specific rules to be modified or rescinded (see below), it is unclear what purpose the reports serve.

One conclusion emerges: agencies cannot simply be mandated or managed into providing competent, credible, and consistent analyses of regulatory costs and benefits. Belzer provides a useful explanation: Each agency has a virtual monopoly on regulatory analysis within its particular sphere of operation. That is, each agency largely gets to select the cost and benefit estimates that inform and justify its decisions. Monopoly, as both economic theory and history teach, produces high cost and poor quality. Section VII of this report discusses how to foster competition between agency experts and outside experts.

d. Public Nominations

The Regulatory Right to Know Act requires OMB to prepare an annual Report to Congress on the costs and benefits of regulations, including recommendations for reform. It is the regulated public, not the agencies, who are

most likely to know whether a specific rule is outmoded, convoluted, or excessive. Appropriately, since 1997, OMB's reports have invited the public to identify regulatory programs or program elements that are "inefficient, ineffective, or...not a sound use of the Nation's resources."¹¹⁶ Under President Bush, OMB organized an administration-wide effort to "take a second look at a limited number" of existing regulations based partly on public nominations of rules to be rescinded or modified.¹¹⁷

OMB's draft 2001 report requested nominations of specific rules "that if rescinded or changed would increase public welfare by either reducing costs or increasing benefits."¹¹⁸ OMB received 71 suggestions from 33 commentators for reforming rules issued by 17 agencies. Of these nominations, OIRA selected 23 as high priority review candidates and directed the relevant agencies to consider them. As of November 2004, agencies had taken "at least some action (e.g., a proposed or final rule) on 17 (or nearly 75%) of these reform nominations."¹¹⁹

In 2002, OMB again requested reform nominations, and expanded the review program to include guidance documents and paperwork requirements as well as rules. OMB received 316 distinct recommendations from more than 1,700 commentators, and referred 156 reform suggestions to agencies for their consideration. OMB's preliminary analysis indicates that agencies have taken action on approximately 55 (about 35 percent) of these nominations. In 2003, OMB did not solicit reform nominations because it wanted to concentrate on upgrading OIRA's regulatory analysis guidelines and publishing Circular A-4. In February 2004, OMB once again requested nominations, but with a new emphasis on regulations, guidance documents, and paperwork requirements affecting the U.S. manufacturing sector. OMB received 189 distinct nominations from 41 commentators, and is still evaluating which to recommend for agency action.¹²⁰

The public nomination process is a worthy endeavor but should be seen for what it is: a weak substitute for the systematic, periodic reviews of existing regulations called for in both President Clinton's Executive Order 12866, *Regulatory Planning and Review*, and the Regulatory Flexibility Act.

Section 5 of E.O 12866 requires each agency to implement a program under which it "will periodically review its existing significant regulations to determine whether any such regulations should be modified or eliminated."¹²¹ Section 610 of the RFA requires each agency to publish annually in the *Federal Register* a "plan for the periodic review of the rules issued by the agency which have or will have a significant economic impact upon a substantial number of small entities." Pre-existing rules are to be reviewed within 10 years of the law's enactment (i.e., January 1, 1991), and new rules are to be reviewed within 10 years of the date they became effective.¹²²

However, as William Kovacs of the U.S. Chamber points out, these requirements have largely been honored in the breach. For example, "nearly all of the items listed in the spring 2004 edition of the *Unified Agenda of Federal Regulatory and Deregulatory Actions*...involve new regulatory proposals, and the Unified Agenda does not even list existing regulations subject to review under Section 5 of Executive Order 12866."¹²³

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Similarly, both GAO and SBA's Office of Advocacy have found that agencies seldom heed the RFA Section 610 look-back requirements.¹²⁴ OIRA Administrator John Graham similarly observes that most of the major or economically significant rules OMB reviewed prior to publication "have never been evaluated to determine whether they have worked as intended and what their actual costs and benefits have been."¹²⁵

Section VII of this paper outlines both a modest proposal to enhance the "public nominations" process and a more far-reaching reform to prune back the mass of existing regulation.

3. Risk Assessment and Cost-Benefit Act

In 1994, Republican candidates for the House signed a Contract with America,¹²⁶ pledging if elected to support an extensive legislative agenda, including several regulatory reform proposals. When Republicans took control in the 104th Congress, the House quickly and by a wide margin passed the Risk Assessment and Cost-Benefit Act of 1995 (H.R. 1022). It was the most comprehensive policing bill either chamber of Congress has ever passed.

The reformers sought to rectify what they regarded as the excesses of the past. Several statutes seemed to require or at least encourage agencies to set up health-at-any-cost¹²⁷ regulatory schemes. Leading examples included Occupational Safety and Health Act provisions dealing with toxic materials and harmful physical agents, the Superfund hazardous waste cleanup program, the Clean Air Act's national ambient air quality standards program, and the Delaney Clause of the Federal Food, Drug, and Cosmetic Act. The reformers wanted agencies to have to demonstrate that the benefits of regulatory proposals justify the costs.

Section 6(b)(5) of the Occupational Safety and Health Act requires OSHA, when it promulgates occupational safety and health standards dealing with toxic materials or harmful physical agents, to set the standard "which most adequately assures, to the extent feasible" that no employee will suffer material impairment of health. According to the Supreme Court, this language means that OSHA "is not required to determine that the costs of the standard bear a reasonable relationship to its benefits," only that regulated entities are technologically and financially capable of achieving the standard.¹²⁸

Superfund is notorious for requiring firms and municipalities to spend millions of dollars removing chemicals from contaminated soils without any measurable public health benefit. EPA has mandated expensive remediation plans based on absurd risk assumptions. For example, EPA risk assessments have assumed that people will build homes on top of known hazardous waste sites, drink well water even though they have access to the municipal water system, and consume significant quantities of contaminants daily by eating home grown produce even in areas with short growing seasons.¹²⁹ In some cases, the same

degree of public health protection achieved by cleaning contaminated soil could be obtained at far less expense by paving over the site or surrounding it with a chain link fence and posting a warning sign. The millions of dollars local governments spend on gold-plated Superfund cleanups cannot be used to address more urgent risks such as crime, fire hazards, and traffic accidents.

Section 109(b)(1) of the Clean Air Act directs the EPA to set primary ambient air quality standards “the attainment and maintenance of which...are requisite to protect the public health...with an adequate margin of safety.” In 1980, the District of Columbia Circuit, in *Lead Industries Assn., Inc. v. EPA*, held that “economic considerations [may] play no part in the promulgation of ambient air quality standards under Section 109,” and that EPA may not consider “any factor other than health effects relating to pollutants in the air.” On February 27, 2001, the Supreme Court upheld that decision in *Whitman v. American Trucking Associations, Inc.*, finding that the law “unambiguously bars cost considerations from the NAAQS-setting process.”¹³⁰

The Delaney Clause (Section 409 of the Federal Food Drug and Cosmetic Act) states that no food additive shall “be deemed safe if it is found to induce cancer when ingested by man or animal,” and directs the FDA not to approve such food additives, which include residues from pesticides. This zero risk standard disregards the first rule of toxicology—the dose makes the poison. Many chemicals that occur naturally in produce are carcinogenic if consumed in large enough quantities, and may be more potent than the trace residues of synthetic pesticides.¹³¹

As scientists developed techniques to measure trace chemicals in parts per billion and even parts per trillion, the Delaney Clause operated as a ban on the use of many pesticides even though the cancer risks were negligible or based solely on animal tests of questionable relevance to humans. Banning such pesticides, however, could increase food prices substantially and harm public health by discouraging low-income households from buying fruits and vegetables.¹³² (In 1996, Congress repealed the Delaney Clause when it enacted the Food Quality Protection Act. The Act allows the FDA to approve a pesticide, despite being linked to cancer at high consumption levels, if there is “reasonable certainty that no harm will result from aggregate exposure to the pesticide chemical residue.”¹³³)

The reformers’ argument for requiring regulators to achieve some balance between benefits and costs may be summarized as follows. The resources available to protect public health, safety, and the environment are finite. Consequently, policymakers should set priorities to target limited resources on the most serious risks. Moreover, because people use income to enhance their health and safety, regulations that destroy jobs, lower wages, and increase the cost of consumer products can literally be lethal. Spare-no-expense health and safety regulations ignore the obvious connection between livelihoods, living standards, and life spans.¹³⁴

To force regulators to set priorities, H.R. 1022 would require agencies to conduct a risk assessment¹³⁵ of the hazard to be addressed, compare those risks with other more familiar hazards (such as the probability of getting cancer from smoking), and use

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risk assessment to inform analyses of benefits and costs. Risk assessments were to include best estimates of the likelihood of exposure to harmful substances to discourage agencies from regulating on the basis of implausible maximum exposure scenarios.

To force regulators to economize, the bill required each (non-independent) agency to conduct a cost-benefit analysis for each major rule,¹³⁶ certify that the incremental benefits of any strategy chosen would likely justify, and be reasonably related to, the incremental costs, and certify that other alternatives would be less cost effective, or provide less flexibility to regulated entities, in achieving the regulation's purpose.

As an additional precaution against biased rulemaking, the bill required each agency head to develop "a systematic program for independent and external peer review" of agency analyses.

Most critically, the bill contained a Supermandate provision whereby its analytical requirements would "supercede" any conflicting provisions of current law and be subject to judicial review under a substantial-evidence standard. This was an ambitious reform agenda. As Steve Milloy explained at the time:

Even such current statutes as Superfund, the Clean Air Act, the Clean Water Act and other health, safety, and environmental statutes have no requirement that the incremental benefits of regulations justify the incremental costs. The Supermandate would impose such a requirement on these statutes. Federal agency decisions would then be reviewed under a "substantial evidence" standard—that is, they would have to be supported by a significant body of evidence, though not necessarily by a preponderance of evidence. The substantial evidence standard is significantly more demanding than the more usual "arbitrary and capricious" standard of the APA [Administrative Procedure Act].¹³⁷

Ambitious though H.R. 1022 was, some reform advocates thought it did not go far enough. Sam Kazman, an attorney with the Competitive Enterprise Institute, argued that the bill should not let individual agencies run the peer review process, "because they will soon figure out ways to bend this to their advantage. Instead, it should be the job of OMB, whose function is to restrain agencies." Kazman also argued for a requirement that every regulation be shown to do more good than harm, i.e., produce a net benefit. If there were necessary exceptions to this net-benefit test, then Congress could re-enact them on a case-by-case basis. Finally, Kazman recommended that rules based on hypothetical threats to human health and safety should be supported by a preponderance of evidence. He explained: "If a rule is not based on direct or epidemiological evidence that the exposure levels at issue pose a risk to people, then it should not receive the deference that courts customarily give to agencies."¹³⁸

Self-styled public interest groups quickly mounted a coordinated campaign to kill the bill and any legislation resembling it. Denouncing the reform agenda as a “Contract on America,” they claimed that H.R. 1022 would gut public health protections and “roll back 25 years of environmental legislation.” Although they could not stop the House from passing H.R. 1022, they were able to stop the Senate from passing a weaker companion bill, S. 343, sponsored by Majority Leader Bob Dole (R-KS). S. 343 did not require agencies to provide best estimates of risk, contained no Supermandate provision imposing cost-benefit and risk-assessment requirements on rules promulgated under laws lacking such criteria, and required judicial review under the substantial evidence standard only if “otherwise provided by law.”

Despite the changes Dole made to the House version, opponents filibustered S. 343, and after three unsuccessful attempts to end debate by cloture, Dole declared the bill dead for the year and never reintroduced it.¹³⁹ The attack on the Contract was so successful that “regulatory reform” became a tainted phrase. The experience of the 104th Congress left no doubt about one thing: numerous advocacy groups will mobilize every available resource to block any serious effort to police the regulators.

4. Regulatory Improvement Act

In the 105th and 106th Congresses, reformers regrouped behind the Regulatory Improvement Act, sponsored by Senators Carl Levin (D-MI) and Fred Thompson (R-TN).¹⁴⁰ This bill provided for cost-benefit analysis based on risk assessment, peer review, and judicial review of agency analyses. However, similar to Dole’s S. 343, the Regulatory Improvement Act contained no Supermandate provision, did not subject agency analyses to separate judicial review, and allowed courts to overturn a rule only if it was “arbitrary, capricious, an abuse of discretion, or is unsupported by substantial evidence where that standard is otherwise provided by law.” Levin-Thompson was a top priority for the business community, and twice appeared on the Senate’s legislative calendar. However, the bill never came to a vote.

Groups like OMB Watch attacked the bill’s cost-benefit provisions as inconsistent with Congress’s intent, embodied in portions of the Clean Air Act and other statutes, that agencies adopt the most protective standard, not the least costly or the most cost effective. They claimed the bill’s risk assessment provisions would force agencies to conduct time-consuming analyses even in cases where Congress had already determined the need for action. They warned that the bill’s peer review program would give industry experts undue influence, and that its judicial review provisions, although carefully couched, would nonetheless place more costly rules, even those required by statute, in legal jeopardy.¹⁴¹

On the other hand, limited government advocates such as Angela Antonelli warned that Levin-Thompson’s “procedural hoops” would not constrain agency decisions in any meaningful way. The bill’s analytic requirements would not apply to rules issued by independent regulatory commissions. The bill would let agencies decide what constitutes “a reasonable number of regulatory alternatives reflecting the

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Although the public paid for the research, agencies would not disclose the underlying data, preventing full public scrutiny of regulatory proposals.

range of regulatory options.” As long as agencies offered an explanation, they would remain free to select options likely to have greater cost than benefit, and to reject options likely to be more cost-effective or achieve greater net benefit. Agencies could evade all the Levin-Thompson requirements simply by breaking up major rule proposals into smaller rulemakings.¹⁴²

The failure of the Levin-Thompson bill again demonstrates the power of advocacy groups to scuttle policing reforms. Such groups will denounce any dilution of regulatory stringency, however modest or ineffectual, as an attack on public health, safety, and environmental protection.

5. Information Quality Laws

a. Data Access Act

When Congress amended the PRA in 1995, it not only set specific statutory goals for paperwork reduction, it also added new provisions governing agencies’ dissemination of information.¹⁴³ Among other purposes, the provisions aimed to “improve the quality and use of Federal information to strengthen decision making, accountability, and openness in Government and society,” and “ensure access to information.” However, the PRA’s dissemination requirements had little effect on agency practices. Agencies frequently contracted out rulemaking analyses to private organizations using proprietary models and data. Although the public paid for the research, agencies would not disclose the underlying data, preventing full public scrutiny of regulatory proposals. This practice became controversial when, in 1996-1998, EPA, on the basis of proprietary data, promulgated and defended costly new standards for fine particles measuring 2.5 microns or less (PM_{2.5}).

Congress responded by enacting, as part of the FY 1999 Omnibus Appropriations Act (P.L. 105-277), an amendment sponsored by Sen. Richard Shelby (R-AL), commonly known as the Data Access Act. Shelby’s two-line amendment directed OMB to revise Circular A-110, which governs federal contracting with institutions of higher learning, hospitals, and other non-profit organizations, “to require Federal awarding agencies to ensure that all data produced under an award will be made available to the public through the procedures established under the Freedom of Information Act.” OMB published the revised version of Circular A-110 in September 1999,¹⁴⁴ and issued a final rule interpreting the Circular and implementing the Act on October 8, 1999.¹⁴⁵

Whether or not the Data Access Act ends the use of “secret science” in regulation remains to be seen. OMB’s final rule states that the revised Circular will apply only to “awards issued after the effective date [November 8, 1999] and those continuing awards which are renewed after the effective date.” The rule would thus seem to deny the public access to data underpinning most of the regulations now on the books. A recent judicial decision, *Salt Institute and the U.S. Chamber of Commerce v. Tommy G. Thompson*, confirms this interpretation.

On November 15, 2004, the U.S. District Court for the Eastern District of Virginia dismissed a lawsuit by the Salt Institute and the U.S. Chamber of Commerce seeking judicial review of alleged violations of the Data Access and Information Quality Acts by the National Heart, Lung and Blood Institute (NHLBI) of the Department of Health and Human Services. Plaintiffs argued that NHLBI had violated the Data Access Act by failing to disclose the data underlying an NHLBI-funded study recommending that people lower their salt intake to reduce the risk of hypertension. Plaintiffs also argued that NHLBI violated the Information Quality Act by disseminating the results of the study on its Web site. The Court concluded that plaintiffs lacked legal standing to sue under the Data Access Act, in part because NHLBI initially funded the study through grants awarded in February 1997, prior to the regulation’s effective date.¹⁴⁶ The Court also held that the Information Quality Act provided no mechanism for judicial review of information quality.¹⁴⁷

There are other reasons to doubt the efficacy of the Data Access Act. OMB’s rule implementing the Act requires an agency to share its rulemaking data only after it “publicly and officially cites to the research findings in support of a regulation (for which notice and comment is required under 5 U.S.C. 533).” Since most public comment periods extend for 30 to 60 days, the public in most cases would have only one or two months to obtain and evaluate the underlying data before the comment period ends—insufficient time for thorough reanalysis of the supporting technical studies.

