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HOW TO IMPROVE REGULATORY ACCOUNTING: COSTS, BENEFITS, AND IMPACTS OF FEDERAL REGULATIONS—PART II

HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTH CONGRESS

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HOW TO IMPROVE REGULATORY ACCOUNTING: COSTS, BENEFITS, AND IMPACTS OF FEDERAL REGULATIONS—PART II

WEDNESDAY, FEBRUARY 25, 2004

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2247, Rayburn House Office Building, Hon. Doug Ose (chairman of the subcommittee) presiding.

Present: Representatives Ose, Schrock, and Tierney.

Staff present: Barbara F. Kahlow, staff director; Anthony Grossi, clerk; Megan Taormino, press secretary; Krista Boyd, counsel; and Jean Gosa, minority assistant clerk.

Mr. OSE. I call to order today's hearing on the Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs. The subject of today's hearing is, "How to Improve Regulatory Accounting: Costs, Benefits, and Impacts of Federal Regulations—Part II."

In the fall of 2001, the Small Business Administration estimated that, in the year 2000, Americans spent $843 billion to comply with Federal regulations. SBA's report concluded, "Had every household received a bill for an equal share, each would have owed $8,164." The report also found that, in the business sector, those hit hardest by Federal regulations are small businesses. The report stated, "Firms employing fewer than 20 employees face an annual regulatory burden of $6,975 per employee, a burden nearly 60 percent above that facing a firm employing over 500 employees." It is clear that regulations add to business costs and decrease capital available for investment and job creation.

Because of congressional concern about the increasing costs and incompletely estimated benefits of Federal rules and paperwork, in 1996, Congress required the Office of Management and Budget [OMB], to submit its first regulatory accounting report. In 1998, Congress changed the report's due date to coincide with the President's budget so that Congress and the public could simultaneously review both the on-budget and off-budget costs associated with each Federal agency imposing burdens on the public. In the year 2000, Congress made this a permanent annual reporting requirement. The law requires OMB to estimate the total annual costs and benefits for all Federal rules and paperwork in the aggregate, by agency, by agency program, and by major rule, and to include an

associated report on the impacts of Federal rules and paperwork on certain groups, such as small business.

Today, we will examine OMB's draft seventh annual regulatory accounting report, which was released on February 13, 2004, which is 11 days after the statutory deadline of release with the President's budget. Unfortunately, this late submission prevented the congressional subcommittees from submitting fully informed recommendations for this year's budget resolution. We will again discuss how to improve compliance with the substantive statutory requirements.

Data by agency and by agency program are important for the public to know the aggregate costs and benefits associated with each agency and each major regulatory program. For example, what are the aggregate costs and benefits of the requirements imposed by the U.S. Department of Agriculture and the Labor Department's Occupational Health and Safety Administration? Is there an alternative approach for USDA or OSHA to more effectively, with less burden on and cost to the public, accomplish their intended objectives?

To date, OMB has issued six final and one draft regulatory accounting reports. All seven did not meet some or all of the statutorily required content requirements. However, OMB has progressively made improvements, such as adding agency level detail for eight agencies in March 2002, and adding agency program level detail for seven major regulatory programs in February 2003. Its just-issued draft report includes a thoughtful discussion of how Federal regulations affect the manufacturing sector. In addition, on September 17, 2003, OMB issued a new OMB Circular A–4 to standardize future agency cost-benefit analyses.

For the President's fiscal budget and OMB's Information Collection Budget, OMB tasks agencies annually with submitting budgetary and paperwork estimates, respectively, for each agency bureau and program. In contrast, for Federal regulations, OMB does not similarly task agencies annually with submitting cost-benefit estimates for each agency bureau and regulatory program. On June 11, 2003, I introduced the Paperwork and Regulatory Improvements Act, H.R. 2432. Section 6 of this bipartisan bill includes requirements to improve regulatory accounting, such as: requiring agencies to submit information, where available, for OMB's annual regulatory accounting statements; requiring the annual regulatory accounting statement and associated report to be submitted "as part of" the President's budget, compared to "with" the President's budget; and requiring OMB to conduct a multi-agency study of regulatory budgeting.

Presently, the huge off-budget expenditures, which truly are hidden taxes to comply with Federal regulations, receive much less scrutiny than proposed on-budget expenditures and the Federal deficit. Regulatory accounting is a useful way to improve the cost-effectiveness of government. Both Presidents Reagan and Clinton issued Executive orders requiring cost-benefit analyses so that policymakers could see the strengths and weaknesses of alternative approaches and could make choices to ensure that benefits to the public are maximized. I support these requirements and want to

make sure that the Government is doing everything it can to minimize the burden of regulations on the American public.

I look forward to the testimony of our witnesses.

[The prepared statement of Hon. Doug Ose follows:]

Opening Statement of Chairman Doug Ose
How to Improve Regulatory Accounting:
Costs, Benefits, and Impacts of Federal Regulations – Part II
February 25, 2004

In Fall 2001, the Small Business Administration (SBA) estimated that, in 2000, Americans spent $843 billion to comply with Federal regulations. SBA's report concluded, "Had every household received a bill for an equal share, each would have owed $8,164." The report also found that, in the business sector, those hit hardest by Federal regulations are small businesses. It stated, "Firms employing fewer than 20 employees face an annual regulatory burden of $6,975 per employee, a burden nearly 60 percent above that facing a firm employing over 500 employees." Regulations add to business costs and decrease capital available for investment and job creation.

Because of Congressional concern about the increasing costs and incompletely estimated benefits of Federal rules and paperwork, in 1996, Congress required the Office of Management and Budget (OMB) to submit its first regulatory accounting report. In 1998, Congress changed the report's due date to coincide with the President's Budget so that Congress and the public could simultaneously review both the on-budget and off-budget costs associated with each Federal agency imposing burdens on the public. In 2000, Congress made this a permanent annual reporting requirement. The law requires OMB to estimate the total annual costs and benefits for all Federal rules and paperwork in the aggregate, by agency, by agency program, and by major rule, and to include an associated report on the impacts of Federal rules and paperwork on certain groups, such as small business.

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Data by agency and by agency program are important for the public to know the aggregate costs and benefits associated with each agency and each major regulatory program. For example, what are the aggregate costs and benefits of the requirements imposed by the U.S. Department of Agriculture (USDA) and the Labor Department's Occupational Health and Safety Administration (OSHA)? Is there an alternative approach for USDA or OSHA to more effectively, with less burden on and cost to the public, accomplish their intended objectives?

To date, OMB has issued six final and one draft regulatory accounting reports. All seven did not meet some or all of the statutorily-required content requirements. However, OMB has progressively made improvements, such as adding agency level detail for eight agencies in March 2002, and adding agency program level detail for seven major regulatory programs in February 2003. And, its just-issued draft report includes a thoughtful discussion of how Federal regulations affect the manufacturing sector. In addition, on September 17, 2003, OMB issued a new OMB Circular A-4 to standardize future agency cost-benefit analyses.

For the President's fiscal Budget and OMB's Information Collection Budget (ICB), OMB tasks agencies annually with submitting budgetary and paperwork estimates, respectively, for each agency bureau and program. In contrast, for Federal regulations, OMB does not similarly task agencies annually with submitting cost-benefit estimates for each agency bureau and regulatory program. On June 11, 2003, I introduced the "Paperwork and Regulatory Improvements Act" (H.R. 2432). Section 6 of this bi-partisan bill includes requirements to improve regulatory accounting, such as: requiring agencies to submit information, where available, for OMB's annual regulatory accounting statements; requiring the annual regulatory accounting statement and associated report to be submitted "as part of" (versus "with") the President's Budget; and, requiring OMB to conduct a multi-agency study of regulatory budgeting.

Currently, the huge off-budget expenditures (these are hidden taxes) to comply with Federal regulations receive much less scrutiny than proposed on-budget expenditures and the Federal deficit. Regulatory accounting is a useful way to improve the cost-effectiveness of government. Both Presidents Reagan and Clinton issued executive orders requiring cost-benefit analyses so that policymakers could see the strengths and weaknesses of alternative approaches and could make choices to ensure that benefits to the public are maximized. I support these requirements and want to make sure that the Government is doing everything it can to minimize the burden of Federal regulations on the American public.