OMB’s implementing rule also holds that research data subject to FOIA “do not include... Trade secrets, commercial information, materials necessary to be held confidential by a researcher until publication of their results in a peer-reviewed journal, or information which may be copyrighted or patented.” Agencies may be able to exempt key data from public access on the grounds that releasing the information would harm a researcher’s commercial interests or violate an author’s agreement with a publisher.

b. Information Quality Act

Secret science is a subset of a larger problem: agencies’ use of biased information to rationalize predetermined policy preferences and agendas. Critics viewed EPA’s new air quality standards for fine particulate matter (PM_{2.5}) as a high water mark of agenda-driven science.¹⁴⁸ Some linked agencies’ co-mingling of policy biases with science to courts’ customary deference to agency expertise. In general, judges are unwilling to second-guess an agency’s use of data, models, or analyses, and will not reverse an agency’s decision just because they would have drawn different policy conclusions from the same (or better) evidence.¹⁴⁹

To address the agency bias problem, Congress enacted Section 515 of the FY 2001 Consolidated Appropriations Act (P.L. 106-554), popularly known as the Information Quality Act (IQA). This law directed OMB to issue government-wide guidelines, and each agency to issue agency-specific guidelines, establishing standards

OMB’s final rule would seem to deny the public access to data underpinning most of the regulations now on the books.

and procedures to improve the quality of agency-disseminated information. In OMB's guidelines, objectivity (lack of bias in presentation and content) is the leading element in the overall definition of quality, which also includes utility (value to users) and integrity (security from tampering).¹⁵⁰ The IQA also required OMB and the agencies to establish "administrative mechanisms" whereby "affected persons" can petition agencies to correct erroneous information.

In theory, the IQA puts citizens and agencies on a more level playing field. It provides a means for affected persons to correct agency biases without having to go to court. And if an agency refuses to correct faulty information or modify a regulatory proposal accordingly, courts should be more likely to review and reverse the agency's action—or so proponents hoped.

Whether or not the IQA actually improves information quality remains to be seen. The Center for Regulatory Effectiveness (CRE), a consulting firm that led the fight for the IQA, found that many agencies' draft guidelines would dilute—or even exempt regulators from—the law's requirements.¹⁵¹ The final guidelines plugged some of the holes, but still interpret the Act as essentially unenforceable—again confirming how difficult it is to police the regulators.

None of the agencies' final guidelines acknowledges that the guidelines are legally binding,¹⁵² and several expressly state that the guidelines are not binding and/or create no right of judicial review.¹⁵³

The final guidelines of at least 11 agencies assert a legal right to disseminate biased and erroneous information.

For example, EPA's final guidelines "provide non-binding procedural and policy guidance, and are therefore not intended to create legal rights, impose legally binding requirements or obligations on EPA...or change or impact the status of information we disseminate..."¹⁵⁴ Similarly, the Department of Labor's final guidelines are only intended to improve "internal management," "are not intended to impose any binding requirements or obligations on DOL," and "are not intended to provide any right to judicial review."¹⁵⁵ In effect, the final guidelines of at least 11 agencies assert a legal right to disseminate biased and erroneous information.

EPA's final guidelines also state that the IQA error correction process does not apply to rulemaking information. Any alleged errors in the rulemaking record are to be addressed solely through the notice and comment process.¹⁵⁶ EPA's interpretation would make the law weak precisely where its sponsors wanted it to be strong. If the notice and comment process were sufficient to identify and correct erroneous information in a timely fashion, there would be little need for an Information Quality Act. If citizens cannot use the IQA to correct faulty rulemaking information, its contribution to regulatory discipline will be marginal at best.

OMB has neither affirmed nor denied that agencies' IQA guidelines are legally binding and can be enforced via judicial review.¹⁵⁷ However, in June 2004, a federal district court in Minnesota ruled that the IQA "does not provide for a

private cause of action,” arguing that the law fails to define the relevant terms: quality, objectivity, utility, and integrity.¹⁵⁸ Alas, this is tantamount to saying that objectivity is in the eye of the beholder—presumably not what lawmakers intended when sought to ensure and maximize the objectivity of agency-disseminated information.

On June 25, 2004—four days after the Minnesota ruling—the Department of Justice (DOJ) filed a brief recommending dismissal of plaintiffs’ lawsuit in *Salt Institute and the U.S. Chamber of Commerce v. Tommy G. Thompson*.¹⁵⁹ DOJ argued, in pertinent part:

Plainly, nothing in the text of the statute indicates that Congress intended for the *federal courts* to serve as ongoing monitors of the “quality” of information maintained and disseminated by federal agencies. Rather, the language and structure of the IQA reflects Congress’s intent that any challenge to the quality of information disseminated by a federal agency should take place in administrative proceedings before federal agencies. Simply put, Congress nowhere provided a new judicial avenue for private parties to enforce the terms of the IQA.

On November 15, 2004, the U.S. District Court for the Eastern District of Virginia decided *Salt Institute* along the lines argued in DOJ’s brief. The Court held that, “Neither the Act itself nor its very limited judicial history provide a mechanism for judicial review of information quality or any avenue for judicial relief.” Although three other IQA lawsuits reportedly remain to be resolved,¹⁶⁰ at this point it looks doubtful that courts will agree to review the quality of information disseminated by federal agencies.

B. Checks and Balances Reforms

1. Unfunded Mandates Reform Act

During the early 1990s, state and local officials realized that federal mandates were overriding their priorities and commandeering their tax bases. According to a Price Waterhouse study at the time, mandates contained in just ten federal regulatory programs would, in 1994-1998, impose \$54 billion in costs on state and local taxpayers.¹⁶¹

Because of strong state and local government support, mandate reform was among the most popular elements of the Contract with America. In 1995, Congress passed and President Clinton signed the Unfunded Mandates Reform Act (UMRA). The Act:

- Requires agencies to prepare a cost-benefit assessment of any rule (subject to certain exceptions) that may result in the expenditure of \$100 million or more by either the private sector or state, local, and tribal governments.
- Requires the Congressional Budget Office (CBO) to determine whether

bills approved by authorizing committees contain mandates and, if so, whether the direct costs are \$50 million or more annually to lower-level governments or \$100 million or more annually to the private sector.

- Enables any member of Congress to raise a point of order against the consideration of legislation if it contains unfunded intergovernmental mandates exceeding \$50 million. The House or Senate would then have to debate the point of order and vote on whether to proceed with consideration of the bill.

What have been the results? UMRA has had a chilling effect on both the number and cost of unfunded mandates emanating from Congress.¹⁶²

- Of the more than 3,000 bills that CBO reviewed between 1996 and 2000, only 32 of the bills with intergovernmental mandates had annual costs of \$50 million or more. The percentage of bills with mandates exceeding the threshold declined from about 2 percent in 1996 to 1 percent in 2000.
- Similarly, bills with private sector mandates above the \$100 million threshold fell from 6 percent in 1996 to less than 1 percent in 2000.
- Only two intergovernmental mandates with annual costs above \$50 million became law—an increase in the minimum wage (in 1996) and a reduction in federal funding to administer the Food Stamp program (in 1997).
- Four intergovernmental mandates and five private-sector mandates that cost more than the threshold amounts when approved by their respective committees were amended before enactment to bring the costs below the thresholds.

On the other hand, apart from more frequent consultation with state and local governments, UMRA has had little effect on agency rulemaking practices, according to the General Accounting Office (GAO).

Title II of UMRA directs agencies to prepare a cost-benefit assessment of any rule likely to result in annual expenditures of \$100 million or more by lower-level governments or the private sector. However, the wording of Title II allows agencies to escape that requirement in most cases. First, agencies need not assess costs and benefits if a rule's requirements are specifically set forth in law. Second, agencies need not provide an assessment of a rule if they did not previously publish a notice of proposed rulemaking. Third, many economically significant rules do not fit UMRA's definition of mandate—an "enforceable duty" that is not "a condition of Federal assistance" or "a duty arising from participation in a voluntary Federal program." It is also worth noting that, by limiting the trigger for a cost-benefit assessment to mandates that "may result in the expenditure by State, local, or tribal governments, in the aggregate, or by the private sector, of \$100,000,000 or more (adjusted annually for inflation) in 1 year," UMRA covers

far fewer rules than are covered by either E.O. 12866 OMB reviews or the provisions of the Congressional Review Act applicable to major rules.

Because of these loopholes, GAO found that, during the first two years after the UMRA's enactment, agencies did not provide assessments for 78 of 110 economically significant rules they issued.¹⁶³ Also, as noted earlier, EPA evaded UMRA's analytical requirements by low-balling the costs of the Total Maximum Daily Load Clean Water Act rule. Although a "flagrant example" of such abuse, it is not unique.¹⁶⁴

In summary, UMRA does not apply to existing mandates, has less restraining effect on agencies than on Congress, and provides less protection to the private sector than to the public sector. It illustrates the importance of making elected officials take more responsibility for regulatory decisions.

2. Mandates Information Act

The House passed this bill (H.R. 350) in the 106th Congress. It would apply certain UMRA provisions to mandates on the private sector, such as rules affecting wages, consumer prices, or small business. The bill would require the Chair to rule on a point of order raised against measures that impose direct costs on the private sector of \$100 million or more. As with UMRA, if the Chair sustained the point of order, the House would then debate for an additional 20 minutes whether to proceed with consideration of the measure. In effect, Members would have an opportunity to affirm or deny that the benefits of the bill's private sector mandates justify the costs before voting on the bill itself.

Like UMRA, this approach would not necessarily stop any mandate. However, by enhancing accountability, it could decrease the number and cost of new private sector mandates.¹⁶⁵

3. Small Business Regulatory Relief

The Regulatory Flexibility Act of 1980 (RFA) was a classic attempt to police agencies via rules of rulemaking. It had little or no effect on regulatory outcomes. The small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA) and Executive Order 13272 strengthened the RFA. Together, these reforms enable one agency—the Small Business Administration (SBA)—to check and balance other agencies, at least to some degree. This change in institutional dynamics has made a real difference, sparing small businesses billions of dollars in unnecessary regulatory costs.

a. Regulatory Flexibility Act

Small firms typically face higher regulatory costs per employee and/or unit of production than do large firms, because the latter can spread the fixed costs of compliance over larger workforces and longer production runs. Large firms also devote more resources to lobbying Congress and agencies, and may support costly rules to restrict market entry by smaller rivals. Concerned that regulations of the one-size-fits-

all variety put small business at a disadvantage, Congress, in 1980, enacted the Regulatory Flexibility Act.¹⁶⁶

The RFA requires each agency to determine whether its proposed and final rules will have a “significant economic impact on a substantial number of small entities.” Unless the agency certifies that a proposed rule will not have such impact, and explains the reasons for such certification, it must prepare an initial regulatory flexibility analysis (IRFA) and publish it in the *Federal Register* for comment. When the agency issues a final rule, it must publish a final regulatory flexibility analysis (FRFA), unless, again, it certifies that the rule will not have significant small entity impacts, and explains the reasons for such certification.

Among other information, flexibility analyses must describe the steps the agency took to minimize small-firm compliance costs, discuss any significant alternatives that might accomplish the rule’s objective at less cost, and explain why the agency rejected those options. Alternatives agencies are to consider include delayed implementation schedules for small firms, performance standards instead of technology or industrial process specifications, and complete or partial exemption from the rule.

More often than not, the RFA was honored in the breach. Agencies paid little attention to small business concerns, in part because “there was no legal consequence for an agency’s failure to comply with the RFA, nor did small entities have a civil remedy to seek redress.”¹⁶⁷

b. Small Business Regulatory Enforcement Fairness Act

To strengthen the RFA, Congress, in 1996, enacted the Small Business Regulatory Enforcement Fairness Act. SBREFA authorized courts to review agencies’ compliance with the RFA, allowing small businesses to sue agencies for improper certification and failure to perform the requisite analyses. Equally important, SBREFA indirectly authorized SBA’s Office of Advocacy to file *amicus curiae* briefs on behalf of small business plaintiffs.

In addition, SBREFA required EPA and OSHA to convene small business advocacy panels to review regulatory proposals that may have a significant impact on a substantial number of small entities. The purpose of these SBREFA panels is to “ensure small business participation in the rule making process, to solicit comments, and to discuss less burdensome alternatives to the regulatory proposal.”¹⁶⁸ Panel members include small business representatives from the affected industries, officials from the rulemaking agency, OIRA, and SBA’s Office of Advocacy. Each SBREFA panel is required within 60 days after it convenes to prepare and submit a report on its findings to the agency head.

How effective has SBREFA been? GAO’s investigations show fairly pervasive agency noncompliance during the first three years after the law’s enactment. Like the RFA it amends, SBREFA allows agencies to exempt

themselves from the Act’s analytical requirements by certifying that a proposed rule will not have a “significant economic impact on a substantial number of small entities.” That is relatively easy to do because, as GAO observes, SBREFA does not define what Congress meant by “significant economic impact” and “substantial number of small entities.” In practice, agencies have had broad discretion to decide when the Act’s requirements do or do not apply.

For example, EPA proposed a rule in August 1999 to lower certain reporting thresholds for lead and lead compounds, under the Toxics Release Inventory program, from as high as 25,000 pounds to 10 pounds. EPA estimated that, in the first year, implementation of the rule would cost \$116 million, imposing costs between \$5,200 and \$7,500 apiece on 5,600 small businesses, or as much as \$42 million in all. EPA subsequently estimated that the proposed rule would affect more than 8,600 small companies, and GAO, using data from the Bureau of the Census, estimated that as many as 1,098 additional small manufacturing firms could be affected. Nonetheless, EPA certified that the rule would not have a significant impact on a substantial number of small entities, and so did not perform a regulatory flexibility analysis.¹⁶⁹

EPA’s questionable certification of the lead rule was not an isolated incident. According to GAO, in the two and a half years after SBREFA took effect, EPA certified that 96 percent of its proposed rules had no significant impact on small entities—up from 78 percent in the pre-SBREFA period. EPA’s Office of Prevention, Pesticides and Toxic Substances and Office of Solid Waste certified that all 47 of their proposed rules in the post-SBREFA period had no significant impact on small entities, while the Office of Air and Radiation certified that 97 percent of its proposed rules had no significant impact.¹⁷⁰

A 2001 CONSAD Research Corporation study, published by the Office of Advocacy, reported “substantial improvement” in agencies’ compliance with the RFA/SBREFA requirements for certification and explanation of rules not having significant impacts on a substantial number of small entities. CONSAD’s appraisal seems overly generous. “In 1995,” CONSAD reports, “about 39 percent of final rule notices failed to comply with either or both of these requirements. In 1999, the rate of noncompliance had been reduced to 32 percent.” CONSAD also found:

In 1995, only 55 percent of all IRFAs we reviewed satisfied all legal requirements of the RFA on a pro forma basis. In 1999, 64 percent of IRFAs satisfied these requirements. Similarly, in 1995, only 50 percent of all FRFAs met the legal requirements of the RFA. In 1999, 65 percent of FRFAs we reviewed met all the requirements of the RFA.¹⁷¹

Only in the bureaucratic (good-enough-for-government-work) sector are reductions in noncompliance with simple legal requirements from 39 percent to 32 percent, or from 50 percent to 35 percent, hailed as “substantial improvement.” Note also that CONSAD does not vouch for the quality of any of the agency analyses that meet the law’s pro forma requirements.

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SBREFA's judicial review provisions are less useful in practice than they appear to be on paper, because most small firms typically cannot afford to sue a federal agency. Under the Equal Access to Justice Act (EAJA), as amended by SBREFA, a successful small business plaintiff can recoup up to \$125 per hour for his legal expenses. However, as one congressional witness remarked, that is "what one pays a plumber to come fix a leak on Saturday"—it does not come close to reimbursing a small business owner for his time and out-of-pocket costs. SBA's Office of Advocacy notes that, "EAJA's rate cap is the exception rather than the norm amongst fee-shifting statutes [i.e., statutes that authorize winning plaintiffs to recover attorneys fees from defendants], and awards under alternative fee-shifting statutes can be significantly higher." Advocacy goes on to observe that, "The EAJA rate cap can result in fees that are well below market rate in many markets, preventing adequate reimbursement of attorneys fees to eligible parties, and discouraging competent counsel from undertaking meritorious cases on a contingency or reduced-fee basis."¹⁷²

EAJA's "substantial justification" standard also deters small businesses from seeking legal redress. Under this standard, a winning plaintiff is not entitled to recover attorney fees if a court determines that the agency's underlying conduct and posture in the litigation are substantially justified, i.e. have a "reasonable basis both in law and fact." Since there is no methodology for distinguishing reasonable from unreasonable actions, the substantial justification standard makes fee recovery something of a crapshoot even when the plaintiff has a strong case. Advocacy, quoting two law journal articles, explains:

"[A]n indispensable attribute of any fee incentive is that a party must be able to judge at the outset of the litigation the likelihood of a fee award upon prevailing." However, a standard of reasonableness, "by its very nature...demands application on a case-by-case basis," making it virtually impossible to evaluate the likelihood of a fee award at the outset of the litigation.¹⁷³

In a recent decision, *Buckhannon Board and Home Care, Inc. v. West Virginia Dept. of Health and Human Resources* 121 S. Ct. 1835, 1838 (2001), the Supreme Court further reduced the ability of small plaintiffs to recover fees. *Buckhannon* invalidated the long-standing "catalyst theory," under which a litigant qualifies as "prevailing," and thus is entitled to a fee award, if the lawsuit prompts the government to change its conduct or policy, whether or not the dispute is ultimately adjudicated by a court.

Since the goal of the EAJA is to encourage small entities to challenge and deter regulatory abuse, it stands to reason that, "a party should be entitled to a fee award under EAJA when litigation serves as a 'catalyst' for voluntary government action that achieves the favorable result sought by the private litigant."¹⁷⁴ The Court's interpretation undermines the EAJA, because it provides an easy way for agencies to sidestep the obligation to pay plaintiff's legal fees.¹⁷⁵ As Justice

Ginsburg said in her dissent, *Buckhannon* “allows a defendant to escape a statutory obligation to pay a plaintiff’s counsel fees, even though the suit’s merit led the defendant to abandon the fray, to switch rather than fight on, to accord plaintiff sooner rather than later the principal redress sought in the complaint.”¹⁷⁶

SBREFA’s judicial review provisions are also vitiated by the fact that winning plaintiffs receive no compensation for damages caused by an illegal rule. The only payoff is to have forced the agency to obey the law—a benefit shared equally by all other firms, whether they joined the suit or not.¹⁷⁷ For a small business, even winning a SBREFA case may be a losing proposition.

c. Executive Order 13272

To further strengthen the RFA, President Bush, on August 13, 2002, issued Executive Order 13272, “Proper Consideration of Small Entities in Rulemaking.” The E.O. requires agencies to notify the Office of Advocacy of draft rules expected to have a significant impact on small entities, and to consider Advocacy’s comments and respond to them in the final rule. It also requires Advocacy to provide regular training to all rulemaking agencies on how to comply with the RFA.¹⁷⁸

How well has SBREFA supplemented by E.O. 13272 worked? Similar to GAO’s findings, Advocacy reports that, of the rules and draft regulatory proposals it reviewed in FY 2003, 32.0 percent had inadequate analysis of small entity impacts, 29.1 percent did not consider significant alternatives, 15.5 percent had inadequate or no IRFA, and 11.7 percent were improperly certified as having no significant impact. Evidently, OMB review and the threat of litigation for noncompliance often fail to keep agencies in line.

However, there is a bright side to the story. Advocacy not only found problems that slipped under OIRA’s radar, it also corrected many of them. According to Advocacy, the changes agencies made in their rules in response to its interventions in FY 2003 reduced small business regulatory costs by more \$6.3 billion in the first year and more than \$5.7 billion on an ongoing annual basis.¹⁷⁹ Similarly, Advocacy estimates that its interventions during FYs 1998-2001 helped save small entities “more than \$16.4 billion, or more than \$4.1 billion per year on average.”¹⁸⁰

Dismissing these figures as self-congratulatory PR would be unfair. Advocacy calculates the savings from rule modifications based on the agencies’ cost estimates of the unmodified rules, and if anything, agencies tend to underestimate regulatory costs. Also, Advocacy’s annual reports describe, in each case, what the rulemaking agency initially proposed and what changes were made as a result of Advocacy’s involvement.¹⁸¹ The supporting documentation is available on SBA’s Web site.¹⁸² One successful intervention in particular is worth mentioning. In FY 2003, Advocacy persuaded EPA to exclude three industrial sectors from a proposed Clean Water Act rule to control effluents from plants manufacturing metal products and machinery. This change will save small entities approximately \$1 billion annually.¹⁸³

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To be sure, the RFA-based reforms, at best, slow the rate of increase in small business regulatory costs; they do not roll back existing regulatory burdens. Nonetheless, Advocacy's achievements are significant, and derive from an important, albeit usually neglected, principle of regulatory reform: competition. Advocacy is more effective than OMB/OIRA in reviewing agency proposals. Why? Instead of attempting to manage the regulators, Advocacy competes with them. Advocacy offers critical analysis and policy alternatives, and does so on behalf of a constituency with an indefeasible interest in cost control. Advocacy provides partial relief from the monopoly each agency otherwise maintains over regulatory analysis and deliberation. The RFA-suite of reforms has injected a modicum of inter-agency checks and balances into the regulatory process.

Does SBA's Office of Advocacy provide a model for general regulatory reform? Small business has a special place in American political culture such that even the most zealous anti-market groups profess to be pro small business. The special standing of small business underpins the entire suite of RFA-related reforms. Big business enjoys no such place of honor, and its high-profile support ultimately proved a liability for the flagship regulatory reform bills of the 104th, 105th, and 106th Congresses. On the other hand, lawmakers on both sides of the aisle are concerned about job losses in the manufacturing sector. It is not inconceivable that Congress would support the creation, within the Department of Commerce, of an Advocacy-type office for manufacturing firms. Whether or not Advocacy can be replicated in other agencies, it illustrates the power of checks and balances to improve regulatory decisions.

4. Congressional Review Act

A portion of SBREFA called the Congressional Review Act (CRA) set up a procedure whereby Congress has the option to veto a final agency rule before it can take effect. The law requires agencies to submit final rules to Congress and the GAO. GAO is to prepare a report on each major rule to determine whether the agency has performed all statutorily required analyses, such as the initial and final regulatory flexibility analyses required by RFA/SBREFA, and the regulatory impact analyses required by UMRA. To block a rule, Congress has 60 legislative days in which to pass a joint resolution of disapproval. The resolution becomes law if the President signs it, or if Congress overrides a presidential veto.

In the seven years since its enactment, CRA has been mostly a toothless tiger. Congress has used the law's expedited procedures to veto only one regulation—OSHA's ergonomics rule.¹⁸⁴ The CRA's ineffectiveness is not surprising. The law imposes no obligation on Congress to review rules, and thus allows members to continue to avoid taking responsibility for regulatory decisions. Nonetheless, the CRA was something of a legislative milestone, because it at least paid lip service to the ideal of a politically accountable regulatory system.

5. Truth in Regulating Act

The Truth in Regulating Act (TIRA), signed into law by President Clinton in October 2000, provides that when a federal agency publishes an economically significant rule, a chairman or ranking member of a committee of jurisdiction may request GAO to review and publish a report on the rule within 180 days. GAO is to assess “the agency’s data, methodology, and assumptions used in developing the rule, and to explain how any strengths or weaknesses in those data, methodology, and assumptions support or detract from conclusions reached by the agency, and the implications of those strengths and weaknesses.”¹⁸⁵

TIRA is a scaled back version of earlier proposals¹⁸⁶ to create a Congressional Office of Regulatory Analysis (CORA)—a regulatory counterpart to the Congressional Budget Office (CBO). The broad intent of TIRA was to provide an independent assessment of agency cost-benefit analyses and, thereby, help Congress carry out its CRA responsibilities. TIRA authorized \$5.2 million, on a three-year pilot basis, to enhance GAO’s regulatory analysis capability. However, Congress did not appropriate any money to hire the personnel GAO would need. Consequently, the law has not been implemented, and its budgetary authority has expired.¹⁸⁷

The thinking behind TIRA was sound—Congress needs a more extensive regulatory analysis capability to effectively check and balance both OIRA and the rulemaking agencies. On May 18, 2004, the House, by a vote of 373-54, passed H.R. 2432, the Paperwork and Regulatory Improvements Act. Section 5 of this bill would make permanent Congress’s authority to request regulatory analyses from GAO.

C. Implications of Previous Reform Efforts

Forcing agencies to meet high standards of regulatory analysis and data quality is much easier on paper than it is in practice. Even when rules of rulemaking are subject to both OMB and judicial review, they may have little real effect on regulatory outcomes, because agencies quickly learn to game most procedural requirements and turn them to their advantage.

Congress—not OMB or the judiciary—controls agencies’ budgets and authorizations. Therefore, reformers’ should strive to increase Congress’s responsibility for regulatory decisions. Agencies will be more likely to respect rules of rulemaking if Congress has to approve regulations before they go into effect. By the same token, Congress will be more likely to make agencies toe the mark if members are accountable to the electorate for agency actions.

However, congressional review can only be as good as the information on which it is based. Regulators may be able to manipulate Congress’s votes on final rules if agencies retain their monopoly power to determine which cost and benefit estimates receive U.S. Government approval.

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Because regulations derive from statutes, some regulatory programs cannot be set right unless Congress amends the underlying statutes.

Because regulations derive from statutes, some regulatory programs cannot be set right unless Congress amends the underlying statutes. For example, in theory, the FCC could adjust the price controls it has issued under the Telecommunications Act so that incumbent carriers are fully compensated when forced to share their facilities with rivals. But what's really needed is legislation that rapidly phases out forced-access regulation. That alone can restore property rights to the telecom industry and discourage creeping infrastructure socialism in other network industries.

The remainder of this report is organized as follows. Section VI outlines a legislative package to liberate America's IT sector from archaic and predatory regulation. Section VII discusses various options—near-term, mid-term, and long-term—to foster a more affordable, effective, and accountable regulatory system.

Due to the complexity and controversial character of the subject, the most far-reaching reform—regulatory budgeting—is discussed separately, in section VIII.

VI. DEREGULATE TELECOM

To rescue America's high-tech sector from regulatory excess, Congress will need to amend the Telecommunications Act, or replace it with a new law. A rational telecom law would do the following:¹⁸⁸

(1) Establish that the goal of the Act is to deregulate telecommunications. It was too easy for the FCC to institute a convoluted price control scheme in the name of fostering competition. An explicit goal of deregulation—that is, a genuine end to price and entry controls—could in itself curb future regulatory excess.

(2) Set a clear federal sunset date for forced-access regulation, perhaps a year in the future. As long as “what's yours is mine,” telecom policy will impede innovation, discourage genuine facilities-based competition, and necessitate price controls.

(3) Set a clear federal schedule for rolling back regulatory price controls, perhaps two years in the future. Forced access at steeply discounted prices not only stifles investment by incumbent Bell companies and upstart local carriers, it also holds back cellular phone companies. Even wireless cannot compete with myriad subsidized entrants operating below cost.

(4) Acknowledge the reality of technological convergence. Various companies from formerly distinct industry sectors (telecom, cable, and wireless) increasingly attempt to provide similar types of service. This means that healthy competition need not entail any specific number of wireline phone companies in a given market. Competition—inter-modal if not always intra-modal—will happen if policymakers dismantle exclusive territorial franchises and other government-created monopoly privileges.¹⁸⁹

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(5) Establish regulatory parity for telephone, cable, and wireless carriers. This also follows from the reality of technological convergence. Multiple regulatory standards impede the development of full-service telecommunications companies, and unfairly treat equals unequally. It is critical, though, that policymakers establish a level playing field by “regulating down” rather than by “regulating up.” Thierer and Crews explain:

That is, to the extent the agency continues to place ground rules on the industry at all, it should consider borrowing a page from trade law by adopting the equivalent of a “most favored nation” (MFN) clause for telecommunications. In a nutshell, the policy would state: “Any communications carrier seeking to offer a new service or entering a new line of business should be regulated no more stringently than its least regulated competitor.”¹⁹⁰

(6) Prohibit state and local governments from balkanizing information networks and telecom markets. In many Information Age industries, especially banking, insurance, telecommunications, and e-commerce, markets are nationwide or international, not statewide. Congress should preempt most state and local regulation, just as it did when it deregulated airlines, trucking, and railroads.

VII. Regulatory Process Reforms

In addition to deregulating the telecom industry and fending off coerced sharing in other network industries, policymakers should increase cost disclosure, competition, and accountability in the rulemaking process generally. The following recommendations build on the lessons learned from past successes and failures, as discussed in section V.

A. Near-Term Options

1. Publish an Annual Regulatory Report Card

Citizens will have to become more aware of regulatory impacts before Congress has much incentive to constrain them. Although regulated entities feel the burdens they are under, regulatory costs are unbudgeted and largely invisible to the public. OMB produces an annual report on the costs and benefits of federal regulation, but, for the reasons discussed above, it is a deeply flawed product and provides no guidance to policymakers. More useful would be a concise summary of information that can provide a moving snapshot of regulatory trends.

There are several types of information OMB could and should publish—whether as part of the President’s budget, as a section of its annual report, or as a separate document—to make the scope and scale of regulation more visible. Wayne Crews of CEI has long recommended that OMB produce a simple Report Card, consolidating vast amounts of regulatory data already provided but scattered across government agencies. Of course, some of this information, such as cost-benefit estimates, may be

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of very poor quality. The subsection below on Mid-Term Options discusses how to improve regulatory analysis.

Featured items in a Report Card might include: total numbers of major and minor rules produced by each agency; estimated costs of economically significant or major rules; numbers of rules lacking cost estimates; the top rule-making agencies; numbers of rules that are discretionary versus required by statute or judicial decision; and, numbers of rules impacting small businesses and/or lower-level governments. Table 2 includes these and other examples:

Table 2. Regulatory Report Card
“Economically significant” rules and minor rules by department, agency and commission
Numbers/percentages impacting small business and lower-level governments
Numbers/percentages featuring numerical cost estimates
Tallies of existing cost estimates, with subtotals by agencies and grand total
Numbers/percentages lacking cost estimates
Short explanation of lack of cost estimates
Analysis of the <i>Federal Register</i>: Number of pages, proposed and final rule breakdowns by agency
Numbers of major rules reported on by the GAO in its database of reports on regulations
Most active rule-making agencies
Rules that are deregulatory rather than regulatory
Rules that affect internal agency procedures alone
Rollover: Number of rules new to the Unified Agenda; number that are carry-overs from previous years
Numbers/percentages of rules required by statute or judicial decision vs. agency discretionary rules
Rules for which weighing costs and benefits is statutorily prohibited
Percentages of rules reviewed by the OMB, and action taken

A Report Card would provide a range of relevant regulatory information without mandating that agencies undertake additional analyses, and without requiring OMB to redo the agencies’ work.

A Report Card would provide a range of relevant regulatory information without mandating that agencies undertake additional analyses, and without requiring OMB to redo the agencies’ work. It would, however, help expose the shortcomings in agency analyses. For example, the number and percentage of

each agency’s major rules lacking estimates can easily be tabulated and published. Cumulatively, years of reporting will help uncover agency attempts to circumvent regulatory disclosure. For example, a flurry of minor rules might indicate that major rules are being broken up to escape the economically significant (\$100 million-plus) classification.

Until 1993, OMB compiled and published summary information annually in the *Regulatory Program of the United States Government*, in an appendix titled “Annual Report on Executive Order 12291.” This report included comparisons of the most active rule-producing agencies, and provided analysis of numbers of pages and types of documents in the *Federal Register*. The report was abandoned when the Clinton administration revoked E.O. 12291 and reduced OMB’s oversight activity.

The report helped illustrate the scope of unbudgeted governance, if not in terms of actual regulatory costs, at least in terms of trends in numbers of rules at the agencies. The same or similar information could also be included in a Report Card. Table 3 provides an overview of charts and tables formerly compiled in the *Regulatory Program*.¹⁹¹

Table 3. Information Collected in the former <i>Regulatory Program of the U.S. Government</i>
Total number of OMB reviews of regulations, by agency; presented in number, and as a percentage of the total. The material was presented in pie charts and tables
Number of major (\$100 million-plus) and non-major rules, by agency
A chart comparing the major and non-major rules from current and previous years
A brief description of all major proposed and final rules
A chart on rules reviewed by OMB, broken down as follows: “Found consistent (with executive order principles) without change;” “Found consistent with change;” “Withdrawn by agency;” “Returned for reconsideration;” “Returned because sent to OMB improperly;” “Suspended;” “Emergency;” “Statutory or judicial deadline”
Several pages of detail on the actions taken on rules reviewed
Average review time
Rules exempted from review procedures
Numbers of <i>Federal Register</i> pages, current and prior years
Analysis of aggregate pages published in the <i>Federal Register</i> (total pages; average pages per month; percentage change year to year; percentage change from 1980 to present
A breakdown of overall proposed and final rule documents in the <i>Federal Register</i>

**Table 3. Information Collected in the former
Regulatory Program of the U.S. Government**

Analysis of aggregate final rule documents published in the *Federal Register* by number and percent. These were broken down into New requirement; Revision to existing requirement; Elimination of existing requirement; and Other

Number of final rule documents by agency

Congress and the interested public would be able to see, for example, whether the number of rules affecting small businesses and localities is going up or going down.