I look forward to the testimony of our witnesses. They include: Dr. John D. Graham, Administrator, Office of Information and Regulatory Affairs (OIRA), OMB; Thomas M. Sullivan, Chief Counsel for Advocacy, SBA; William Kovacs, Vice President, Environment, Technology and Regulatory Affairs, U.S. Chamber of Commerce; Susan Dudley, Director, Regulatory Studies Program, Mercatus Center, George Mason University; Dr. Richard B. Belzer, President, Regulatory Checkbook; Joan Claybrook, President, Public Citizen; and, Robert R.M. Verchick, Ruby M. Hulen Professor of Law, University of Missouri at Kansas City School of Law, representing the Center for Progressive Regulation.

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February 18, 2004

MEMORANDUM FOR MEMBERS OF THE SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS

FROM: Doug Ose

SUBJECT: Briefing Memorandum for February 25, 2004 Hearing, "How to Improve Regulatory Accounting: Costs, Benefits, and Impacts of Federal Regulations – Part II"

On Wednesday, February 25, 2004, at 10:00 a.m., in Room 2247 Rayburn House Office Building, the Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs will hold a hearing on the annual regulatory accounting statement and associated report required to be submitted with the President's Budget. The hearing is entitled, "How to Improve Regulatory Accounting: Costs, Benefits, and Impacts of Federal Regulations – Part II."

In 1996[1], Congress required the Office of Management and Budget (OMB) to submit its first regulatory accounting report by September 30, 1997. In 1997, Congress continued this requirement. In 1998, Congress changed the report's due date to coincide with the President's Budget. Congress established this simultaneous deadline so that Congress and the public could be given an opportunity to simultaneously review both the on-budget and off-budget costs associated with each Federal agency and each Federal agency program imposing regulatory or paperwork burdens on the public. Finally, in 2000, Congress made this a permanent annual reporting requirement. The law requires OMB to estimate the total annual costs and benefits for all Federal rules and paperwork in the aggregate, by agency, by agency program, and by major rule, and to include an associated report on the impacts of Federal rules and paperwork. The philosophy behind these laws was the belief that the public has the right to know the costs and benefits of Federal rules and paperwork and the right to open and accountable government.

[1]The requirements for OMB's regulatory accounting reports were enacted as: Sec. 645 of the Treasury, Postal Services and General Government Appropriations Act for 1997 (P.L. 104-208); Sec. 625 of the Treasury and General Government Appropriations Act for 1998 (P.L. 105-61); Sec. 638 of the 1999 Omnibus Consolidated and Emergency Supplemental Appropriations Act (P.L. 105-277); Sec. 628 of the Treasury and General Government Appropriations Act for 2000 (P.L. 106-58); and Sec. 624 of the Treasury and General Government Appropriations Act for 2001 (P.L. 106-554).

An October 2001 report, entitled "The Impact of Regulatory Costs on Small Firms," by Drs. W. Mark Crain and Thomas D. Hopkins, commissioned by the Small Business Administration's (SBA) Office of Advocacy, estimated that, in 2000, Americans spent $843 billion to comply with Federal regulations. These off-budget costs to Americans are on top of the costs reflected in the President's Budget. In September 2002, Dr. Crain co-authored a study entitled "Compliance Costs of Federal Workplace Regulations: Survey Results for U.S. Manufacturers." This paper revealed that, in 2000, manufacturers spent an average of $2.2 million per firm (or $1,700 per employee) to comply with Federal workplace regulations. Also, in September 2002, Dr. Joseph M. Johnson published a study entitled "A Review and Synthesis of the Costs of Workplace Regulation." This paper compiled available estimates of the costs of different workplace regulations, totaling at least $91 billion annually.

On March 12, 2002, this Subcommittee held a hearing entitled "Regulatory Accounting: Costs and Benefits of Federal Regulations." It was intended to be a hearing about the fifth report due February 4th; however, OMB did not publish its draft report until after the hearing (i.e., on March 18th). On March 11, 2003, this Subcommittee held a hearing entitled "How to Improve Regulatory Accounting: Costs, Benefits, and Impacts of Federal Regulations." It considered the draft sixth report that was published on February 3rd, the same day as release of the President's Fiscal Year (FY) 2004 Budget. Unfortunately, it was not part of the various Budget documents; instead, it was published in the Federal Register on the same day as release of the Budget. This approach was not particularly useful to the Government Reform, Budget and Appropriations Committees since it prevented a side-by-side comparison for analytic purposes of the on-budget and off-budget costs associated with each major regulatory agency (e.g., Department of Labor (DOL)) and each of its regulatory programs (e.g., DOL's Occupational Safety and Health Administration (OSHA)).

This year, OMB missed the statutory deadline for simultaneous reporting with the February 2, 2004 release of the FY 2005 Budget[2]. As a consequence, in their Views and Estimates on the FY 2005 Budget for the Budget Committees, Congressional Subcommittees, including this Subcommittee, were unable to analyze the full impact of the President's Budget for the major regulatory agencies and their programs.

To date, OMB has issued six final regulatory accounting reports - in September 1997, January 1999 (dated 1998), June 2000, December 2001, December 2002, and September 2003 (see attached chart). All six did not meet some or all of the statutorily-required content requirements. For example, all six were not presented as an accounting statement and both the February draft and September final 2003 reports did not include the required associated report on impacts, e.g., on small business.

The Subcommittee annually submits comments both on OMB's draft and final reports. However, in its September 2003 final report, OMB did not include the Subcommittee as a commenter and, thus, did not respond to many of the March 18, 2003 comments submitted by

[2] On February 13, 2004, OMB released its draft report but it has not yet been published in the Federal Register.

this Subcommittee. After release of the final report, the Subcommittee submitted September 25th comments. In addition, the Schrock-chaired Small Business Subcommittee submitted October 24th comments on resources that OMB can use to include a full impacts report on small business in its future reports, starting with the report due February 2, 2004.

Partially in response to this Subcommittee's oversight hearings and comment letters, OMB has progressively made improvements, such as adding agency level detail for eight agencies in March 2002, and adding agency program level detail for seven major regulatory programs in February 2003. For the Budget and for paperwork reduction, OMB requires agencies to annually provide detail by agency program. In March 2002, I wrote OMB stating, "To assist OMB in preparing estimates by agency and by agency program, I recommend that OMB issue annual OMB Bulletins to the agencies like it does for paperwork reduction. ... OMB's regulatory accounting Bulletins should require each agency to submit estimates of its aggregate and new regulatory burden for the agency as a whole and for each of the agency's major regulatory programs." To date, OMB has not done so.

In response to the Subcommittee's March 2002 and March 2003 hearings, on June 11, 2003, I introduced the "Paperwork and Regulatory Improvements Act" (H.R. 2432), a bi-partisan bill to increase the probability of results in paperwork reduction, assist Congress in its review of agency regulatory proposals, and improve regulatory accounting. Section 6 of the bill includes requirements to improve regulatory accounting, such as: requiring agencies to submit information, where available, for OMB's annual regulatory accounting statements; requiring the annual regulatory accounting statement and associated report to be submitted "as part of" the President's Budget; and, requiring OMB to conduct a multi-agency study of regulatory budgeting.

In January 1996, OMB issued "Best Practices Guidances" to help standardize agency cost-benefit analyses of significant regulatory actions, as required by President Clinton's regulatory reviews Executive Order (E.O.) 12866. However, since it was in the form of nonbinding guidance to the agencies instead of requirements for agencies to follow, such as those in an OMB Circular, OMB did not enforce agency compliance. The result was that agency practices continued to substantially deviate from OMB's guidance, with some agencies not even estimating costs or benefits. In February 2003, OMB proposed a new OMB Circular A-4, "Regulatory Analysis," which was finalized on September 17, 2003. It should greatly improve the quality and consistency of agency cost-benefit analyses. In addition, it includes a helpful discussion of alternative regulatory approaches, including: different choices defined by statute, different compliance dates, different enforcement methods, different degrees of stringency, different requirements for different sized firms, different requirements for different geographic regions, performance standards rather than design standards, market-oriented approaches rather than direct controls, and informational measures rather than regulation (pp. 7-9).

The invited witnesses for the February 25, 2004 hearing are: Dr. John D. Graham, Administrator, Office of Information and Regulatory Affairs (OIRA), OMB; Thomas M.

Sullivan, Chief Counsel for Advocacy, SBA; William Kovacs, Vice President, Environment, Technology and Regulatory Affairs, U.S. Chamber of Commerce; Susan Dudley, Director, Regulatory Studies Program, Mercatus Center, George Mason University; Dr. Richard B. Belzer, President, Regulatory Checkbook; and, Joan Claybrook, President, Public Citizen.

Attachment

Laws Requiring Regulatory Accounting Reports and OMB Issuances

Date of Law	Due Date for OMB Report	Date of OMB Report	Required Content for OMB
9/30/96	9/30/97	9/97	(1) annual costs & benefits of Federal regulatory programs & of each major rule (2) impacts on private sector & State/locals (3) recommendations to reform/eliminate
10/10/97	9/30/98	1/99	same as prior year
10/21/98	with the President's Budget (2/7/00)	6/00	(1) accounting statement with annual costs & benefits of Federal rules & paperwork in the aggregate, by agency & agency program, & by major rule (2) associated report with impacts on small business, State/locals, etc. (3) recommendations for reform also: (4) OMB guidelines to agencies to standardize cost/benefit measures & format of accounting statements
9/29/99	with the Budget (4/9/01)	12/21/01	same as prior year
12/21/00	permanently with the Budget (2/4/02)	draft 3/18/02 final 12/18/02	same as prior year
	with the Budget (2/3/03)	draft 2/3/03 final 9/22/03	same as prior year
	with the Budget (2/2/04)	draft 2/13/04	same as prior year

Prepared for Congressman Doug Ose

Progress in OMB's Regulatory Accounting Reports

DEPARTMENT/AGENCY	Date Started	Agency PROGRAM	Date Started
Agriculture	3/02		
Commerce			
Defense			
Education	3/02		
Energy	3/02	Energy Efficiency & Renewable Energy	2/03
		All Other DOE	
Health & Human Services	3/02	FDA	2/03
		All Other HHS	
Homeland Security	2/04		
Housing & Urban Development	3/02		
Interior			
Justice			
Labor	3/02	OSHA	2/03
		All Other DOL	
State			
Transportation	3/02	NHTSA	2/03
		Coast Guard (now in Homeland Security)	*2/03 but removed 2/04*
		All Other DOT	
Treasury			
Veterans Affairs			
EPA	3/02	Office of Air	2/03
		Office of Water	2/03
		All Other EPA	
Independent Regulatory Commissions			
rest of Government			

Single Squiggle = Missing information from OMB's reports

Double Squiggles = Only Agency Program information in OMB's report, i.e., all other Agency Program information is missing (e.g., HHS's Centers for Medicare and Medicaid Services, and Treasury's IRS)

Prepared for Congressman Doug Ose

Mr. OSE. I am pleased to recognize my good friend from Virginia, Mr. Schrock, for the purpose of an opening statement.

Mr. SCHROCK. Thank you, Mr. Chairman. I have no opening statement. I am just looking forward to the testimony of Mr. Sullivan, among others, and to asking several questions I hope will clear up some issues. Thank you.

Mr. OSE. All right, apparently there is a long line to get into Rayburn this morning, and we are concerned that Dr. Graham may be caught in that line. We are going to proceed at pace with Mr. Sullivan's testimony and subsequent witnesses, as time permits.

Our typical practice here is to swear in all of our witnesses. We are not picking on anybody, that is just what we do here. So, Mr. Sullivan, if you would please rise.

[Witness sworn.]

Mr. OSE. Please let the record show the witness answered in the affirmative.

Joining us today, our first witness today, Mr. Tom Sullivan, who is the Chief Counsel for Advocacy at the Small Business Administration.

Mr. Sullivan, you are recognized for 5 minutes for the purpose of an opening statement.

STATEMENTS OF THOMAS M. SULLIVAN, CHIEF COUNSEL FOR ADVOCACY, SMALL BUSINESS ADMINISTRATION; AND JOHN D. GRAHAM, ADMINISTRATOR, OFFICE OF INFORMATION AND REGULATORY AFFAIRS, OFFICE OF MANAGEMENT AND BUDGET

Mr. SULLIVAN. Thank you, Chairman Ose, Congressman Schrock. Good morning and thank you for giving me the opportunity to appear before you this morning. My name is Tom Sullivan, joined by Dr. John Graham, Administrator of OIRA. I am the Chief Counsel for Advocacy at the U.S. Small Business Administration. The Office of Advocacy is an independent office within SBA, and, therefore, the comments expressed in this statement do not necessarily reflect the position of the administration or the SBA.

With the Chair's permission, I would like to submit my entire written statement for the record, but briefly summarize it under 5 minutes.

Mr. OSE. Without objection.

Mr. SULLIVAN. In general, Advocacy believes that improving regulatory analysis to delineate small business impacts, together with greater overall adherence to regulatory accounting requirements, will allow OMB to develop more comprehensive reports to Congress.

While the draft OMB report recognizes the importance of the regulatory burden on small business, it does not attempt to quantify the impact of that burden beyond citing my office's sponsored Crain-Hopkins study in 2001. That study found that small businesses pay a disproportionately large share of the total Federal regulatory burden, which was estimated to total $843 billion in 2000. For firms employing fewer than 20 employees, the annual regulatory burden in 2000 was estimated to be just under $7,000 per employee, nearly 60 percent higher than the burden for firms with more than 500 employees.

The draft OMB report would benefit from impact analyses that, at a minimum, should accompany all major rules reviewed by OIRA. From the Office of Advocacy's perspective, the draft OMB report would also benefit from small business impact analyses that should be prepared for rules reviewed by OIRA.

My office believes that the recently issued Circular A–4, entitled "Regulatory Analysis," will go a long way to improve regulatory accounting. The OMB circular includes a section calling on Federal agencies to identify the effects of rules on small businesses, and the regulatory accounting worksheet that accompanies the circular has a section for agencies to list the impacts of their rules on small business. The circular became effective just this past January, so, at this hearing next year, we will have an opportunity for us to see if the circular works.

While Advocacy would have preferred to see a quantitative analysis of the regulatory impacts on small business in the draft OMB report, I would be remiss if I did not commend Dr. Graham and our colleagues in OIRA for their daily efforts to ensure agencies' compliance with the Regulatory Flexibility Act through aggressive interagency review of proposed regulations.

My office recommends that OMB issue return letters on a rule-by-rule basis to enforce agency compliance with Executive Order 12866, the Regulatory Flexibility Act, Executive Order 13272, and the recently issued OMB Circular A–4.

Last year, my office endorsed H.R. 2432, the Paperwork and Regulatory Improvement Act of 2003. Small business groups continue to tell me that the legislation would improve agencies' attention and sensitivity to how regulatory mandates impact the small business community. For that reason, the Office of Advocacy continues to support the legislation.

Advocacy believes that improving the regulatory analysis of small business impacts, together with greater adherence to regulatory accounting requirements in general, will greatly improve the quality and transparency of economic analyses provided to OMB and will, in turn, allow Dr. Graham's office to develop more comprehensive reports to Congress.

Thank you for allowing me to present these views, and I am happy to answer any questions.

[The prepared statement of Mr. Sullivan follows:]

A Voice for Small Business

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Testimony of
Thomas M. Sullivan
Chief Counsel for Advocacy
U.S. Small Business Administration

U.S. House of Representatives
Committee on Government Reform
Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs

Date:	February 25, 2004
Time:	10:00 A.M.
Location:	Room 2247 Rayburn House Office Building Washington, D.C.
Topic:	"How to Improve Regulatory Accounting: Costs, Benefits, and Impacts of Federal Regulations – Part II"

Created by Congress in 1976, the Office of Advocacy of the U.S. Small Business Administration (SBA) is an independent voice for small business within the federal government. The Chief Counsel for Advocacy, who is appointed by the President and confirmed by the U.S. Senate, directs the office. The Chief Counsel advances the views, concerns, and interests of small business before Congress, the White House, federal agencies, federal courts, and state policy makers. Issues are identified through economic research, policy analyses, and small business outreach. The Chief Counsel's efforts are supported by offices in Washington, D.C., and by Regional Advocates. For more information about the Office of Advocacy, visit http://www.sba.gov/advo, *or call (202) 205-6533.*

Chairman Ose and Members of the Subcommittee, good morning and thank you for giving me the opportunity to appear before you today. My name is Thomas M. Sullivan and I am the Chief Counsel for Advocacy at the U.S. Small Business Administration (SBA). Congress established the Office of Advocacy to represent the views of small business before Federal agencies and Congress. The Office of Advocacy is an independent office within the SBA, and therefore the comments expressed in this statement do not necessarily reflect the position of the Administration or the SBA.