Even without new cost estimation requirements, an official Report Card would help reveal regulatory trends, especially if supplemented with easy-to-read historical tables. 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, the minimum cost of recently adopted major rules, and whether regulatory activity at the top rule-making agencies is primarily driven by statute or agency initiative.

2. Create New Categories of Major Rules

The “major” or “economically significant” threshold merely specifies a *minimum* level of burden, revealing only that a rule costs \$100 million or more—but it doesn’t say *how much* more. For example, EPA’s entry in the 2003 *Unified Agenda of Regulatory and Deregulatory Actions* lists 22 economically significant rules in various stages of development.¹⁹² Those 22 rules will cost at least \$2.2 billion, but that is all one can tell without combing through the agency’s cost analyses.

OMB (or Congress) could easily require the use of additional categories in official publications to better portray the full range of regulatory burden. Such information could be incorporated in the annual Regulatory Report Cards. Table 4 offers one suggested breakdown of high-cost regulations by category.

Table 4. Breakdown of Economically Significant Rules

Category 1	>\$100 million, <\$500 million
Category 2	> \$500 million, < \$1 billion
Category 3	> \$1 billion
Category 4	> \$5 billion
Category 5	>\$10 billion

By assigning rules to categories, the economically significant designation would carry more meaning than it currently does. For example, EPA estimates that its new rule to reduce air emissions from non-road, locomotive, and marine diesel engines will cost \$1.5 billion in 2013.¹⁹³ In this case, describing the rule as a

Category 3 regulation would be more informative shorthand than merely knowing that the rule was economically significant.

3. Extend OMB Review to Independent Agency Rulemakings

“In comparison to the agencies subject to E.O. 12866,” observes OMB, “the independent agencies provided relatively little quantitative information on the costs and benefits of major rules.” For example, in the period from October 1, 2001 to September 30, 2002, the FCC did not include cost or benefit estimates in any of the four major rules it issued. The Securities and Exchange Commission (SEC), on the other hand, included cost estimates in all three of the major rules it issued, and benefits estimates in one of those rules. However, OMB cannot vouch for the “rigor” and “extent” of SEC’s benefit-cost analyses, “because OMB does not review rules from independent agencies.”¹⁹⁴

Given the potentially devastating impacts of ill-designed economic rules (the FCC’s forced-access regulations being a prime example), a strong case can be made for extending OMB review to independent agency rulemakings.

The type of review contemplated here would be strictly advisory, and thus would not compromise the independence of the independent agencies, nor require legislation to implement. The independent agencies would be legally free to disregard OMB’s recommendations, but they would risk public disapprobation for ignoring good advice, failing to address reasonable criticism, or refusing to correct material errors. This reform has the potential both to increase the quality of regulatory information available to policymakers and the public, and to foster healthy inter-agency competition.

The Center for Regulatory Effectiveness has identified several statutory provisions that enable OMB “to review and/or offer input on independent agencies’ regulatory activities.”¹⁹⁵

- **Paperwork Reduction Act.** This Act applies to independent agencies. OMB clearance is required for agencies’ information collection requests, and since most independent agency rulemakings contain information collection requirements, OMB has an opportunity to review those rules during the PRA process. PRA review provides OMB with a mechanism to submit views on the rules in which independent agencies’ information collection requests are embedded.¹⁹⁶
- **Information Quality Act.** The Act provides no exemption for independent agencies. OMB is responsible for monitoring the number, nature, and resolution of information correction petitions under each agency’s data quality guidelines. The IQA provides another mechanism for OMB assessment of independent agency rulemakings, “because proposed rules constitute disseminations of information to the public under the statute.”¹⁹⁷

Several statutory provisions enable OMB to review and/or offer input on independent agencies’ regulatory activities.

- **Regulatory Flexibility Act.** The RFA applies to independent agencies, which accordingly must publish initial and final regulatory flexibility analyses in the *Federal Register* when they propose and issue rules expected to have a significant impact on a substantial number of small entities. “Like any other public commenter, OMB has an opportunity to review and offer input on independent agencies’ analyses related to the RFA... This will permit OMB to discuss the costs, benefits, and other substantive issues under the rule, to the extent they impact small entities.”¹⁹⁸
- **Regulatory Right to Know Act.** The Act requires OMB, in an annual report and accounting statement, to estimate the total costs and benefits of federal rules and paperwork, to the extent feasible, in the aggregate, by agency, and agency program, and by major rule. Usually, OMB summarizes without evaluating what little information independent agencies have provided to GAO about the costs and benefits of their economically significant rules. However, nothing in the legislation prevents OMB from conducting its own analysis of independent agency rules and including the results in its report.¹⁹⁹

To sum up, OMB should revamp its review process to offer public comment on key rulemakings by independent agencies.

4. Make the Rule Reform Nominations Process More Transparent

At a recent hearing on the Bush Administration’s regulatory reform record, both William Kovacs of the U.S. Chamber and Thomas Sullivan of SBA’s Office of Advocacy testified that the regulatory reform nominations process is not transparent and informative enough to ensure the regulated community’s effective participation. “Small business stakeholders have told us that they become frustrated when follow-up information about the progress (or lack of progress) on a reform is not provided to the public,” Sullivan stated.²⁰⁰ Kovacs noted that the update OMB provided on the 2001 “high priority” nominations in its final 2003 report was more than a year old, “making it useless to rely upon and no doubt leading to duplicate nominations of the same regulations in succeeding years.”

Compounding the problem, OMB’s update included “only a few brief sentences about each nomination, making it difficult to know how the nominations are being reviewed, what transpired in the review process, or where things stand with respect to completion of the process.” Information OMB provided about the active 2002 nominations “suffers from the same drawbacks, and... OMB has not yet posted a list of the manufacturing-related nominations submitted in 2004.” In the summer of 2004, the U.S. Chamber contacted all the nominators of the 2001 and 2002 active nominations and requested a status report on their nominations. “While some of the nominators were familiar with

their nominations, many did not know what had been done with them and were, not surprisingly, frustrated with the entire process.”²⁰¹

Kovacs offers a common-sense plan to remedy these defects: “OMB should post all of the nominations it receives on its Web site, and provide timely status reports about them. Further, any items slated for action by OMB, or by an agency, also should be posted in the Unified Agenda, with a hyperlink to the OMB Web site list.”²⁰²

5. Uphold Information Quality Standards

For the IQA to be an effective check on agenda-driven science, the Act’s petition correction process must be applicable to rulemaking records, and agency responses to information correction petitions must be subject to judicial review. Whether or not the Act grows real teeth or becomes another paper tiger will probably be decided in the courts. In the meantime, OMB should press the agencies to comply with information quality standards.

Unfortunately, in a recent case, the Bush administration refused to apply quality standards to influential documents disseminated by federal agencies. Despite several actions taken by CEI pursuant to the IQA correction process, EPA and the White House Office of Science and Technology Policy continue to disseminate the Clinton administration’s report, *U.S. National Assessment of the Potential Consequences of Climate Variability and Change*, a work of dubious scientific value.

The *National Assessment* relied on two outlier climate models—the “hottest” and “wettest” out of some 26 models available to the Clinton team. Worse, as University of Virginia climatologist Patrick Michaels discovered, and National Oceanic and Atmospheric Administration scientist Thomas Karl confirmed, the two underlying models—British and Canadian—could not replicate past U.S. temperature trends regardless of the averaging period used—one-year, five-years, 10-years, or 25-years.²⁰³ Models that cannot hind-cast past climate cannot be trusted to forecast future climate. Both biased and useless, the *National Assessment* flouts IQA standards of objectivity and utility.

In response to CEI’s petitions, the administration agreed to slap a caveat on the report, acknowledging that it “has not been subjected to” federal information quality standards. However, that does not satisfy the law’s requirements. The report should be “subjected to” the standards, and if it does not pass muster, agencies should cease disseminating it.

Apparently, Bush officials are unwilling to apply the IQA to the *National Assessment* because doing so would also discredit the administration’s *Climate Action Report 2002* (CAR), which incorporates the *National Assessment*’s scary climate impact scenarios. But in trying to avoid the embarrassment of disavowing its climate report, the Administration now risks the greater embarrassment of having to recant its climate policy.

Twelve state attorneys general, three cities, two island states, and several environmental groups are suing the Bush Administration because it refuses to regulate carbon dioxide as a pollutant under the Clean Air Act. The litigants repeatedly cite the CAR’s disaster scenarios as proof that Bush’s EPA has tacitly classified carbon dioxide as a pollutant endangering public health and welfare under the Clean Air Act.²⁰⁴ Repudiating the CAR on information quality grounds would demolish a key premise of the carbon dioxide litigation. Yet the Administration has gone to great lengths to shield the CAR from information quality review. As a consequence, it could end up both gutting the IQA and losing the carbon dioxide litigation.²⁰⁵

6. Small Business Regulatory Enforcement Act: Clarify Key Terms and Strengthen Private Cause of Action

As discussed earlier, agencies wiggle out of SBREFA’s analytical requirements by picking their own definitions of “significant impact” and “substantial number of small entities.” Moreover, litigation costs discourage many small businesses from pursuing legal remedies for SBREFA violations.

The Administration has gone to great lengths to shield the CAR from information quality review. As a consequence, it could end up both gutting the IQA and losing the carbon dioxide litigation.

Congress should modify SBREFA so that it exerts more pressure on agencies to consider and reduce the impacts of rules on small business. Specifically, Congress should: (1) authorize SBA’s Office of Advocacy to define “significant impact” and “substantial number” via a notice-and-comment rulemaking;²⁰⁶ (2) require courts to accept SBREFA cases recommended by SBA’s Chief Counsel for Advocacy; and, (3) strengthen the ability of private parties to enforce the Act’s requirements.

To strengthen SBREFA’s judicial review provisions, Congress should:

- ***Eliminate the \$125 per hour rate cap on the award of attorney fees and tie awards to market rates.*** This will make the Equal Access to Justice Act equal to other fee-shifting statutes. “More importantly, allowing recovery in amounts that more accurately reflect existing market rates will ensure that eligible parties are able to obtain competent counsel, and that they are adequately reimbursed for litigation costs.”²⁰⁷
- ***Eliminate courts’ discretion to deny attorney fees to winning plaintiffs on the grounds that the agency’s action was “substantially justified.”*** The substantial justification standard makes it almost impossible for plaintiffs to predict whether they will recover attorney fees no matter how strong their case. Automatic fee shifting for prevailing parties—an entitlement for winning plaintiffs to collect attorney fees from agency defendants—“would significantly enhance EAJA’s predictability and boost incentives” for small entities to challenge defective rulemakings.²⁰⁸

➤ **Reinstate the “catalyst theory.”** The Supreme Court’s *Buckhannon* decision allows agencies to sidestep the obligation to pay attorney fees “by abandoning its position whenever faced with the probability of losing its case.”²⁰⁹ Congress should intervene legislatively to overturn *Buckhannon*. It should amend the EAJA to define “prevailing party” to include plaintiffs who substantially cause an agency to provide relief whether or not the issue is adjudicated by a court.

➤ **Award damages to winning plaintiffs for costs incurred as a result of unlawful regulation.** Mere recovery of legal expenses is probably not incentive enough for small firms to sue agencies—nor is it adequate as a matter of simple justice.

David Burton of the Argus Group proposes a bolder fix for SBREFA’s judicial review provisions. In addition to the foregoing options, he recommends authorizing lawyers to sue agencies on behalf of small businesses *as a class*, and to collect contingency fees enhanced by a percentage of the overall damage awards. Class action lawsuits “allowing lodestar awards and contingency enhancements” would “dramatically encourage the plaintiffs’ bar to bring tort actions” on behalf of small firms abused by regulatory agencies.²¹⁰ This is a bold plan. Whether or how such a litigation regime might advance or hinder tort reform is an important issue, but one that is beyond the scope of this paper.

7. Unfunded Mandates Relief Act—Shrink Regulatory Impact Assessment Loopholes

As mentioned earlier, UMRA requires agencies to prepare a regulatory impact assessment (RIA) before publishing any notice of proposed rulemaking (NPRM) and before issuing any final rule preceded by an NPRM. By implication, agencies can avoid assessing a final rule’s impacts by not publishing an NPRM.

In some cases—for example, emergency situations—not publishing an NPRM may be appropriate. Accordingly, the Administrative Procedure Act (APA) provides a “good cause” exception whereby agencies may bypass the usual notice-and-comment process if adherence to it would be “impracticable, unnecessary, or contrary to the public interest.” When agencies use the good cause exception, they are to say so explicitly in the final rule and provide an explanation. However, the explanations are not always adequate, as GAO documents:

For example, in one such case, the agency said it was using the good cause exception because the rule would “facilitate tourist and business travel to Slovenia,” and therefore delaying the rule to allow for public comments “would be contrary to the public interest.” In another case, the agency said that soliciting public comment was “contrary to the public interest” because the rule authorized a “new and creative method of financing the development of public housing.”²¹¹

It is important for Congress and the public to understand the costs of high-impact rules, regardless of whether the basic requirements are discretionary or set forth in law.

As GAO notes, when agencies bypass the notice-and-comment process, they not only limit public participation in rulemaking, they also dodge “several of the regulatory reform requirements that Congress has enacted during the past 20 years that use as their trigger the publication of an NPRM.”

Two minor amendments to UMRA would shrink the NPRM loophole. First, when an agency decides to use the good cause exception, it should have to publish an explanation in the *Federal Register* at least 30 days before it issues the final rule, and invite public comment; it should not be allowed to wait until promulgation to present its rationale. Second, if the rule is likely to impose costs of \$50 million or more on lower-level governments or \$100 million or more on the private sector, agencies should still be required to publish an RIA in the *Federal Register* no later than 60 days after issuance of the final rule, and invite public comment.

UMRA also exempts agencies from the obligation to perform an RIA if the rule’s requirements are specifically set forth in law. This exemption should also be rescinded. It is important for Congress—and the public—to understand the impacts of high-cost rules, regardless of whether the basic requirements are discretionary or set forth in law.

B. Mid-Term Options

1. Make Agencies Compete for the Right to Score Regulatory Impacts

As noted earlier, the Regulatory Flexibility Act (RFA), as amended and strengthened by the Small Business Regulatory Enforcement Fairness Act (SBREFA) and President Bush’s E.O. 13272, has had some success in reining in agency discretion and small business regulatory costs by empowering one agency—SBA’s Office of Advocacy—to compete with other agencies in the rulemaking process. Reformers should now take the next logical step—make agency experts compete on a level playing field with outside experts from industry, the non-profit sector, and lower-level governments.

Although citizens are free to submit comments on regulatory proposals and even offer alternative cost-benefit estimates, it is the agencies that ultimately decide which estimates are best. Executive orders like E.O. 12866 and statutes like UMRA and SBREFA create a massive demand or *market* for regulatory analysis, but it is a market in which the agencies face no competition. The agencies’ exclusive right to score the impacts of regulatory proposals partly explains why existing procedural and analytical requirements are often ineffective. No matter how bad a job they do in estimating regulatory costs and benefits, agencies face no competitors who can take the business away from them.

Unless Congress dismantles the agencies’ monopoly power to pick which estimates of cost and benefits inform regulatory development, all other reforms

may be undermined, because the agencies will continue to be in a position to bias the estimates in their favor.

Agencies' monopoly power to score the costs and benefits of regulatory proposals presents a classic conflict of interest, because agencies have an obvious incentive to skew regulatory analyses to justify rules that expand the scale and scope of their power. As economists Randall Lutter and Richard Belzer point out:

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.²¹²

The EPA's October 1997 report to Congress, *The Benefits and Costs of the Clean Air Act, 1970-1990*, required by Section 812 of the Clean Air Act, epitomizes the self-promotional extravagance in which agencies, shielded from competition, are currently free to indulge. The report 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 assessment:

One such implication of EPA's estimate is that in 1990 the nation would be willing to pay 20 percent of 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 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.²¹³

A key question for policymakers, then, is how to subject agency analyses to a reality check. For many years, reformers have been calling for new and tougher peer-review procedures to improve the quality of regulatory analysis, and OMB recently proposed a government-wide program of peer review for “information that is relevant to regulatory policies.”²¹⁴ However, Belzer cautions, it is doubtful “whether agency-

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sponsored peer review would ever be adequately independent, or genuinely effective in improving quality as long as agencies retain the discretion to adopt or reject the advice they receive.” He elaborates:

Independence is inherently problematic when the sponsor of peer reviews selects the reviewers and writes the charge. An agency can delegate these tasks to a contractor (including the National Academies of Science), but contractors that do not please their clients tend not to be rehired.²¹⁵

A more effective approach, Belzer argues, is for Congress to remove the agencies’ control over what information is finalized and disseminated. “The Regulatory Right-to-Know Act,” he notes, “gives OMB the responsibility for informing Congress concerning the benefits and costs of federal regulation, but it doesn’t give OMB any statutory authority to determine whose estimates are most reliable.” Congress could remedy that asymmetry simply by authorizing OMB to make such determinations.