Section 624 of the FY 2001 Treasury and General Government Appropriations Act, which was enacted as part of Pub. L.106-554, (referred to as the "Regulatory Right-to-Know Act"), directs the Office of Management and Budget (OMB) to quantify annually the costs and benefits of Federal regulations and to prepare a Report to Congress summarizing the results. Among other things, the Report to Congress is to include an analysis of the impacts of Federal regulations on small business. On February 13, 2004, OMB released the draft Report to Congress, entitled *Informing Regulatory Decisions: 2004 Draft Report to Congress on the Costs and Benefits of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities* (Draft OMB Report).

The Subcommittee asked that I provide the Office of Advocacy's assessment of the Draft OMB Report. Specifically, the Subcommittee requested Advocacy's views on (1) the adequacy of the Report's regulatory accounting statement, by agency and program, (2) the adequacy of the Report's analysis of the impacts of Federal regulations on specifically-identified groups, including small businesses, and (3) recommendations for improving future reports to Congress.

The Office of Advocacy's review of the Draft OMB Report has focused primarily on the treatment of small business impacts. Consequently, my comments on the overall report are couched in terms of the adequacy of the Draft OMB Report's discussion of regulatory impacts on small businesses and recommendations to help ensure that future reports quantify these impacts. My testimony today should be considered in conjunction with the comments and recommendations I provided to the Committee on Government Reform last year on regulatory accounting and OMB's Reports to Congress.[1]

In general, Advocacy believes that improving the regulatory analysis to delineate small business impacts, together with greater overall adherence to regulatory accounting requirements, will greatly improve the quality and transparency of the economic analyses provided to OMB under Executive Order 12866,[2] and will in turn allow OMB to develop more comprehensive Reports to Congress.

The Impact of Federal Regulation on Small Business.

The Draft OMB Report provides a general overview of the impact of Federal regulations on small entities without specifically quantifying those impacts. The Draft OMB Report acknowledges that Federal agencies need to recognize the impact of their regulations and paperwork burdens on small businesses, and lists the statutes and Executive Orders intended to require considerations of those impacts. The Regulatory Flexibility Act (RFA),[3] as amended by the Small Business Regulatory Enforcement

[1] Testimony of Thomas M. Sullivan, Chief Counsel for Advocacy, U.S. Small Business Administration, before the U.S. House of Representatives, Committee on Government Reform, July 22, 2003, on H.R. 2432, the "Paperwork and Regulatory Improvements Act of 2003," available at http://www.sba.gov/advo/laws/test03_0722.html.
[2] Exec. Order No. 12,866, 58 Fed. Reg. 51,735 (Sept. 30, 1993).
[3] Pub. Law No. 96-354, 94 Stat. 1164 (1980) *codified at* 5 U.S.C. § 601 *et seq.*

Fairness Act of 1996 (SBREFA),[4] Executive Order 12866, and Executive Order 13272[5] each call on agencies to tailor their regulations by business size to impose less burden while achieving regulatory objectives.

While the Draft OMB Report recognizes the importance of the regulatory burden on small business, it does not attempt to quantify the impact of that burden, beyond citing the 2001 Office of Advocacy-sponsored Crain-Hopkins study. The Crain-Hopkins study found that small businesses pay a disproportionately large share of the total Federal regulatory burden, which was estimated to total $843 billion in 2000.[6] For firms employing fewer than 20 employees, the annual regulatory burden in 2000 was estimated to be $6,975 per employee – nearly 60% higher than the $4,463 estimated for firms with more than 500 employees.[7]

To help address this disproportionate impact, the RFA, which was enacted in 1980, requires Federal regulatory agencies to determine the impact of their rules on small businesses, consider effective alternatives that minimize adverse impacts, and make their analysis available for public comment. The RFA was strengthened by SBREFA in 1996, and by Executive Order 13272 in August 2002. Executive Order 13272 requires agencies to establish written procedures and policies on how they consider the impact of their regulatory proposals on small businesses, notify Advocacy of draft rules that are expected to have a significant economic impact on a substantial number of small entities, consider Advocacy's comments on draft rules, and publish a response to Advocacy's comments in the final rule.

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[4] Pub. Law No. 104-121, 110 Stat. 857 (1996) *codified at* 5 U.S.C. § 601 *et seq.*
[5] Exec. Order No. 13,272, 67 Fed. Reg. 53,461 (Aug. 13, 2002).
[6] See *The Impact of Regulatory Costs on Small Firms*, an Advocacy-funded study by W. Mark Crain and Thomas D. Hopkins (October 2001), available at http://www.sba.gov/advo/research/rs207tot.pdf.
[7] *Id.*

As referenced in the Draft OMB Report, Advocacy's recently released its *Report on the Regulatory Flexibility Act, FY 2003* (FY 2003 RFA Report) in January 2004.[8] The FY 2003 RFA Report highlights those agencies that have successfully evaluated their draft rules' impacts on small businesses and have adopted less burdensome alternatives. These less burdensome alternatives saved small business more than $6 billion in 2003. Unfortunately, some agencies continue to fail to conduct small business impact analyses. The FY 2003 RFA Report documents agencies that do not comply with the RFA. Those agencies' failure to conduct an impact analysis when proposing new rules and regulations makes it nearly impossible to get an accurate picture of the true impact of their regulatory actions.

The Draft OMB Report does not attempt to quantify, on an annual basis, what the impact of Federal regulation actually is on small business. I suspect that OMB's Office of Information and Regulatory Affairs (OIRA) receives some rules from agencies accompanied by good economic analysis and some without. The Draft OMB Report would benefit from impact analyses that, at a minimum, should accompany all major rules reviewed by OIRA (e.g., rules expected to impose over $100 million in annual costs). From the Office of Advocacy's perspective, the Draft OMB Report would also benefit from *small business* impact analyses that should be prepared for rules reviewed by OIRA.

While Advocacy would have preferred to see a quantitative analysis of the regulatory impacts on small business in the Draft OMB Report, I would be remiss if I did not commend Dr. Graham and our colleagues in OIRA for their daily efforts to ensure

[8] Office of Advocacy, *Report on the Regulatory Flexibility Act, FY 2003, The Annual Report of the Chief Counsel for Advocacy on Implementation of the Regulatory Flexibility Act and Executive Order 13272* (January 2004), available on the Office of Advocacy webpage, http://www.sba.gov/advo.

agencies' compliance with the Regulatory Flexibility Act through interagency review of proposed regulations.

On March 19, 2002, the President announced his Small Business Agenda, which included the goal of "tearing down the regulatory barriers to job creation for small businesses and giv[ing] small business owners a voice in the complex and confusing federal regulatory process."[9] To accomplish this goal, the President sought to strengthen the Office of Advocacy by enhancing its relationship with OIRA and directing agencies to work closely with Advocacy and properly consider the impact of their regulations on small entities pursuant to Executive Order 13272. Advocacy and OIRA signed a Memorandum of Understanding (MOU) to ensure the two offices work closely together as early as possible in the regulation development process to address small business issues, particularly as they relate to disproportionate regulatory burden.[10] Together, the two offices are able to work with Federal agencies to make improvements in their impacts analyses, help ensure that small business issues are addressed and, where possible, ease regulatory burdens. With a focus on information sharing between Advocacy and OIRA during interagency review of draft rules under Executive Order 12866, the two offices work collaboratively to address small business concerns early in the rulemaking process. Much of our success in making Federal agencies more accountable to small entities, as documented in the 2003 RFA Annual Report, is due to our close working relationship with OIRA.

Furthermore, OMB has been responsive to Advocacy's past recommendations aimed at improving agencies' cost-benefit data and the analysis of regulatory impacts on

[9] President Bush's Small Business Agenda, announced March 19, 2002, can be viewed at http://www.whitehouse.gov/infocus/smallbusiness/regulatory.html.
[10] The Memorandum of Understanding can be viewed at http://www.sba.gov/advo/laws/law_mou02.pdf.

small businesses. Advocacy believes OMB's recently issued Circular A-4, "Regulatory Analysis,"[11] will go a long way to improve agency compliance with Executive Order 12866. Better cost-benefit analysis will also enable OMB to issue more comprehensive Reports to Congress. OMB Circular A-4 includes a section calling on Federal agencies to identify the effects of rules on small businesses, wages, and economic growth. The accompanying Regulatory Accounting worksheet has a section for agencies to list the impacts of their rules on small businesses, wages, and economic growth. The Circular became effective on January 1, 2004, so increased agency identification of impacts was not included in the Draft OMB Report. We encourage OMB to use its return letter authority to enforce agency compliance with Circular A-4, including use of a Regulatory Accounting Statement that includes quantification of the impacts on small business, wages, and economic growth.

Advocacy is also pleased that OMB called for nominations for promising regulatory reforms to address the regulatory burden confronting manufacturers and to reduce the overall tax paperwork burden. Prior nominations evaluated by OMB are prompting ongoing revisions to regulations that are likely to reduce the regulatory burden borne by small businesses, including small manufacturers. The U.S. Environmental Protection Agency (EPA), for example, has announced that it is now considering revising paperwork requirements for businesses that must file annual Toxic Release Inventory reports, while still providing significant environmental information to the public. Advocacy believes that such regulatory reforms could be effective in reducing the regulatory burden on small business, particularly in the manufacturing sector.

[11] OMB Circular A-4, Regulatory Analysis (Sept. 17, 2003), can be viewed at http://www.whitehouse.gov/omb/circulars/a004/a-4.pdf.

The Regulatory Accounting Statement.

The Draft OMB Report includes a regulatory accounting statement, as required by the Regulatory Right-to-Know Act. Unfortunately, as has been the case in prior years, the Draft OMB Report's regulatory accounting statement reflects major gaps in the cost and benefit information received from the Federal agencies. Agencies that promulgated six of the twelve major new "social regulations" reviewed by OIRA in 2003 – rules that are anticipated to provide societal benefits while imposing at least $100 million in new costs upon regulated entities each year – provided no information about the cost or benefits of their rules.

For example, the Health and Human Services' Center for Medicare and Medicaid Services (CMS) adopted new standards for the security of health information under the Health Insurance Portability and Accountability Act of 1996. The standards impose new paperwork management requirements on health care plans, doctors, and other health care providers. Although CMS acknowledged that the standards would cost these entities more than $100 million in compliance costs annually, the agency failed to estimate the costs and benefits of the standards for OMB.

Likewise, the U.S. Department of Agriculture's Agricultural Marketing Service (AMS) issued revised price formulae for butterfat, protein, and nonfat solids used in milk, cheese, and butter. Although the changes are estimated to impose at least $100 million in new costs, AMS provided no estimates of the costs or benefits of the action to OMB.

Agencies' failure to provide data on the costs and benefits of their rules potentially harms OMB's ability to abide by the Regulatory Right-to-Know Act, and it

Congressional oversight is also tremendously helpful. This hearing sends a message to agencies that analysis does matter. The Paperwork and Regulatory Improvements Act of 2003 would compel Federal agencies to analyze the impacts of their regulations on small businesses and state and local governments. This would help identify whether the costs imposed on small firms by regulations are justified by their benefits. If cost and benefit estimates are required for small entities on regulatory accounting statements, small business considerations would figure more prominently in agencies' regulatory calculus.

Recommendations for Improving OMB's Future Reports to Congress.

Increased Use of OMB Return Letters.

Advocacy strongly recommends that OMB issue return letters on a rule-by-rule basis to enforce agency compliance with the Executive Order 12866 and OMB Circular A-4. We note that former OMB Director Mitch Daniels advised this Committee on March 24, 2001, that OMB would issue return letters to enforce agency compliance with the Unfunded Mandates Reform Act of 1995, Pub. L. 104-4. Advocacy believes that return letters should be issued to agencies that do not follow OMB's Circular and Bulletin(s) on accounting for regulatory impacts imposed on small entities.

Improved Regulatory Accounting.

H.R. 2432 would amend the Regulatory Right-to-Know Act to require (1) agencies to submit annual estimates to OMB of the costs and benefits of their regulations and paperwork requirements, (2) OMB in turn to develop regulatory accounting

also contravenes Executive Order 12866, which requires this information to be provided pursuant to OIRA's review of major rules. Moreover, agencies' failure to provide regulatory accounting information makes rules far less transparent to the public. Small entities are particularly affected when agencies ignore Executive Order 12866 requirements, since a lack of impact analysis means that agencies are unlikely to satisfy the regulatory flexibility analysis required under the Regulatory Flexibility Act and Executive Order 13272.

While my testimony focuses on ways to better achieve the goals of the Regulatory Right-to-Know Act, I should also acknowledge the efforts that are underway within the Administration to accomplish the Act's objectives. Every two years the Office of Advocacy produces a study on the impact of federal regulations on small businesses. The 2001 Crain-Hopkins study[12] is being updated and will be published later this year. Second, Advocacy's RFA Annual Reports commend agencies for leadership and shames others for noncompliance. The U.S. Department of Commerce's recently released report, *Manufacturing in America*,[13] highlights the need for cost-benefit and regulatory impact analysis that will be part of the Department of Commerce's new Assistant Secretary for Manufacturing and Services' responsibilities. OMB has returned rules to agencies when regulatory action is poorly justified. And the recently issued OMB Circular A-4 has significant potential to help address the deficiency in obtaining regulatory impact data.

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[12] *The Impact of Regulatory Costs on Small Firms*, an Advocacy-funded study by W. Mark Crain and Thomas D. Hopkins (October 2001).

[13] U.S. Department of Commerce, *Manufacturing in America: A Comprehensive Strategy to Address the Challenges to U.S. Manufacturing* (January 2004).

statements, and (3) five agencies to undertake pilot projects to conduct regulatory budgeting. Advocacy recommends that the bill also require agency submissions to OMB (and OMB's corresponding accounting statements) identify and analyze regulatory impacts on small entities, consistent with the impact analysis required under the current regulatory accounting law.

Conclusion.

Advocacy believes that improving the regulatory analysis of small business impacts, together with greater adherence to regulatory accounting requirements in general, will greatly improve the quality and transparency of the economic analyses provided to OMB under Executive Order 12866, and will in turn allow OMB to develop more comprehensive Reports to Congress.

Thank you for allowing me to present these views. I would be happy to answer any questions.

Mr. OSE. I appreciate the gentleman offering his comments, and I want to remind him that some of us might not be here next January, but we will be watching from the small business side of the table.

Now, Dr. Graham, thank you for making it. I understand you had to hoof it up here. We went ahead and swore in Mr. Sullivan, so let us repeat that.

[Witness sworn.]

Mr. OSE. Let the record show that Dr. Graham answered in the affirmative.

We are pleased to have join us on this first panel Dr. John Graham, who is the Administrator of the Office of Information and Regulatory Affairs at the Office of Management and Budget.

Dr. Graham, we have received your written testimony. We invite you to utilize 5 minutes for the purpose of making this statement.

Mr. GRAHAM. Thank you, Mr. Chairman. Good morning, and I look forward to offering a few comments of overview on the draft report, which, as you know, is now out for public comment, agency comment, and expert peer review.

The first point I would like to highlight in the report is good news about progress in this administration on slowing the rate of growth of regulatory burdens. Some of the key data in the 2004 draft report on this subject are quite interesting. If you look at the overall magnitude of unfunded mandates on the private sector and State and local governments, this report tracks them all the way back to 1987 for the first time. If you look at an annual average of the new regulatory burdens each year from 1987 until the year 2000, they were accumulating at a rate of $6 billion in additional unfunded mandates per year. You can think of that on a decade basis. It means each decade we are adding $60 billion of additional unfunded mandates on the private sector and State and local governments.

We are pleased to report to you, Mr. Chairman, that in the first 3 years of the Bush administration, we have cut that growth of about $6 billion a year to $1.6 billion per year, roughly a 70 to 80 percent decline in the rate of growth.