The agencies currently monopolize the power to score regulatory proposals, but they have no monopoly on regulatory expertise. Businesses, think tanks, universities, advocacy organizations, and state governments employ hundreds, perhaps thousands of competent professionals skilled in economic and scientific analysis. “Open the door to competition by creating a market for high-quality, policy-neutral, and independent regulatory analysis, and they will respond,” says Belzer. “The agencies also will respond—first by trying to undermine the legitimacy of their competitors, and once that fails to work, by improving the quality of their own work to avoid being driven out of the regulatory analysis business.”²¹⁶

Under Belzer’s proposal, OMB would invite the public to submit analyses of regulatory proposals, and then use a procedure known as “Final Offer Arbitration” (FOA) to select the best one. He explains:

A restricted form of FOA is used by Major League Baseball to decide whether the player’s or the team’s estimate of market value is most reasonable. Unlike other forms of arbitration, in FOA the arbitrator cannot negotiate amongst contending parties or devise face-saving compromises intended to ensure that everybody “wins.” Because arbitrators can easily and quickly discard extreme or flamboyant positions, FOA discourages competing parties from exaggerating the strengths of their own case and the weaknesses of the others’.²¹⁷

In other words, FOA is a winner-takes-all system. OMB would not be allowed to split the difference between, or combine elements of, competing analyses. OMB would have to select one analysis and reject the rest. This would put pressure on all contenders to avoid submitting analyses that contain unsubstantiated cost and benefit estimates, fail to examine reasonable alternatives, rely on implausible scenarios, or conceal critical uncertainties and assumptions.

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Thus, for example, to have a realistic chance of winning, EPA's analysis of a proposed environmental regulation would have to be at least as plausible as those submitted by experts in industry, the academy, think tanks, advocacy groups, and state-level agencies. At a minimum, EPA's analysis would have to conform to OMB's best practices and information quality guidelines.

Some might object that third parties should not prepare cost-benefit analyses, because rulemaking is an inherently governmental function. That objection is valid, however, "only if one believes that the purpose of regulatory analysis is not to inform decision making or the public, but to provide the legal or public justification for decisions that have already been made."²¹⁸ In other words, if performed by an outside party, the winning analysis should and presumably would inform further rule development, the final regulatory decision, and congressional review, but the agency would not be required to endorse the winning analysis or adopt it as its own.

Finally, some might object that authorizing OMB to determine whose analysis is best would simply transfer monopoly power from the agencies to OIRA, giving undue influence to the president or his appointees. That is a valid concern, but it is easily addressed. "If for whatever reason you do not have sufficient trust in OMB's judgment," says Belzer, "ask the General Accounting Office to evaluate the same information and reach its own conclusions. Even OMB can benefit from some competition."²¹⁹

2. Extend Unfunded Mandate Relief Act Protections to the Private Sector

UMRA has had a damping effect on Congress's propensity to impose new regulatory burdens on state, local, and tribal governments. The Act has been a real (albeit limited) success because it embodies the principles of cost disclosure (CBO analysis of regulatory mandates) and accountability (point of order provisions facilitating congressional debate on regulatory costs). Congress should extend to the private sector the protections UMRA provides to the public sector. In fact, UMRA tacitly provides some private sector protection already, because private firms and households ultimately pay for all regulation, including unfunded intergovernmental mandates, which result in higher taxes, fees, and property assessments.²²⁰

Just as any member of Congress can now force the House or the Senate to debate and vote on whether to consider measures that would cost lower-level governments \$50 million or more, so members should have the option to force Congress to debate and vote on whether to consider legislation containing \$50 million mandates on the private sector, or \$25 million mandates on small business.

3. Establish a Congressional Regulatory Office

To participate effectively in regulatory decisions, Congress needs its own independent expert analytic capability—a regulatory counterpart to CBO. Congress took a small step in that direction when it enacted the Truth in Regulating Act

(TIRA) in 2000. TIRA directed GAO to analyze major rules at the request of the committee of jurisdiction's chairman or ranking member, and authorized an additional \$5.2 million over three years to expand GAO's regulatory analysis capability. As mentioned earlier, Congress declined to appropriate any funds to make TIRA operational, but the House, on May 18, 2004, overwhelmingly approved H.R. 2432, which would "make permanent" the authority of committee chairmen and ranking members to commission GAO analyses of major rules.

The basic idea behind TIRA remains sound. GAO already provides valuable independent perspectives on agency actions.²²¹ In some cases, GAO investigations have "disclosed inadequate data, methodologies, or assumptions, and in others disclosed noncompliance with statutory requirements or executive orders." Some GAO reviews have shown that the applicable analytic requirements were "narrowly tailored and had little effect on rulemaking," and others have shown that some regulations "considered burdensome by the regulated community were required by the statute being implemented." This is exactly the kind of information Congress must have to begin taking responsibility for regulatory outcomes.

If adequately staffed and funded, GAO's regulatory division could help provide a reality check on agencies' analyses. That is critical, because OIRA is a watchdog in constant danger of becoming a rubber stamp. Ultimately, what's needed is a full-fledged Congressional Regulatory Office (CRO), which would foster a healthy ongoing competition between the agencies' experts and Congress's experts. As AEI-Brookings scholars Robert Hahn and Eric Layburn explain:

OIRA faces inherent limits in the scope of its review of individual regulatory proposals. The OIRA Administrator is nominated by the President, who also nominates the heads of the various regulatory agencies. Therefore, there is likely to be some implicit understanding that the head of OIRA is not to press the agencies excessively hard because he or she is part of the same Administration as the agency heads. The constraints on OMB are manifested in its annual report, in which it has, so far, simply accepted the benefit and cost estimates compiled by the agencies instead of providing any of its own assessments. A new office of regulatory analysis outside the executive branch would not have this conflict of interest and could more easily criticize the analysis done by federal regulatory agencies. Competition between agencies has the potential to enhance the analysis produced by OIRA and its independent competitor, much like competition between CBO and OMB has done in the budget arena.²²²

Opposition to a CRO may come from both sides of the political spectrum. Groups on the Left may oppose it, fearing it would increase the prominence of

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economics and cost considerations in regulatory decisions. Politicians on the Right may oppose it, fearing it would create “another layer of bureaucracy.”

On the other hand, the fact that Congress enacted TIRA by a voice vote and the House passed H.R. 2432 by an overwhelming majority demonstrates broad support for at least the rudiments of a CRO. Congress would at a minimum need to expand GAO’s regulatory program if, as recommended above, it opens the market for regulatory analysis and tasks GAO to compete with OMB in selecting the best analyses of new regulatory proposals.

C. Long-Term Options

1. Require Congressional Approval before New Rules Are Effective

Congress would have much greater motivation to consider economic impacts when drafting regulatory statutes, and to insist that agencies consider low-cost and non-regulatory alternatives, if it has to approve final agency rules before they can take effect.

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 a resolution of disapproval, opponents of the rule must then assemble super-majorities in both chambers to prevail. Under conditions of divided government, in which the party that controls Congress does not control the White House, enacting a CRA resolution of disapproval is nearly impossible.

What is needed is a mechanism that deters agencies from proposing exorbitant rules in the first place, not one that makes it almost impossible to stop rules after agencies have finalized them. The Congressional Responsibility Act (H.R. 110), sponsored by Rep. J.D. Hayworth (R-AZ), would promote compliance with Article I §1 of the U.S. Constitution, which vests “all legislative powers” in Congress. The Act would require Congress to approve final agency rules before they can become binding on the public. As with any other legislative action, the president could veto Congress’s approval of a regulation, and Congress, in turn, could override the president’s veto. Under this arrangement, a simple majority in either chamber could stop an ill-advised rule just by declining to vote for it. Instead of opponents having to organize legislative coalitions to block a rule, proponents would have to organize legislative coalitions to enact a rule.

A 1999 Competitive Enterprise Institute survey found that 76 percent of Americans “agree that Congress should be required to approve regulations written by federal bureaucrats and administrators before they take effect.”²²³

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“No regulation without representation” clearly echoes the words and philosophy of those who signed the Declaration of Independence.

Such a plan is indeed more radical than most other regulatory reform proposals, but its radicalism lies in its fidelity to American principles of self-government. “No regulation without representation” clearly echoes the words and philosophy of those who signed the Declaration of Independence. No other regulatory reform proposal has as great a potential appeal to common-sense populism. Regulations are implicit taxes that have the force of law. To most Americans, it is obvious that nobody but their elected representatives should have the power to make laws or raise taxes.

An accountability regime would work best if combined with a system of competitive regulatory analysis. As long as agencies get to select which cost and benefit estimates inform decision-making or the public, they have the power to bias public discussion in their favor and manipulate congressional review.

Once the debate on regulatory reform is reframed as a debate on congressional reform, defenders of the status quo should find themselves at a disadvantage. After all, how many members of Congress will want to defend the proposition that they should continue to exercise “power without responsibility”? And how many public interest groups will want to defend the proposition that voters should have no one to hold accountable for regulatory decisions? How many will want to vouch for the moral and constitutional legitimacy of regulation without representation? Paradoxically, this bold reform proposal may ultimately be the most politically attractive.

a. Is Regulatory Accountability Feasible?

Status quo defenders may object that Congress could not manage the increased workload if it had to approve 4,000-plus new regulations ever year. Because there are only so many hours in a legislative session, a Congress constrained to debate and vote on agency rulemakings would very likely pass fewer laws and more carefully consider the regulatory provisions of laws it does pass. However, to those who think America suffers from a surfeit rather than a dearth of laws and regulations, the prospect of gaining a more deliberative Congress is an additional reason to support an accountability regime.

Be that as it may, there are various ways Congress could streamline a regulatory review process to ensure that it does not crowd out other essential business. Congress could limit the time allotted to debate individual rules, and limit the types of rules eligible to be debated. 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. Administrative and other non-controversial rules could be bundled together and approved by a voice vote.

Congress could also implement an accountability regime in phases. This would allow for trial-and-error learning, and ensure manageable workloads in the early stages. For example, in the first two years, Congress would only review

economically significant rules—those likely to “have an annual effect on the economy of \$100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities.”²²⁴

A little-known, twice-yearly publication called the *Unified Agenda of Federal Regulatory and Deregulatory Actions* depicts the total number of proposed and final federal rules on which action is anticipated within 12 months. The *Agenda* also presents actions recently completed, as well as a handful of regulations planned for the long term. The *Agenda* is a rough gauge of what is in the regulatory pipeline.

The Fall 2003 edition shows a total number of 127 economically significant regulations in various stages of development, including 22 “completed” actions.²²⁵ Congress unquestionably could review 22 or even several dozen economically significant final rules per year without shortchanging other important business.

Under one possible incremental regime, OMB would transmit final economically significant rules to the relevant congressional committees, which would have the option—and incentive—to conduct hearings and oversight. For example, EPA’s entry in the 2003 *Unified Agenda of Regulatory and Deregulatory Actions* lists 11 economically significant rules in the “final rule” stage.²²⁶ The Senate Environment and Public Works Committee could undeniably find the time to hold hearings on a dozen or so key environmental rules per year. After receiving an economically significant final rule from OMB, Congress would have a specified period of time, such as 60 legislative days, within which to consider and vote on the rule. Shorter time periods could be set for rules responding to emergency situations.

In later years, as Congress becomes more familiar with the process, the threshold for review could be lowered to include rules imposing \$50 million or more in costs on lower-level governments or the private sector, or \$25 million or more on small business. All other rules—about 97 percent of the total—could be handled through various expedited procedures.

Such a process would not guarantee the wisdom of any particular regulatory action. But, at least, Congress would take responsibility for regulations promulgated under the laws it enacts, the public would have someone to hold accountable at the ballot box for regulatory decisions, and agencies would be more careful to consider the costs imposed by their actions on the regulated public.

b. Is Regulatory Accountability Constitutional?

This question may seem odd, because ensuring the accountability of administrators to lawmakers, and of lawmakers to citizens is a central purpose of constitutional government. Also, as we have seen, the Constitution clearly vests “all legislative powers” in Congress, and nowhere authorizes Congress to delegate lawmaking authority to administrative agencies or regulatory commissions.

There are various ways Congress could streamline a regulatory review process to ensure that it does not crowd out other essential business.

Ensuring the accountability of administrators to lawmakers, and of lawmakers to citizens is a central purpose of constitutional government.

Nonetheless, the question is pertinent because the accountability regime outlined in this report is a type of legislative veto, and, according to the Supreme Court, not all legislative vetoes are constitutional.

Under a legislative veto, agency actions cannot go into effect, or remain in effect, unless Congress, or a part thereof, approves those actions, or does not disapprove them, within a specified time period.²²⁷ In *INS v. Chadha*, 462, U.S. 919 (1983), the Supreme Court overturned a provision of the Immigration and Nationality Act allowing the House of Representatives to veto an attorney general’s decision to suspend the deportation of aliens. In the process, the Court invalidated legislative veto provisions in hundreds of statutes enacted during the previous five decades. Is the legislative veto outlined in this report constitutional? Yes.

Chadha struck down a *unicameral* legislative veto—a provision authorizing the House, acting unilaterally, to overturn an otherwise lawful decision by an executive branch official. By implication, *Chadha* invalidated all similar provisions vesting veto authority in one chamber, a single committee, or an individual committee chairman.

Chadha’s argument may be summarized as follows. A legislative veto is a “legislative action.” As such, it must conform to the Constitution’s requirements for lawmaking. To make law, both the House and the Senate must pass a bill, they must then present the bill to the president for his approval or veto, and if he vetoes, two-thirds of both chambers must re-pass the bill. When the House vetoed the attorney general’s decision to suspend the deportation of an alien, Mr. Jagdish Chadha, it did not obtain the approval of the Senate, nor did it present its decision to the President for his review. The Immigration and Nationality Act’s veto provision violates the Article I §1 principle of “bicameralism” and the Article I §7 principle of “presentment” to the president. It is therefore unconstitutional.

The Court’s reasoning in *Chadha* poses no obstacle to the type of legislative veto outlined in this report. The bicameralism requirement is satisfied, because both houses would have to approve a regulation before it goes into effect. The presentment requirement is satisfied, because Congress would have to present a joint resolution to the president for his review.

c. Can Regulatory Accountability Restore Checks and Balances?

In his famous dissent, Justice Byron White argued that the Court’s reasoning in *Chadha* was inconsistent with the legal premises of the administrative state as it has evolved—premises the Court had repeatedly affirmed. Congress often delegates legislative power to executive and independent agencies, which routinely issue rules with the force of law. In fact, Congress has even delegated legislative power to farmers—a private interest group—authorizing them to propose and vote on agricultural commodity marketing and production restrictions

issued by the Department of Agriculture. The Court has upheld such unquestionably legislative actions, even though the House and the Senate did not vote on them, and even though the president had no opportunity to sign or veto them. *Chadha*'s reasoning "cannot be defended as consistent with the Court's view of the Article I presentment and bicameral commands."²²⁸

White did not consider the possibility that the earlier cases upholding bureaucratic and private lawmaking were wrongly decided. However, he implicitly affirmed the constitutional necessity for congressional review of agency actions. *Chadha*, he warned, would cripple Congress's ability to check and balance the administrative state:

The prominence of the legislative veto mechanism in our contemporary political system and its importance to Congress can hardly be overstated. It has become a central means by which Congress secures the accountability of legislative and independent agencies. Without the legislative veto, Congress is faced with a Hobson's choice: either to refrain from delegating the necessary authority, leaving itself with the hopeless task of writing laws with the requisite specificity to cover endless special circumstances across the entire political landscape, or in the alternative, to abdicate its law-making function to the executive branch and independent agencies. To choose the former leaves major national problems unresolved; to opt for the latter risks unaccountable policymaking by those not elected to fill that role.²²⁹

"Unaccountable policymaking by those not elected to fill that role" is a fundamental defect of the modern administrative state. However, that defect did not begin with *Chadha*, and *Chadha* has not had much effect on the way Congress operates. As constitutional historian Louis Fisher documents, Congress frequently ignores *Chadha* or improvises around it. In the 16 months between *Chadha* and the close of the 98th Congress on October 12, 1984, Congress enacted 53 new legislative vetoes, mainly of the unicameral and single committee variety. From the day *Chadha* was decided, on June 23, 1983, to the end of 1997, Congress enacted more than 400 new legislative vetoes.²³⁰ In addition, committee chairmen and agency heads reach informal understandings that function as de facto committee vetoes, "the only difference being that the congressional control is less public."²³¹ Notification requirements can also substitute for committee veto provisions, since few agency heads "will be willing to notify a committee, learn of its opposition, and proceed anyway."²³²

House and Senate rules provide another means of evading *Chadha*'s ban on unicameral and committee vetoes:

Each house can stipulate that no funds may be appropriated for a particular purpose unless the authorizing committee has granted its approval by committee resolution. Since this procedure concerns the internal workings of Congress, the "committee veto" is directed at the appropriations committee rather than at the executive branch. To that extent it should create no problem under *Chadha*, even

Justice White did not consider the possibility that the earlier Supreme Court cases upholding bureaucratic and private lawmaking were wrongly decided.

if this type of committee veto is the functional equivalent of the legislative veto declared invalid.²³³

What accounts for these evasions? *Chadha*, says Fisher, directs the political branches to follow an “impracticable and unworkable” lawmaking process:

Chadha has produced a “record of noncompliance, subtle evasion, and a system of lawmaking that is now more convoluted, cumbersome, and covert than before.”