Having said that, I have two cautionary remarks. One is that the 4th year of most administrations tends to be the worst year with regard to growth of regulatory burdens. In the eighth year of the Clinton administration, that number was $13 billion. We are all familiar with a lot of the midnight regulations that occurred in that last year.

The second point is that we have to ask ourselves why do we only talk about the rate of growth of regulation? Why can't we ever actually cause a reduction in regulatory burden? I have to acknowledge to you that the progress we are making is only on reducing the rate of growth. I particularly want to thank Tom Sullivan and his colleagues because they have joined us in a variety of rulemakings to make sure that this rate of growth is as small as possible.

Now, a person might ask why do we have to have any growth in regulatory burden? Why, Dr. Graham, don't you just put a moratorium on all new regulations? The answers are found in the report that is available for the committee to review. The answer is some

regulations are beneficial. Indeed, they are so beneficial that we have made a judgment that their benefits justify their burdens.

For example, the Food and Drug Administration has mandated that food labels contain information on the trans-fat content of the food, not just the saturated fat content, because growing scientific evidence indicates that trans-fat content is linked to coronary heart disease. The benefits of this rule are estimated on a ratio of 10 to 1 to costs. Another example is the U.S. Department of Agriculture in the control of Listeria in red meat and poultry products, with a benefit-cost ratio on the order of 8 to 1. We need to have a smart regulation approach, recognizing that there are cases when we need regulation, we should provide it, but always at the lowest cost necessary to achieve congressional objectives.

The second major point of this report is we have begun the review of the sea of existing regulations. Since 1980, 4,000 per year have been adopted. Over 20 years, that is 80,000 new regulations have been adopted. I must acknowledge to you most of them have been never looked at to determine whether they were beneficial or whether they were cost-effective. We have, this year, taken a very modest step by simply picking a single sector of the American economy, the manufacturing sector, and asked for public nominations of specific rules, guidance documents, or paperwork requirements that could result in more cost-effective regulation of manufacturing companies.

Why did we choose the manufacturing sector for particular focus? No. 1, the SBA report that Mr. Sullivan mentioned—The Crain and Hopkins 2001 Report—has quantified the fact that the manufacturing sector is subject to higher overall burdens than other sectors in the American economy. And, second of all, we are all aware that the manufacturing sector has been one of the slowest to come back in the economic recovery, struggling to join other sectors in growth, jobs, earnings, and so forth. We feel there is ample rationale for this focus on streamlining regulation in the manufacturing sector.

The final point I would like to make in the area of good news is the studies from the World Bank and the OECD that we reviewed in this report. They looked at over 130 countries throughout the world, in terms of the extent of their regulatory burden, and they have found that those countries that are the least regulated, Australia, Canada, the Netherlands, New Zealand, Singapore, and the United States, are characterized by more prosperity, more life expectancy, better health, and overall improved economic performance. In the underlying reasoning process, these studies point to a simple fact: least regulated countries find it is easier for people to start a new business, to hire workers, to enforce contracts, and to get credit.

The United States of America is a small business-friendly country. That is why we are prosperous, that is why the economy is on the mend, and that is why we are here to streamline the regulatory process.

Thank you very much.

[The prepared statement of Mr. Graham follows:]

STATEMENT OF
JOHN D. GRAHAM, PH.D.
ADMINISTRATOR,
OFFICE OF INFORMATION AND REGULATORY AFFAIRS
BEFORE THE
SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES
AND REGULATORY AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

February 25, 2003

Mr. Chairman, and Members of this Subcommittee, thank you for inviting me to this hearing. I am John D. Graham, Ph.D., Administrator, Office of Information and Regulatory Affairs, Office of Management and Budget. Prior to joining the Bush Administration, I served as a faculty member at the Harvard School of Public Health, where I founded and directed the Harvard Center for Risk Analysis.

Since I testified last year before this subcommittee, our office has been working to improve the regulatory review process and to produce the reports to Congress required under the Regulatory Right to Know Act[1], which is the focus of this hearing.

As you know the Regulatory Right-to-Know Act, also known as the Regulatory Accounting Act, requires that:

a) For calendar year 2002 and each year thereafter, the Director of the Office of Management and Budget shall prepare and submit to Congress, with the budget, an accounting statement and associated report containing:

1) an estimate of the total annual costs and benefits (including quantifiable and nonquantifiable effects) of Federal rules and paperwork, to the extent feasible
   (A) in the aggregate;
   (B) by agency and agency program; and
   (C) by major rule;

2) an analysis of impacts of Federal regulation on State, local, and tribal government, small business, wages, and economic growth; and

3) recommendations for reform.

(b) The Director of the Office of Management and Budget shall provide public notice and an opportunity to comment on the statement and report under subsection (a) before the statement and report are submitted to Congress.

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[1] Section 624 of the Treasury and General Government Appropriations Act, 2001, 31 U.S.C. ' 1105 note, Pub. L. 106-554, '1(a)(3) [Title VI, ' 624], Dec. 21, 2000, 114 Stat. 2763, 2763A-161.

(c) To implement this section, the Director of the Office of Management and Budget shall issue guidelines to agencies to standardize

1) measures of costs and benefits; and
2) the format of accounting statements.

(d) The Director of the Office of Management and Budget shall provide for independent and external peer review of the guidelines and each accounting statement and associated report under this section.

Today I would like to report on the progress we have made in providing the Congress and the public with the regulatory information and accounting statements required by the Act. We released the 2004 draft report for comment and peer review on February 13, 2004, and published a notice of availability in the Federal Register on February 20, 2004. Since I last testified before this committee on the issue of regulatory accounting, we also released, in September, 2003, the 2003 final report. These two reports, which devote significant attention to regulatory accounting, are the focus of my testimony.

OMB's 2003 Final Report to Congress

We released the final version of our sixth report to Congress in September 2003. The report expands considerably upon earlier reports, particularly in the area of regulatory accounting. The report presents estimates for the first time of the costs and benefits of major regulations reviewed by OMB between October 1, 1992, and March 31, 1995. With the addition of costs and benefits from rules issued during fiscal year 2002, the report contained estimates for all major rules issued between October 1, 1992, and September 30, 2002. Overall, the annual quantifiable benefits of major rules issued during this period were estimated to range between $146 billion and $231 billion, with their quantifiable costs ranging between $37 billion and $43 billion. Information on the nonquantifiable benefits and costs for all major regulations issued during this ten-year period is found for the individual regulations in the appropriate annual report.

For the first time, the report also describes the costs and benefits over a ten-year period for eight cabinet departments and several agencies and programs. Most notably, the report indicates that the Clean Air Program in the Environmental Protection Agency's Office of Air and Radiation accounts for the majority of regulatory benefits over the past decade (between $118 billion and $177 billion).

The report also updates the status of the 23 high-priority rules OMB suggested for reform in 2001, based on suggestions we received from commenters regarding 71 regulations involving 17 agencies. Many of these changes would afford regulatory reform to businesses, and small businesses in particular. Agencies have already taken action on a number of these suggestions. For example, the Department of Transportation issued a final rule this past year reforming the Hours of Service of Truck Drivers, which was the nominated for reform in both 2001 and 2002. In addition, the Department of Labor

issued a proposed rule reforming the Overtime Compensation Regulations under the Fair Labor Standards Act, changes which Labor concludes are necessary for the rule to remain relevant and useful for tomorrow's workplace.

The report also contains our Final Guidelines for the Conduct of Regulatory Analysis and the Format of Accounting Statements, which was also released as OMB Circular A-4. After first proposing the guidelines in the 2003 draft report, in collaboration with the President's Council of Economic Advisors, OMB revised them based on substantial public comments and peer review. We also convened a group of agency experts and practitioners to review and offer suggestions to improve the guidelines. The final guidelines are designed to help analysts in the regulatory agencies by encouraging good regulatory impact analysis and standardizing the way that benefits and costs of Federal regulations are measured and reported. The new guidelines went into effect on January 1, 2004, for economically significant proposed rules, and will become effective on January 1, 2005, for economically significant final rules.

The 2003 final report also followed up on our solicitation of public comment on 1) how federal agencies are currently assessing and managing emerging risks to human health, safety, and the environment, particularly those risks that are subject to substantial scientific uncertainty; and 2) how agencies could improve the analysis of the benefits and costs of homeland security proposals.