Even with *Chadha*, the need for a quid pro quo between Congress and the executive branch remains. The conditions that spawned the legislative veto a half-century ago have not disappeared. Executive officials still want substantial latitude in administering delegated authority; legislators still insist on maintaining control without having to pass another law.²³⁴

Because *Chadha* effectively asks Congress to neglect a basic institutional interest and constitutional duty, the decision has produced a “record of noncompliance, subtle evasion, and a system of lawmaking that is now more convoluted, cumbersome, and covert than before. In many cases the Court’s decision simply drives underground a set of legislative and committee vetoes that had previously operated in plain sight.”²³⁵

Three questions—actually, three formulations of a single question—emerge from the foregoing discussion. Can Congress hold agencies accountable without resorting to covert practices that also weaken accountability to the public? Can Congress authorize agencies to develop rules, maintain control without having to amend the enabling statute, and respect the Article I requirements of bicameralism and presentment? Can Congress check and balance the regulatory agencies without putting new rents and tears in the constitutional fabric?

The answer to those questions is a resounding yes. Requiring Congress to approve final rules before they can go into effect, and to present joint resolutions of approval to the president for his signature or veto, would reconcile the practical necessity for bureaucratic rule development with Congress’s constitutional duty to make law. Indeed, Congress might allow administrators more discretion in crafting rules, if it were clear that no emerging regulatory proposal could go into effect until and unless Congress votes to enact it.

Ending regulation without representation would by definition bring agency actions into compliance with the Article I bicameralism and presentment principles, and would likely improve Congress’s compliance with *Chadha* as well. Congress would regularly deliberate on agency actions “in plain sight,” and presumably would have less need or justification to employ covert forms of the legislative veto. Indeed, Congress probably could not end bureaucratic lawmaking without advancing *Chadha*’s argument that all valid legislative actions must be approved by both chambers and presented to the president for his signature or veto.

d. Would Regulatory Accountability Impede Judicial Review?

Some policymakers worry that an accountability regime might preclude judicial review of agency rulemakings and preempt litigation to overturn or modify defective rules. New laws trump old laws. Consequently, these critics warn, if Congress enacts not only the regulatory statute but also the implementing rules, then any rule Congress approves must be legal even if the agency's rulemaking actions were arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.

This is a serious concern, and an accountability regime worthy of the name should include safeguards to ensure that congressional review does not end up legalizing agency lawlessness.

As a reasonable precaution, every joint resolution of approval should include a standard clause affirming the unqualified force and effect of all existing statutory criteria and requirements for rulemaking. Such a clause might read: "This joint resolution of approval shall not be construed as superceding or weakening any procedural or substantive requirements for rulemaking, whether set forth in the rule's governing statute, other federal laws, or judicial decisions; nor shall the resolution be construed as impairing any rights of private action or judicial review."

2. Establish a Bipartisan Regulatory Reduction Commission

The reforms discussed so far in this report apply mostly to new rules. Since agencies promulgate thousands of new rules each year, with many more regulatory than deregulatory actions, even a congressional accountability regime combined with competitive regulatory analysis would only slow the growth of new regulatory burdens, leaving the existing mass of regulations untouched.

As discussed earlier, Section 5 of E.O. 12866 and Section 610 of the RFA already require agencies to conduct periodic reviews of existing regulations and eliminate outmoded or inefficient rules, yet few rules are ever re-assessed. Two eminently doable measures, advocated by William Kovacs of the U.S. Chamber, would help rectify this situation.

- Congressional committees should put pressure on agencies under their jurisdiction to identify regulations due for a Section 610 review, notify Congress as to when the reviews will take place, and report to Congress the results of the reviews.
- The president should issue an executive order specifically requiring agencies to establish a program to review each economically significant rule it issues within 10 years of the rule's becoming effective. For each rule reviewed, the agency should determine "whether the initial cost and benefit forecasts were accurate, and assess the expected future costs and benefits of the rule, as well as feasible alternatives."²³⁶

Every joint resolution of approval should include a standard clause affirming the unqualified force and effect of all existing statutory criteria and requirements for rulemaking.

To reduce the mass of existing federal regulation, reformers must create a mechanism outside the agency-dominated rulemaking process.

Although these steps would be helpful, agencies will always prefer to look ahead rather than look back, and they will never be tough critics of their own handiwork. To reduce the mass of existing federal regulation, reformers must create a mechanism outside the agency-dominated rulemaking process.

A reasonable model for reviewing regulations already on the books is the military base closure and realignment process. Congress found that closing obsolete bases one at a time was politically impossible. It chose instead to close and consolidate bases via an up-or-down vote on a package of recommendations assembled by a bipartisan commission. Carrying the technique over to the regulatory arena, Congress should appoint a bipartisan Regulatory Reduction Commission to review agency regulations. The Commission would invite OMB, GAO, and the interested public to submit recommendations; hold hearings; and assemble a yearly package of proposed regulatory reductions. The package would be subject to an all-or-nothing vote, with no amendments allowed. Congress would send any package it approved to the president for his signature.

The process of holding hearings combined with the bundling of regulations from across the spectrum of government activity would make the Commission's recommendations difficult to oppose politically. As in the base closure model, everybody stands a good chance of getting "hit," but the Commission, not Congress, compiles the hit list. Thus, for members, the process provides political cover. The Commission could be kept active for as long as Congress deems necessary, and potentially could shave off large chunks of ineffective regulations over a number of years.

VIII. Regulatory Budgeting

Once Congress begins to take responsibility for regulatory decisions, it will face political pressures to limit the economic burdens regulations impose. Agencies, in turn, will be motivated to develop less costly rules in order to obtain congressional approval. That is desirable, because: (1) the resources available to protect public health and safety are limited; (2) regulations that reduce employment, incomes, and innovation can subtly but significantly harm public health and safety; and (3) agencies left to their own devices do not always select the most cost-effective alternatives.

As noted above, competitive regulatory analysis should inform congressional review. As long as agencies determine which cost and benefit estimates inform regulatory decisions, Congress may literally have no idea what it is voting on.

But is congressional review based on high-quality analysis an optimal accountability and cost control regime? Or should Congress in addition, place statutory limits on the costs agencies may impose the private sector and lower-level governments?

The ultimate goal of regulatory reform is to make regulators and legislators act more like households. However devoted to the health and safety of their members, households face inexorable tradeoffs in the use of their resources and, consequently, have strong incentives to set priorities and economize. For example, a single working mother may decide to keep her reasonably safe older vehicle rather than spend \$50,000 for the safest new car on the market, because doing so would mean she could not afford to purchase health insurance, save for her daughter's college tuition, or own a house in a "safe" neighborhood. She acts responsibly when she weighs and balances competing goals and does not indulge the fantasy that no expense is too high a price to pay for auto safety. Whether consciously or intuitively, the household budget guides and constrains her choices. A similar decision framework should—but does not—inform regulatory choices.

Because government appropriates other people's resources, its natural tendency is to spend as if the sky is the limit and money is no object. In the fiscal arena, the illusion of free money is tempered somewhat by a budget process that forces policymakers to consider the impacts of total taxes and spending on the economy, set spending targets for the government as a whole and its various components, and thus make tradeoffs among competing agencies and programs. What is most critically lacking in the regulatory arena is a budget mechanism forcing elected officials to make explicit choices about the size of regulatory burden in relation to the economy, and about the allocation of scarce resources among the myriad of regulatory objectives.

Congressional review informed by competent analysis is a consummation devoutly to be wished. Nonetheless, we would never accept such a regime as adequate for making tax and spending decisions. Consider the following thought experiment, suggested by former OMB economist Jim Tozzi:

In particular, suppose that individual agency budgets are subject to Congressional approval but that, in place of the overall budget for the Executive Branch, agencies are required to submit each of their programs to a rigorous cost-benefit analysis. Apart from other considerations, this system would have two major economic flaws. First, the costs or benefits of a program are sometimes dependent on features of another program, and these relationships could not be handled without moving away from the completely decentralized mechanism hypothesized. Second, the value of public goods [such as national defense, workplace safety, and environmental quality] is not revealed in any market, but must be established through the political process. The decentralized system assumed would not present the relevant choices [about alternate uses of the same resources] where a budget system can do so.²³⁷

In the fiscal arena, we do not ask Congress and the president to maximize the net benefit of each program one at a time, in isolation from decisions about other programs, and without regard to the effects of total spending on the economy. But that is roughly what the current regulatory system asks agencies to do—assure the wisdom

The ultimate goal of regulatory reform is to make regulators and legislators act more like households.

of each rule, considered one at a time, without regard to the impacts of other rules, or to the cumulative burden of all rules on the economy.

Regulatory costs are, in a word, *unbudgeted*. That is the central defect of the modern regulatory state, and it would persist even under a system of congressional review based on rigorous cost-benefit analysis. However, congressional review combined with competitive analysis could evolve into a *regulatory budget*—the capstone of regulatory reform in the opinion of several policy thinkers.²³⁸

A. What Is a Regulatory Budget and How Would It Work?

Although the details of regulatory budget proposals can be complex, the basic idea is simple. Under a regulatory budget, agencies would be required, in advance of proposing rules to meet a particular statutory objective, to obtain authority from Congress to spend private sector resources via regulation. Regulatory spending authority could be doled out by major rule, by regulatory program, by regulatory function, or by agency. For example, Congress could enact limits on compliance burdens resulting from (a) EPA’s non-road diesel engine rule, (b) all of EPA’s clean diesel programs, (c) all air quality regulations, or (d) all EPA rules. Conceivably, a regulatory budget could cover all compliance costs resulting from federally promulgated rules.

Presumably, the process for setting a regulatory budget would work much like the process for setting the fiscal budget. Each agency would estimate both the cost of its existing rules and the incremental costs of rules it plans to issue in the next fiscal year, and submit to OMB a request for authority commensurate with the estimated combined costs of its existing and planned rules. OMB along with the president and his aides would review the agencies’ requests, and make adjustments in light of the president’s priorities. Ideally, the president’s regulatory budget would propose caps not only for individual agencies and programs (or regulatory functions), but also for the government as a whole. The president would annually submit his regulatory budget, and Congress would make whatever modifications it desires. Congress would then pass the budget and send it to the president for his signature or veto.

Congressman Doug Ose (R-CA) and former OMB Director James Miller argue that the spending appropriations process provides a rough model for how Congress would organize itself to develop and approve annual regulatory budgets:

First, the congressional leadership would establish a regulatory appropriations committee, comprised of members with interest and expertise in regulatory matters. The committee would then divide itself into several subcommittees—perhaps environmental (including EPA), other health and safety (FDA, OSHA, NHTSA, USDA, etc.), and economic (FCC, FTC). The goal would be a logical grouping of regulatory

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goals and approaches, and covering the whole gamut of federal regulatory efforts.

Each year, along with the spending budget, the administration would send Congress a proposed regulatory budget, detailing the major programs and the costs it proposes the federal government to impose for the fiscal year, by agency. Congress would then establish, by concurrent resolution, an overall limit for regulatory costs, and then divide this total among the regulatory appropriations subcommittees. Like their spending counterparts, these subcommittees would approve regulatory appropriations for consideration by the full committee and then the respective chambers and the president.²³⁹

Regulatory budgeting is not a new idea.²⁴⁰ Robert Crandall of the Brookings Institution first mentioned the use of “shadow budgets” for expenditures required of the private sector in 1978.²⁴¹ In 1979, Jim Tozzi produced a report for OMB on regulatory budgeting.²⁴² In both the 95th and 96th Congresses, Senator Lloyd Bentsen (D-TX) sponsored legislation to establish a regulatory budget.²⁴³ The Contract with America included a regulatory budget proposal, and Rep. Lamar Smith (R-TX) introduced regulatory budget bills in the 103rd and 104th Congresses. The Paperwork and Regulatory Improvements Act (H.R. 2432), sponsored by Rep. Doug Ose (R-CA) in the 107th and 108th Congresses, would require OMB to undertake pilot projects in regulatory budgeting, and report to Congress on the feasibility and advisability of establishing regulatory cost caps as part of the president’s annual budget.

What are the potential benefits and perils of regulatory budgets? And is regulatory budgeting feasible?

B. What Are the Potential Benefits of Regulatory Budgets?

In theory, formal cost caps on private and public expenditures to comply with federal regulations would yield several important benefits.²⁴⁴

Regulatory caps would make hidden costs visible. Regulation is in some cases a substitute for more visible forms of government intervention. For example, Congress can provide for environmental cleanup, workplace safety improvements, or worker training programs either by levying taxes and appropriating funds for those purposes, or by authorizing agencies to issue rules compelling private entities to accomplish those objectives at their own expense. If Congress opts for taxes and spending, the costs are visible and the public has an opportunity to weigh them against the putative benefits. However, if Congress opts for regulation, the benefits, at least to the general public, will appear to be free, even though the rules may increase consumer prices, reduce employment, or make U.S. firms less competitive. Consequently, citizens will tend to demand or tolerate more intervention than they would if the costs were visible and paid for with taxes.

Because regulatory costs are hidden, regulation has long been a preferred intervention strategy of both special interests pursuing competitive advantage and ideological groups pursuing their particular visions of the public interest. As the

The spending appropriations process provides a rough model for how Congress would organize itself to develop and approve annual regulatory budgets.

federal deficit soars and pressures mount to control spending, politicians may be increasingly tempted to use hidden regulatory taxes to accomplish their goals. A regulatory budget would make the cost of rules as visible as the cost of taxes, discouraging regulation's use as a tool of fiscal legerdemain.

Caps could constrain the overall size and cost of government. Regulatory budget ceilings would encourage policymakers to confront and make explicit choices about the total cost of government. Today, regulatory costs are mostly invisible to the public, and largely escape congressional review. Congress would be more likely to consider and limit governmental costs if it had to debate and approve annual authorizations for federal regulatory expenditures.

Caps could encourage agencies to target the most urgent risks, choose the most cost-effective alternatives, and terminate under-performing rules. Regulatory agencies bear no clear opportunity costs for the decisions they make. Unlike spending agencies, they do not use up their authority in the act of exercising it. They face no risk that imposing large burdens today will limit their ability to act tomorrow. They face no pressure to share—and, thus, divide—their control of private resources with other regulatory agencies.

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In contrast, opportunity cost is an ever-present reality for spending agencies. In the fiscal arena, debate swirls around the question of whether an agency (say, the Department of Defense) could better advance its objectives by spending more in category A (say, a new air mobile division) than in category B (say, a new battleship). DoD 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, make tradeoffs among competing programs, and cede to other agencies some part of the spending authority they would like to have. Even though they spend other people's money, they are constantly reminded by opportunity costs that there is no such thing as a free lunch.

Regulatory budgets could introduce into agency deliberations a whole new calculus of opportunity cost. Suddenly an agency would need to rank risks and target the most pressing ones first, if it did not want to exhaust its authorization before accomplishing anything important. Regulating one hazard or alleged market failure would impinge on its ability to regulate others. There likely would be fewer such irrational cases as the EPA's program to remove asbestos from buildings even though the risk ranked low on a scale of peril.²⁴⁵ Without a budget, only the regulated entities face costs. With a budget, an agency's own choice will constrain it in the future, which may help induce it to make wiser choices.

Caps could force agencies to compete for regulatory authority, fostering innovation and excellence. During every regulatory budget cycle, Congress would have an opportunity to ask, "What are the most lethal hazards facing

Americans, and which agencies are best suited to address those risks?” Budgeting would force regulators, regulatory programs, or even entire agencies to compete with one another for the right to impose burdens on the American people. Each would have an incentive to find and expose the weaknesses in others’ cost and benefit estimates. Each would have an incentive to find smarter ways to serve the public in order to justify its requests for budget authority.

Suppose a single regulatory budget were developed for all programs addressing health, safety, and environmental risks. The tighter the budget, the more regulators would be constrained to compete on the basis of the most meaningful bottom line: each agency would want its least effective mandates to save more lives per dollar than the rules of another agency. Under an (obviously unachievable) ideal regulatory budget, any reshuffling of agency budget allocation could not save more lives.²⁴⁶ A more competitive system would likely not only be more economical but also spur agencies to invent more effective ways to protect public health and safety.

C. What Are the Potential Perils of Regulatory Budgets?

Regulatory reform is a political process and, as such, subject to the “law of unintended consequences.”²⁴⁷ Depending on its design and other factors, a budget could conceivably make regulation less accountable and/or more costly, if it:

1. Allows agencies to expand their authorizations by offsetting costs with benefits;
2. Creates a bias in favor of rules, such as product bans, with small direct compliance costs but large indirect effects on consumer prices, efficiency, or profits;
3. Encourages agencies to produce false and misleading cost estimates;
4. Spends political capital needed to accomplish other reforms; or
5. Significantly increases paperwork burdens on regulated entities.

Perils 1-4 are discussed immediately below. Peril 5 is discussed later, in the subsection on the tracking of regulatory compliance costs.

Net cost trickery. Agency officials and public interest groups typically abhor the idea of placing explicit monetary limits on an agency’s capacity to issue rules. However, some might be willing to countenance a budget that allows agencies to offset costs with benefits to arrive at a net-cost of regulation. In their view, leaving benefits out of budget calculations would present a one-sided picture of regulatory impact, creating a bias against the public interest in regulatory safeguards.

This criticism is unwarranted. Neither the president’s budget submission nor Congress’s budget resolution includes benefit estimates for federal mandatory and discretionary spending programs. Yet, with the deficit now approaching half a trillion dollars, no one would claim that the fiscal budget process is biased against spending. If a spending agency attempted to squeeze more spending authority out of OMB or Congress by offsetting program costs with benefits, it would be laughed out of court.

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Allowing agencies to offset costs with benefits would defeat a regulatory budget's central purpose—cost control. In fact, a net-cost “budget” would be a license to spend. Agencies inevitably believe that their regulations, at least in the aggregate, generate net benefits. Thus, if an agency is allowed to regulate as long as it achieves a net benefit, it will never run out of budget authority, no matter how costly its rules.

If spending agencies were allowed to use net-cost calculations to develop their budgets, fiscal responsibility would be utterly destroyed. For example, the monetary benefit of preventing a full-scale military attack on the United States, and of being able to win such a war if it occurred, is larger than any expenditure we might make on military programs. Thus, if we allowed DOD to offset costs with benefits in its annual budget request, defense spending could easily be multiples of what it is today. To describe such profligacy as budgeting would be an abuse of language.

Indirect cost explosion. Regulations have both direct and indirect costs. Direct costs are the expenditures—for capital equipment, operating systems, paperwork, and R&D—that entities specifically make to comply with a rule. The indirect costs are all the other costs to producers and customers as a consequence of regulation, including higher consumer prices, inefficiencies, lower profits, and reduced innovation. A case can be made that just as a fiscal budget applies solely to direct dollar outlays, not to the economic repercussions of such outlays, so too a regulatory budget should cover only direct compliance expenditures. A budget's main purpose is to control spending, and, as Tozzi points out, “indirect costs do not show up as identifiable expenditures required by regulation.” Rather, indirect costs are effects of regulation on pricing, investment, and employment, and “their measurement typically requires use of complex economic models,” not the types of accounting tools used, for example, to calculate a firm's taxable income.²⁴⁸

But excluding indirect costs has risks. Indirect costs may in some cases be larger than the direct costs of regulation. And, as Wayne Crews cautions, if a budget system overlooks rules with large indirect costs, agencies will have an incentive to increase production of such rules:

Imagine a regulatory budget were established that addressed only direct costs of regulations—such as the engineering costs of controlling an emission. But suppose outright input or product bans are not regarded as direct costs for budgeting purposes [because not purchasing an input or not selling a product is not an identifiable expenditure], and therefore not counted in the budget. Under that structure, nearly every environmental regulation could be expected to entail a ban so that regulators would avoid exhausting their budgets. The incentives set up by this sort of budget would be disastrous.²⁴⁹

To avoid an indirect cost explosion under a regulatory budget, Crews recommends that Congress “forbid just those types of regulatory activities—such as product bans—most likely to produce indirect costs.” But what if a product or input ban is the only feasible way to address an urgent health or safety hazard? In such cases, advises Crews, the rulemaking agency should be required to assess the indirect costs, and Congress should have to approve the ban before it can go into effect.

Analysis: from bad to worse. Budgets could exacerbate agencies’ perverse incentives to produce regulatory analyses with inflated benefit estimates and deflated cost estimates. As Belzer explains:

As it stands now, an agency’s incentive to understate costs is largely driven by the fact that high costs (irrespective of the magnitude of benefits) generate bad public and Congressional relations. But an enforced regulatory budget would limit what regulations an agency could issue....Agencies would respond to a regulatory budget much like they do to the Information Collection Budget—by reducing their estimates as necessary to make them fit under the allowable ceiling, not by reducing the paperwork burdens they impose.²⁵⁰

Rather than limit regulatory spending, budgets might simply intensify agencies’ incentives to low-ball regulatory costs.

On the other hand, regulatory budgets might improve agencies’ estimation of both costs and benefits, because there would be a much greater demand for reliable information. Under a budget, agency analyses would receive far greater scrutiny than they do today, and regulatory accounting would be held to higher standards of accuracy, consistency, and verifiability.

Political capital costs. In his multi-country review, *Constraining Government Regulation*, economist Bryce Wilkinson, although sympathetic to proponents’ goals, suggests that regulatory budgeting is a cul-de-sac:

Currently, we are unaware of any country that has successfully implemented this approach. The practical difficulties look formidable. There appears to be a risk that implementation difficulties would absorb too much time and goodwill that could be put to better use in making an assault on regulations that are obviously causing disturbing outcomes and whose rationale is unclear if not decidedly dubious.²⁵¹

The same advocacy groups that torpedoed regulatory reform in the 104th, 105th, and 106th Congresses abhor regulatory budgets. Indeed, groups like OMB Watch and Public Citizen oppose cost-benefit tests, OMB’s annual regulatory report, and an independent Congressional Regulatory Office, partly because such initiatives are steps toward the creation of regulatory budgets.²⁵² Regulatory budget advocates would have to spend much time and political capital battling such groups, perhaps jeopardizing other more attainable reforms.

On the other hand, as recent experience suggests, anti-reform forces will mobilize against any proposal to rein in regulatory costs, however timid or ineffectual, so reformers might as well aim high. Indeed, reformers are unlikely to advance their agenda unless they are prepared to fight for dominance of the moral high ground, and advocacy of a budget would allow them to directly challenge the moral legitimacy of the status quo.

Groups like OMB Watch and Public Citizen believe that agencies should be required to adopt the most protective regulations, not the most cost-effective or least burdensome. In their view, it is immoral to cap private expenditures for such priceless things as children's health, worker safety, or environmental quality. But although this health-at-any-cost dogma may seem like a moral suit of armor, it is actually an Achilles heel. In a world of scarcity, ignoring costs means ignoring the unavoidable tradeoffs between alternate uses of the same resources; it means ignoring the health and welfare benefits that regulatory burdens diminish or preclude. As Tozzi points out:

A myriad of national goals are all competing for a share of our limited resources. The dollars spent on passive restraint systems for automobiles could be spent by the government on cancer research, by private citizens on housing, or by anyone on anything from smoke detectors to skateboards. The question is what is the correct size of the regulatory budget—how much of our national income should we devote to regulatory purposes?²⁵³

DOD military procurement programs, National Institutes of Health AIDS programs, and Federal Aviation Administration aviation safety research and development programs all contribute to the safety or health of the American people. A case can be made moreover, that defense programs, by deterring nuclear and other attacks on the people and territory of the United States, protect the environment. Yet no responsible policymaker would argue that Congress should not set budgets for weapons procurement, AIDS programs, or aviation safety research, or that it is immoral to consider the economic impacts of the taxes required to pay for those programs.

Households also spend money for many worthy purposes. In fact, most household- spending is for goods and services that sustain life, enhance health and safety, and develop human capital. Yet no one scolds households for attempting to budget their expenditures. Since the costs of regulation ultimately fall on households, shouldn't those costs, too, be subject to budget discipline? Moreover, if Congress has a duty to deliberate on how much of the household's resources spending agencies should control, doesn't it also have a duty to deliberate on how much regulatory agencies should control?

The regulatory status quo is a system of special privilege. Regulatory actions are outside the system of checks and balances—the annual appropriations

No one scolds households for attempting to budget their expenditures. Since the costs of regulation ultimately fall on households, shouldn't those costs, too, be subject to budget discipline?

process—in which defense contractors, AIDS researchers, and households seeking tax relief compete for shares of limited resources. The unbudgeted character of regulation means that some policy agendas—and their partisans—are *more equal* than others.

D. Is Regulatory Budgeting Feasible?

Estimation, tracking, and enforcement are essential functions of any budget process. Can policymakers develop the information and tools needed to reasonably estimate, accurately track, and credibly enforce limits on regulatory expenditures?

1. Estimation Issues

The first phase in developing a fiscal budget is cost and revenue estimation. Similarly, cost estimation would be the first step in preparing a regulatory budget, whether for an individual rule, a regulatory program, or an agency as a whole. As we have seen, agencies often fail to meet minimum standards of regulatory accounting, and a budget could intensify perverse incentives to overestimate benefits and underestimate costs.

On the other hand, a budget would increase the demand for and value of reliable cost information, and the market might respond by increasing the supply and quality of regulatory analysis. Just as environmental rules that set goals beyond current technological capabilities can sometimes be “technology forcing” (spur development of new capabilities),²⁵⁴ so regulatory budgets could be “information forcing” (spur development of new and better systems to collect and analyze cost data).

Initial estimates of regulatory burden might be quite crude. But estimation errors should be no more fatal to regulatory budgeting than they are to expenditure budgeting. OMB and CBO seldom reach the same projections for federal revenues and outlays, and both agencies periodically revise their estimates in light of new information. Moreover, fiscal budget estimation is an art that has developed over many decades and continues to evolve. Time and experience would similarly improve regulatory cost estimation, especially as regulated entities begin to track and report their expenditures to comply with federal rules.

Tozzi, writing in 1979, noted more than a dozen studies, surveys, and sources policymakers at the time could use to estimate the direct costs of federal air and water pollution controls.²⁵⁵ For example, from 1973 to 1994, and then in 1999, the Census Bureau conducted an annual survey of about 20,000 manufacturing plants to estimate expenditures for pollution abatement and control.²⁵⁶ Similarly, from 1973 to 1994, the Bureau of Economic Analysis (BEA) surveyed thousands of entities to estimate private and public spending for pollution abatement.²⁵⁷ Census also produced separate reports on expenditures for public sewage treatment plant and sewer line construction, and on operating expenditures for sewage treatment, solid waste collection, and solid waste disposal. Congress would need to commission similar studies if it decides to explore the feasibility of regulatory budgets. At a minimum, it would also have to crack

down on agencies that fail to provide monetized cost estimates for new economically significant or major rules.

Estimating indirect regulatory costs can be highly speculative, depending on “huge, complex and often proprietary models of the economy.”²⁵⁸ However, this poses no problem if the budget caps apply only to direct compliance costs. As noted earlier, indirect costs are not identifiable expenditures and, thus, are not easily integrated into an accounting framework or budget process.

Most of the costs of economic regulations—rules dealing with business decisions such as pricing, entry, and investment—are indirect. Thus, a case can be made that economic rules should not be included in a regulatory budget. As Tozzi explains:

The economic thinking behind the use of a budget as an allocation mechanism doesn’t work so well for economic regulation; i.e., control of prices, entry, exit, and service levels. Economic regulation rarely presents choices of the degree or cost of spending, involved in some reasonably well-defined goal. Typically, the costs of economic regulation appear to be by-products of policies adopted for a variety of reasons and...the issue is often whether the regulation is needed at all. In these circumstances, it is not clear what would be the point of attempting to impose a budget constraint.²⁵⁹

If policymakers believe economic regulations produce more cost than benefit, the appropriate response is not to try to cap the indirect effects on consumer prices or producer profits, but to eliminate the rules altogether.

To be sure, social regulations mandating direct expenditures to meet specific health, safety, or environmental objectives may also entail indirect costs. In cases where indirect costs are likely to be as large as or larger than the direct costs, agencies could be required to estimate both direct and indirect costs. Again, however, one way to keep estimation responsibilities manageable is to prohibit those types of social rules—such as input or product bans—likely to have substantial indirect costs.

2. Tracking Issues

Although Congress seldom succeeds in balancing the federal budget, it has little difficulty preventing agencies from spending in excess of their annual appropriations. Ever since 1870, a provision that later became the Antideficiency Act has made it illegal for agencies to commit or spend more money than Congress previously made available.²⁶⁰ Under the Act, agencies may not enter into contracts that exceed the enacted appropriations for the year, purchase services and merchandize before appropriations are enacted, or pay bills when there is no cash in the appropriation or fund account.²⁶¹ The Act also establishes penalties for spending violations. For example, an official convicted of willfully and

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knowingly over-obligating or over-expending agency funds may be fined up to \$5,000 and imprisoned for up to two years.²⁶²

The Antideficiency Act works—i.e., prevents agencies from exceeding their annual appropriations—because it is relatively easy to determine when an agency spends its last allowable dollar. Tracking regulatory compliance expenditures is more difficult. Literally thousands of entities spend billions of dollars to comply with federal rules, and few currently maintain separate accounts to track such expenditures. However, many firms might track compliance expenditures if they believed OMB and Congress would use the information to limit regulatory costs. Firms would surely do so if required by law to institute regulatory accounting and reporting systems. If Congress decides to explore the feasibility of regulatory budgets, it should probably start with regulations affecting a relatively small number of easily identified and closely monitored entities, such as steam electric generating units.

To determine when a regulatory agency had exhausted its budget authority, firms would need to monitor their compliance expenditures and report the information to the agency and/or OMB. Tozzi points out that current law already includes a provision for tracking compliance costs, albeit on a limited scale:

Section 120 of the Clean Air Act establishes a noncompliance penalty program. This program levies penalty on any firm that violates emission requirements established pursuant to the Clean Air Act. The penalty is calculated as the incremental expenditures—beyond those currently being expended—needed to bring the source into compliance.²⁶³

The Section 120 penalties apply to *any* owner or operator of a major stationary source in noncompliance with *any* emission limitation, emission standard, or other requirement established under *any* of the Act's regulatory programs. "Obviously," Tozzi comments, "the ability of the Federal Government to perform an accurate calculation of the compliance costs resulting from the imposition of a Federal regulation on a private sector source is a key element of this program." Even though no regulatory budget exists, Congress, in Section 120, has adopted a "statutory requirement to estimate compliance costs for a major sector of the economy." Moreover, because the penalty equals the incremental cost of compliance, "there is considerable incentive to develop accurate estimates of compliance cost. The higher the estimates of compliance costs—the higher the penalty."

If it is possible to track compliance costs for the purpose of penalizing a firm, then in principle it is also possible to track compliance costs for the purpose of determining when an agency runs out of regulatory authority. The record keeping and accounting systems required to implement a regulatory budget would, of course, be far more extensive than those required to assess Section 120 noncompliance penalties. Compliance costs would have to be calculated not only for a few errant firms, but also for all firms subject to the rule or regulatory program for which a budget was enacted.

To keep both reporters and agencies honest, Congress may need to create a new IRS—an Internal Regulatory Service. There is a risk that a regulatory budget could spawn paperwork burdens, fines, and criminal penalties akin to those associated with tax preparation, filing, and auditing.

At some point Congress would also have to provide for a system of regulatory audits. Under a budget, firms would have an incentive to report higher costs than they actually incur both to justify demands for regulatory relief and to deplete more rapidly agencies' authority to regulate. By the same token, agencies would have an incentive to low-ball costs to delay exhausting their budget authority. Compounding this problem is the fact that some investments may have more than one possible explanation. For example, electric technologies such as infrared paint drying, ultrasonic metal cleaning, and microwave disinfection of medical wastes can reduce toxic emissions and other waste products.²⁶⁴ EPA regulations may be a factor in a firm's decision to purchase such technologies, but so might state regulations, threats from the tort system, or a desire to improve the firm's performance and efficiency. It would not be surprising if the firm and EPA take different views as to whether, or to what extent, the firm's expenditure should count against EPA's budget.

To sort out such issues and keep both reporters and agencies honest, Congress may need to create a new IRS—an Internal Regulatory Service. Like the Internal Revenue Service, the regulatory audit agency would need to promulgate rules to standardize accounting procedures and reporting requirements. The audit agency would also need the power to penalize firms for non-compliance with such procedures, and to prosecute firms for fraudulent reporting of regulatory cost information. There is a risk that a regulatory budget could spawn paperwork burdens, fines, and criminal penalties akin to those associated with tax preparation, filing, and auditing.