OMB's 2004 Draft Report to Congress.

OMB released the 2004 draft report on February 13, 2004. It revises the benefit-cost estimates in last year's report by updating the estimates to the end of fiscal year 2003. Like the 2003 report, it uses a ten-year look-back: major federal regulations cleared by OMB from October 1, 1993, to September 30, 2003, were examined to determine their quantifiable benefits and costs. The estimated annual benefits range from $62 billion to $168 billion, while the estimated annual costs range from $34 billion to $39 billion. It is our intention to continue to report costs and benefits of major rules using a ten-year look-back.

The report also reproduces the totals by program we introduced in the 2003 Report. A substantial portion of both benefits and costs is attributable to a handful of EPA clean-air rules that reduce public exposure to fine particulate matter, and the Clean Air Program in EPA continues to account for the majority of regulatory benefits for rules finalized over the past ten years (between $35 billion and $115 billion).

In addition to the accounting statement, the 2004 draft report includes an expanded discussion of the impact of regulations on State, local, and tribal government, small business, wages, and economic growth.

In particular, the report includes an expanded analysis of the impacts of regulations on small business, using newly released reports from the Office of Advocacy of the Small Business Administration. The need to be sensitive to the impact of regulations and

paperwork on small business was recognized in Executive Order 12866, "Regulatory Planning and Review." The Executive Order calls on the agencies to tailor their regulations by business size in order to impose the least burden on society, consistent with obtaining the regulatory objectives. This Administration's E.O. 13272 reinforces the need for agencies to assess the impact of regulations on small businesses, and OIRA has a Memorandum of Understanding with Advocacy that supports our review of these analyses.

In short, our report confirms once again the relatively large burden that regulation imposes on small businesses, and demonstrates the need for an effective voice for small business during the regulatory review process. In previous reports, OMB has requested public nominations of promising regulatory reforms. Agencies have adopted or are continuing to follow up on many suggestions relevant to small business, including recommendations from Advocacy, and OMB will continue to seek information from agencies on how they plan to address their candidates for reform. In addition, OMB will continue to provide status reports to Congress on agency progress. In this draft report, OMB requests public nominations of promising regulatory reforms relevant to the welfare of manufacturing enterprises, especially small and medium-sized ones. Also, because studies have found that tax compliance was particularly burdensome for small businesses, OMB is especially interested in suggestions to simplify IRS paperwork requirements. Comments will be shared with relevant federal agencies for evaluation and, if meritorious, implementation. Final reform directions will be outlined in OMB's final report, to be published later this year.

This small business report and request for reform nominations complements our recent activity in connection with the implementation of the Small Business Paperwork Relief Act of 2002 (SBPRA). OMB, with the help of this Subcommittee, has undertaken many measures to reduce the paperwork burden that Federal requirements impose on small businesses, and to facilitate the use of agency information and resources available to small businesses.

For example, in an October 28, 2003, memorandum to the President's Management Council, we informed agencies of their responsibilities under this Act. In the memorandum, I drew special attention to the December 31, 2003 deadline for submission of regulatory enforcement reports to Congress. In addition, this Act requires OMB to publish, on an annual basis, a list of compliance assistance resources available to small business. Because we thought it would be helpful for the public to have the list of agency contacts along with the list of compliance assistance resources, OMB published these lists together. These lists are available on the OMB website (http://www.whitehouse.gov/omb/inforeg/infocoll.html#sbpra) and the SBA website (http://www.sba.gov/ombudsman/compliance/dsp_compliance.html). Finally, as you know, this Act requires the OMB Director or his representative to convene and chair an interagency task force, which must issue two reports addressing a total of five specific issues. The first final Task Force report was delivered to Congress on June 26, 2003 and a Notice of Availability was published in the Federal Register on June 27, 2003. This Task Force found that reducing small business paperwork burden is a challenge that

raises both regulatory and information technology issues. The Task Force also found that the presidential e-government initiatives, such as the Business Compliance One-Stop Initiative, represent the best opportunity for reducing the paperwork burden on small business. Since the first Task Force report was released, the Business Compliance One-Stop Initiative has been renamed the Business Gateway initiative. The Task Force is already working on the second report, which is due by June 28, 2004.

The 2004 draft report also includes an expanded review of the international literature on the effects of regulation on national economic growth and performance. Based on a comparison of 130 countries, the ten least regulated economies are Hong Kong, Singapore, the United States, New Zealand, the United Kingdom, Canada, Switzerland, Ireland, Australia and the Netherlands. These same economies have experienced relatively good economic performance measured by economic growth, per capita income and life expectancy. The adverse impacts of regulation may be mediated through factors such as the number of procedures required to start a new business, the time and costs of registering a new business, and the enforceability of contracts. More research is needed to determine the precise causal relationships between regulation and economic growth and performance.

Finally, in light of recent concerns about the health of manufacturing in the U.S., the draft report reviews the economics literature on the impacts of regulation on manufacturing enterprises. The review finds that the cumulative costs of regulation on the manufacturing sector are large compared to other sectors of the economy. In the report, OMB requests public nominations of promising regulatory reforms relevant to this sector. In particular, commenters are requested to suggest specific reforms to rules, guidance documents or paperwork requirements that would improve manufacturing regulation by reducing unnecessary costs, increasing effectiveness, enhancing competitiveness, reducing uncertainty and increasing flexibility. Final reform directions regarding manufacturing regulations will also be outlined in OMB's final report.

Thank you very much for the opportunity to appear today. I am willing to answer any questions you may have.

Mr. OSE. Thank you, Dr. Graham.

I am pleased to be joined here by my good friend from Massachusetts, Congressman Tierney. I would be happy to recognize him for the purpose of an opening statement.

Mr. TIERNEY. Thank you, Mr. Chairman.

Mr. Graham, Mr. Sullivan. Mr. Graham, you are getting to be quite a regular around here.

Let me just make a few brief remarks, if I may. I apologize for being somewhat late, and I am going to have to keep going in and out for a hearing that is going on in Education also.

Each year we hold a hearing like this one to review OMB's report estimating the costs and benefits of major agency rules. I continue to be troubled by OMB's increasing emphasis on basing public policy decisions on estimates of the costs and benefits of Federal protections. OMB uses cost-benefit analysis as if it is a neutral and conclusive formula for deciding the worth of agency rules. However, agencies should not enact and enforce regulations independent of their costs. Dollars and cents do matter. But, another kind of sense matters as well, and that is common sense. It is important to look at the reasons behind regulations. An analysis of a proposed action should take into consideration not just dollars, but costs and benefits that are not easily defined in terms of money, such as human life, a protected ecosystem, future impacts, and even how one regulation impacts other regulations.

OMB issued guidance last September, instructing Federal agencies on specific methods for evaluating regulatory decisions. In its guidance, OMB encouraged agencies to find out the net benefit of decisions by calculating the estimated benefit minus the estimated costs of compliance with the decision. It is frequently not possible to accurately calculate such a number. Some benefits are impossible to put into dollar form and plug into a calculator, and the costs are frequently overstated. The end result is incomplete and inaccurate. When cost-benefit calculations are done for Federal rules, they ought to be as completely, accurately, and transparently as possible. I think OMB fails in many of these areas.

One specific example of OMB providing analysis that is difficult to understand and incomplete is in its 2004 draft report. In its draft report, OMB provides cost and benefit estimates for an EPA rule requiring factory farms to obtain clean water permits. In its explanation of the estimates for this rule, OMB provides a list of benefits, such as contamination of coastal waters, that have not been translated into dollar amounts so, therefore, are not included in the estimated benefits.

The second section of OMB's draft report asks for public comment on regulatory reforms that will help the manufacturing industry. I am concerned that this is a solicitation for a hit list of environmental and health protections, much like that which OMB created in 2002. In evaluating the process of regulation, I am interested in learning more about the role OIRA is playing in approving and rejecting agency rules. As GAO reported last year, it seems that OIRA has increasingly become less of a counselor to agencies

and more of a gatekeeper for agency decisions.

I want to thank the witnesses for being here today. I look forward to your presentation.

And I thank the chairman for the opportunity to speak.

[The prepared statement of Hon. John F. Tierney follows:]

STATEMENT
REPRESENTATIVE JOHN F. TIERNEY
GOVERNMENT REFORM SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS
HEARING ON REGULATORY ACCOUNTING
FEBRUARY 25, 2004

Thank you, Mr. Chairman.