3. Enforcement Issues

A budget worthy of the name must be enforceable. That a regulatory budget could be as enforceable as a fiscal budget seems doubtful, because it will always be easier to count the dollars federal agencies spend than to monetize the resources thousands of firms invest to comply with federal rules. However, a regulatory budget would not need to be air tight to accomplish its central purpose: compel elected officials to make explicit choices about how much money regulated entities are to spend, and what they are to spend it on.

Moreover, we should bear in mind that the federal fiscal budget is far from a perfect system of spending control. At first glance, the enforceability of the federal budget may seem absolute.²⁶⁵ Under the Antideficiency Act, agencies are forbidden to spend more money than Congress has appropriated. However, as is widely known, annual appropriations control only about one-third of all federal expenditures in a typical year. Most spending is governed by so-called permanent authorizations—laws authorizing agencies to spend money without first obtaining an annual appropriation from Congress.

Permanently authorized expenditures include interest payments on the public debt and spending for several entitlement programs, such as Social Security,

Medicare, Medicaid, unemployment insurance, and federal employee retirement.²⁶⁶ Under those programs, any person meeting the eligibility criteria is entitled to a payment from the Treasury, and spending grows on autopilot along with the number of eligible beneficiaries. Such “mandatory” spending is “uncontrollable,” at least on a year-to-year basis. Congress could but does not cap entitlement programs, which are projected to double in cost over the next 10 years.²⁶⁷ Washington’s red ink nightmare is, however, a reason to reform the fiscal budget process, not an excuse to keep regulatory expenditures unbudgeted.

Regulations often take years to implement, and this, too, raises questions about how regulatory spending caps would be enforced. The annual costs of a particular rule may begin small, increase dramatically as compliance deadlines kick in, and then decline sharply after the regulated industry has made the necessary adjustments. At what point in its implementation should a rule be reviewed to determine if compliance costs are within or beyond the cap? If compliance burdens are variable over time, should the budget include annual caps or multi-year caps? Review of a multi-year cap might be more accurate than review of an annual cap, but it might also be less useful. The longer Congress or OMB waits to assess a rule’s cumulative costs, the harder it will be to keep costs within the cap by modifying the rule.

Moreover, modifying an existing rule is seldom easy or quick. To do so, an agency must propose a new rule and go through the APA-governed public notice and comment process, which can drag on for years. In addition, if the rule is mandated by statute or court order, agency actions to modify the rule could become bogged down in litigation.

It should be recognized, however, that fiscal programs often fund multi-year projects with variable annual costs, yet that does not prevent policymakers from setting and enforcing budget caps. Weapons procurement programs, highway construction programs, and other public works programs all fund multi-year projects whose annual costs may vary considerably and whose cumulative costs may not be known until completion of the project. Furthermore, there is a remedy for budget-busting cost overruns: scale back appropriations in future years. As Tozzi comments:

The absence of a corrective mechanism in the year the actual expenditures exceed estimated expenditures is not to suggest the absence of a corrective mechanism in future years. In fact, corrective mechanisms are developed—in the fiscal budget—as a result of the information gained during the budget year. There is a large array of such corrective mechanisms—these range from requesting less funds in future years to developing better models for the expenditure of funds.²⁶⁸

Similar mechanisms could be developed to enforce regulatory spending caps. For example, if after full implementation, the cost of a rule exceeds the agency’s budgeted authority by \$100 million, Congress would reduce the agency’s regulatory budget for the next fiscal year (or multi-year period) by \$100 million.

A regulatory budget would not need to be air tight to accomplish its central purpose: compel elected officials to make explicit choices about how much money regulated entities are to spend, and what they are to spend it on.

Since regulatory budgeting is uncharted policy territory, development of regulatory budgets should be seen as an experiment, and should proceed by small steps.

As the slow evolution of the federal expenditure budget over several decades suggests, the development and implementation of regulatory budgets could take many years.

To arouse public ire against Congress and overturn its regulatory spending caps, an agency might pursue a variant of the Washington Monument ploy, claiming it must rescind its most essential rules in order to stay within budget. Congress could preempt such gamesmanship by requiring that regulatory budget cuts fall first on rules with the least benefits per dollar, on discretionary rules before statutorily prescribed rules, or on newer rules before longstanding rules.²⁶⁹

E. Next Steps

Since regulatory budgeting is uncharted policy territory, development of regulatory budgets should be seen as an experiment, and should proceed by small steps. It might be best to start with an industry that is already closely monitored for regulatory purposes, and types of regulation for which large amounts of cost data are already available. Thus, Congress might experiment with a budget for new air quality controls on steam electric generating plants. Such a budget could be run as a simulation exercise to test its feasibility and reveal the potential accounting, reporting, and enforcement problems policymakers would need to address in designing statutory limits on regulatory compliance burdens.

If Congress finds the simulation promising, it would need to take several steps to implement a budget, including: (1) commission statistical agencies such as the Census Bureau, the Bureau of Economic Analysis, the Bureau of Labor Statistics, the Bureau of Transportation Statistics, and the Energy Information Administration to survey regulatory compliance costs in various industries; (2) require the pertinent regulatory agency or agencies to estimate the compliance costs of existing and new regulations; (3) require the affected industry or industries to track and report compliance cost information; and, (4) establish a committee structure and legislative process for setting regulatory cost caps. As the slow evolution of the federal expenditure budget over several decades suggests, the development and implementation of regulatory budgets could take many years.

F. Relationship between Regulatory Budgeting and Congressional Review

As indicated above, congressional review combined with competitive analysis of regulatory costs and benefits could evolve into a budgeting system, because high-quality cost estimates would continually inform Congress's decisions to approve or not approve agencies' final rules. As also noted, congressional review could be implemented incrementally, with Congress at first voting only on completed economically significant rulemakings—a relatively small number (two to three dozen annually). There are too many minor rules for Congress to review one-at-a-time. It was suggested earlier that each agency's minor rules could be bundled into a package subject to an up-or-down vote. A budget process would provide an alternative and probably superior form of review.

Under a budget system, instead of voting on an agency's minor rules as a package, Congress would vote on program-wide or agency-wide cost caps for all rules, major and minor. Congress would still take full responsibility for regulatory decisions, because the caps would be set through a regulatory appropriations process modeled on the spending appropriations process. Congress would set the caps only after proper review of the president's regulatory budget proposal by the relevant committees and subcommittees.

Several options are possible. If the budgeting system evolves from a system of congressional review informed by competitive regulatory analysis, Congress might elect to retain targeted, case-by-case, review of economically significant rules, and review all other rules in the context of agency- or program-wide budget caps. On the other hand, Congress might opt for a pure budget system in which authority for all rules, major and minor, is granted when lawmakers enact the overall budget for an agency or program. When approving an agency or program budget, Congress might allow the agency broad flexibility to develop and adopt rules within the specified caps. Alternatively, Congress might insist (through appropriations and report language) that the agency stick to a fairly detailed regulatory agenda.

IX. Summary and Conclusion

What (or who) caused the recession of 2001 and the slow recovery of subsequent years will likely remain a hotly debated issue for some time. The dot.com crash, the September 11 terrorist attacks, and weak export markets all played a part in killing the 1990s economic boom. However, the regulatory-induced telecom crash also contributed to and prolonged the recession. The Telecommunications Act inflicted price controls and infrastructure socialism on a key high-tech industry. A regulatory system in which non-elected officials not only draft but also enact regulations allowed the FCC to subsidize entry into local telephone markets, creating an unsustainable bubble.

Those entrusted with stewardship of the U.S. economy should begin now to review the serious defects of the current regulatory process and develop a reform agenda for the future. Delegation of legislative powers to non-elected bureaucrats violates Article I of the U.S. Constitution and creates an unaccountable system in which decision-makers have no incentive to control regulatory costs. Allowing agencies to pass final judgment on the analytical basis of their regulatory proposals creates an obvious conflict of interest and is bound to skew policymaking in favor of regulatory activism. The unbudgeted character of federal rules creates a system of special privilege in which agencies and their allies control enormous resources without having to compete for the authority to do so.

Regulatory reform is difficult, but it need not be a pipedream. Although many interests profit from the status quo, few will be comfortable attacking reforms that clearly aim to replace monopoly privilege with competition, bureaucratic lawmaking with democratic accountability, and hidden costs with cost control.

Although many interests profit from the status quo, few will be comfortable attacking reforms that clearly aim to replace monopoly privilege with competition, bureaucratic lawmaking with democratic accountability, and hidden costs with cost control.

This report has outlined numerous options to make federal regulation more affordable, effective, and accountable. A concise summary follows:

- ***Amend the Telecommunications Act.*** Make clear that the goal is to deregulate the telecom industry; set clear schedules to phase out price controls and forced-access regulation; establish regulatory parity for telephone, cable, and wireless carriers by removing, not increasing, regulatory burdens; and, prohibit state and local governments from balkanizing information networks and telecom markets.
- ***Publish an Annual Regulatory Report Card.*** OMB should produce an annual Report Card consolidating vast amounts of quantitative information already available in agency databases. Congress and the interested public would be able to see at a glance whether the number of rules affecting small businesses and localities is going up or going down, whether any significant deregulation is occurring, the minimum cost of recently adopted major rules, and whether regulatory activity at the top rulemaking agencies is primarily driven by statute or agency initiative.
- ***Create New Categories of Major Rules.*** OMB (or Congress) should require the use of new rankings or categories (Category 1, 2, 3, etc.) in official publications to better convey the full costs of the major or economically significant rules that agencies propose or adopt.
- ***Make the Rule Reform Nominations Process More Transparent.*** There currently exists no up-to-date information clearinghouse on what actions, if any, agencies are taking on public nominations of rules to be reviewed and modified or rescinded. The lack of timely information discourages the public from submitting nominations and following up on agency performance. OMB should post all nominations it receives on its Web site, and provide timely status reports about them. Further, OMB should post any items slated for OIRA or agency review in the Unified Agenda, with a hyperlink to the OMB Web site list.
- ***Extend OMB Review to Independent Agency Rulemakings.*** Several statutes—the Paperwork Reduction Act, the Information Quality Act, the Regulatory Flexibility Act, and the Regulatory Right to Know Act—create regular opportunities for OMB to review and offer comment on independent agencies’ regulatory activities. Independent agencies would be under no legal obligation to heed OMB’s views, but they would risk public disapprobation for ignoring good advice, failing to address reasonable criticism, or refusing to correct significant errors.
- ***Uphold Information Quality Standards.*** OMB should insist that all agency-disseminated information be held to high standards of objectivity and utility. It should also affirm that the Act’s petition process applies to

rulemaking information, and that agency responses to information correction petitions are subject to judicial review.

- ***SBREFA: Clarify Key Terms and Compensate Winning Plaintiffs.*** To prevent agencies from evading the duty to perform regulatory flexibility analyses, Congress should authorize SBA's Office of Advocacy to define "significant impact on a substantial number of small entities" via a notice-and-comment rulemaking. To level the legal playing field between agencies and the small entities they regulate, Congress should authorize winning small business plaintiffs to collect compensation for damages and full reimbursement for all reasonable attorneys fees. Congress should also overturn the Supreme Court's *Buckhannon* decision so that small business plaintiffs once again qualify as prevailing and, thus, entitled to recover legal expenses if they prompt an agency to change its conduct or policy, whether or not the change is ordered by a court.
- ***UMRA: Shrink Regulatory Impact Assessment Loopholes.*** Agencies avoid preparing regulatory impact assessments (RIA) of intergovernmental mandates simply by claiming to have a good cause to skip the usual notice-and-comment process. An agency should not be allowed to use the good cause exception unless it publishes an explanation in the *Federal Register* at least 30 days before issuing the rule, and invites public comment. Agencies should also have to perform an RIA for major intergovernmental mandates even if the rule's requirements are specifically set forth in law. The public has a right to know how much it will be paying whether the rule is discretionary or statutorily prescribed.
- ***Make Agencies Compete for the Right to Score Regulatory Impacts.*** Agencies enjoy an exclusive right to score the impacts of their regulatory proposals. This creates a classic conflict of interest, because agencies have an obvious incentive to skew regulatory analyses to justify their predetermined preferences and agendas. OMB (and GAO, if Congress approves) should hold a contest to determine which analysis of each major regulatory proposal is best, reviewing the rulemaking agency's cost-benefit analysis plus those submitted by experts in industry, state agencies, and the non-profit sector. Unless the rulemaking agency's analysis visibly conforms to OMB's best practices and information quality guidelines, it would have zero chance of winning. Agencies would have to clean up their analytical acts or lose credibility as regulatory experts.

➤ ***Extend UMRA Protections to the Private Sector.*** Just as any member of Congress can now force the House or Senate to debate and vote on whether to consider measures that would cost lower-level governments \$50 million or more, so members should have the option to force Congress to debate and vote on whether to

consider legislation containing \$50 million mandates on the private sector, or \$25 million mandates on small business.

- ***Establish a Congressional Regulatory Office.*** OMB is a watchdog in constant danger of becoming a rubber stamp, because the OMB director and the heads of various rulemaking agencies work for the same administration and serve at the pleasure of the president. To participate effectively in regulatory decisions, and effectively check both OMB and the agencies, Congress needs an independent analytic arm—a regulatory counterpart to CBO. At a minimum, Congress will need to expand GAO’s regulatory program if, as recommended above, it tasks GAO to compete with OMB in selecting the best analyses of regulatory proposals.
- ***Require Congressional Approval before New Rules Are Effective.*** Congress will have much greater motivation to consider economic impacts when drafting regulatory statutes, and to insist that agencies consider low-cost and non-regulatory alternatives, if it has to approve agencies’ final rules before they can take effect. Regulations are implicit taxes that have the force of law. To most Americans, it is obvious that nobody except their elected representatives should have the power to make laws or raise taxes. Policymakers should end the current system of regulation without representation and replace it with a system of regulatory accountability.
- ***Establish a Bipartisan Regulatory Reduction Commission.*** To reduce the mass of existing federal rules, Congress should appoint a bipartisan Regulatory Reduction Commission. The Commission would review agency regulations; invite OMB, GAO, and the interested public to submit recommendations; hold hearings; and assemble a yearly package of proposed regulatory reductions. The package would be subject to an all-or-nothing vote, with no amendments allowed. Congress would send any package it approved to the president for his signature. The Commission could be kept active for as long as Congress deems necessary, and potentially could shave off large chunks of ineffective regulations over a number of years.
- ***Conduct Pilot Projects to Test the Feasibility and Desirability of Establishing Regulatory Budgets.*** The ultimate goal of regulatory reform is to make agencies act more like households. However devoted to the health and safety of their members, households face inexorable tradeoffs in the use of their resources and, consequently, have strong incentives to set priorities and economize. Whether consciously or intuitively, a household budget guides and constrains the typical family’s spending decisions. A similar decision framework should—but does not—inform regulatory choices. What is most critically lacking in the regulatory arena is a budget process enabling elected officials to make explicit choices about the size of regulatory burden relative to the economy, and about

the allocation of scarce resources among the myriad of regulatory objectives. Congress should authorize OMB to conduct pilot projects to explore the estimation, tracking, and enforcement issues policymakers would need to resolve before setting statutory limits on regulatory costs.

Regulatory reform is an enterprise fraught with political risk. However, the regulatory status quo is itself a source of considerable risk, as the regulation-induced telecom meltdown and its economic repercussions show. If war is too important to be left to the generals, then regulation is too important to be left to the regulators. Elected officials should take more responsibility for regulatory decisions, and agency analyses should have to compete for public approval with analyses prepared by non-agency experts. If spending agencies are not above being constrained by budget caps on the costs they may impose, then regulatory agencies should not be either.

Those who flinch at the thought of challenging the regulatory status quo should remember: “Noble things are hard.”²⁷⁰ No guts, no glory. Alexander Hamilton, the nation’s first Treasury Secretary, called “love of fame” “the ruling passion of the noblest minds.”²⁷¹ If even a few policymakers seek the honor of renewing America’s constitution of liberty, regulatory reform may yet have a political future.

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ACKNOWLEDGEMENTS

The author is grateful to the following persons for their helpful comments on earlier drafts of this report:

- Dr. Richard Belzer, President, Regulatory Checkbook
- Clyde Wayne Crews, Jr., Vice President and Director of Technology Studies, Competitive Enterprise Institute
- Susan Dudley, Director, Regulatory Studies Program, Mercatus Center
- James L. Gattuso, Research Fellow in Regulatory Policy, Thomas A Roe Institute for Economic Policy Studies, Heritage Foundation
- Barbara Kahlow, Former Staff Director, House Government Reform Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs
- Solveig Singleton, Former Director of Technology Studies, Competitive Enterprise Institute
- Jim J. Tozzi, Former Deputy Administrator Office of Information and Regulatory Affairs, Office of Management and Budget, and currently Director, Multinational Business Services

NOTES

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