Each year we hold a hearing like this one to review OMB's report estimating the costs and benefits of major agency rules.

I continue to be troubled by OMB's increasing emphasis on basing public policy decisions on estimates of the costs and benefits of federal protections. OMB uses cost benefit analysis as if it is a neutral and conclusive formula for deciding the worth of agency rules.

Agencies should not enact and enforce regulations independent of their costs. Dollars and cents matter. However, another kind of sense matters, common sense. It is important to look at the reasons behind regulations.

An analysis of a proposed action should take into consideration not just dollars but costs and benefits that are not easily defined in terms of money, such as a human life, a protected ecosystem, future impacts, and even how one regulation impacts other regulations.

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number. Some benefits are impossible to put into dollar form and plug into a calculator. And the costs are frequently overstated. The end result is incomplete and inaccurate.

When cost benefit calculations *are* done for federal rules, they ought to be done as completely, accurately and transparently as possible.

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Thank you to the witnesses for being here today. I look forward to hearing your perspectives.

Mr. OSE. I thank the gentleman.

We will just go to questions here.

Gentleman, one of the first questions, Dr. Graham and I have struggled with this, trying to figure out how to get it put together, and we are making progress. I want to go back to the statutory deadline issue for the regulatory accounting report. One of the difficulties that we have up here, when we are asked for comments on the President's budget, is that when we don't have the documents we think are integral to us providing feedback, it makes it obviously difficult to provide feedback, and the regulatory accounting report is one of those. H.R. 2432 tries to or would align the delivery of the regulatory accounting report with the delivery of the President's budget so that they must be contemporaneous. So it would be part of the President's budget, as opposed to with the President's budget.

Now, would you support a requirement to integrate that regulatory information in the President's documents?

Mr. GRAHAM. Mr. Chairman, I am familiar with the fact that there are informal staff discussions that have been taking place on a range of provisions in the kind of legislation that your question addresses, including the specific question that you have asked about. As I think you are aware, OMB does have concerns with the kind of language that you are talking about for two reasons that I can cite to you, and I am sure the OMB general counsel has offered a few additional ones. But, the concern at the most principal level is the notion that the President would be required to submit certain kinds of information with his budget. The notion that would be a legal requirement is something I think people in the administration are not entirely comfortable with.

The second much more practical consideration is, what we have provided to you admittedly 10 or 11 days late, is a draft report that has not yet gone out for public comment or for peer review, as required by Congress. I am a little uncomfortable including in the President's budget documents something like this draft report, which has not had the vetting process that we have become accustomed to for this report. And, as a consequence, I don't think it would be wise to have this report remove public comment and peer review at this stage so that we can get it out in the context of the budget documents. And, I can assure you there aren't going to be draft parts of the President's budget, that is just not going to happen.

Mr. OSE. Does the law not already indicate or specify what the President's budget shall include?

Mr. GRAHAM. I think that there may be some parameters on that, and I would suggest to you that the administration is very reluctant to see any more precedence in the direction of requiring the President to provide certain kinds of information with his budget.

Mr. OSE. Mr. Sullivan, from the Small Business Advocacy standpoint, do you have any comment on the submittal of the regulatory accounting report as part of the President's budget submittal?

Mr. SULLIVAN. The Office of Advocacy does not have comment on that specific provision, Mr. Chairman.

Mr. OSE. The second question I have is, Dr. Graham, OMB uses the information collection budget to manage the paperwork bur-

dens on the public, and in one of the sections of our bill we have a requirement to conduct a multi-agency study of regulatory budgets, Section 6, if I recall. My question is whether or not you support such a study. I mean, I look at it as a tool that would help OMB and the agencies rank risk and then prioritize use of resources, and then make judgments to maximize the use of those resources. I am curious whether or not you have come to any conclusion on that, whether you support that particular requirement.

Mr. GRAHAM. I think that, again, this particular topic, as I understand it, is part of the informal dialog that is going between our staffs, and my understanding is we are making constructive progress in those discussions. You know that I am very optimistic and enthusiastic about the concept of a regulatory budget. That I am enthusiastic about the idea of trying to move forward for a pilot project, to try to actually demonstrate and study the potential promise of this type of activity. In terms of the specific language, I am not sure we are there yet, but my understanding is that we have made progress, if we are not thus hopefully that is something that we can work out if we don't yet have a detailed plan.

Mr. OSE. Thank you, Dr. Graham.

Mr. Tierney.

Mr. TIERNEY. Thank you.

Doctor, I am, as you noticed from my comments, a little concerned about the inclusion in your draft report of a call for public comments on reforms that can be made to regulations that affect the manufacturing sector. My concern obviously is that it is really an effort to target critical health, safety, and environmental protections that manufacturing industries feel are too expensive. Is that your aim?

Mr. GRAHAM. Our aim is to look at the cost effectiveness and degree of flexibility that are provided in existing regulations that govern the manufacturing sector. The motivation is, one, that studies demonstrate that compared to all other sectors of the economy, the manufacturing sector, particularly small and medium-sized manufacturers, bear a larger cost overall, and per firm, than firms in other sectors of the economy; and, second, as you know, in the last couple of years, while much of the economy is on the mend, the manufacturing sector is particularly struggling and, hence, we feel that is a good rationale for a priority and focus on the manufacturing sector.

Mr. TIERNEY. I wouldn't think that the administration is trying to say that the problem with manufacturing job loss in this country is due to regulation. You are not going to tell me that, are you?

Mr. GRAHAM. Well, I think that, as both the Commerce Department study indicated and as our study indicates, regulation is part of a range of factors, including liability lawsuits and other factors unique to the U.S. system, that cause our manufacturers to be placed at a disadvantage.

Mr. TIERNEY. And, so you are going to do a comparative study, I assume, of regulations before these jobs started to go out the window and since the date 2001, when they started to go?

Mr. GRAHAM. Well, I don't know how many studies we are going to do.

Mr. TIERNEY. Well, I want to really see. If we are going to go down this path, let us take a look at how manufacturing was doing before 2001 with the regulations or what has changed in the regulatory atmosphere from then until now, because the jobs started going down about 2001. So, let us take a look at that, if you are going to do it. Let us not just go out there and try to find a boogyman for why the administration has lost almost 2.3 million jobs, let us find out if something has changed in that there has been a real market change in the regulatory atmosphere around here.

Mr. GRAHAM. Right. And, I think the comment process will allow companies or any member of the public to offer opinions and make constructive suggestions in that area.

Mr. TIERNEY. Well, but it seems the comment period is not asking them to do that; the comment period seems to be saying give us a list of things you would like to see go out the window here.

Mr. GRAHAM. Well, that may be your interpretation, but, in fact, the exact words are there should be a consideration of the benefit and cost case for those regulations. We have no intention of altering regulations that have a strong benefit-cost case.

Mr. TIERNEY. Well, and I guess that depends on how we want to measure benefit and cost here. The guidance that OIRA issued last September asked the agencies to consider when they were evaluating regulations, estimates of the value of statistical life years in addition to estimates on the value of the statistical life. Now, it is my understanding that estimating the value of statistical life years would involve measuring the number of life years that would be saved by a particular regulation. Is that pretty much the case?

Mr. GRAHAM. Yes, sir.

Mr. TIERNEY. Well, couldn't such an evaluation result in protections for the elderly being valued as less beneficial because they have fewer years left?

Mr. GRAHAM. Yes. One of the purposes of offering both measures is to provide children and infants who may lose 30 or 70 years of life some indication of the measurement of their benefits, but then also adding the number of lives saved as a benefit measure, which provides for senior citizens, an accounting of each of the adverse impacts for seniors, without any adjustment for the number of years of remaining life. So, both pieces of information are provided to the regulator.

Mr. TIERNEY. But, it is not your intention, at least you don't think that this is designed to value the elderly lives as less beneficial because they have fewer years left?

Mr. GRAHAM. No. In fact, the language you are referring to is the same language that has been in our guidance throughout the 1990's, unchanged from the language that was in there from the previous administration.

Mr. TIERNEY. Doctor, you also, in your testimony that you submitted to the committee last July, discussed some of the limitations of the Crain and Hopkins estimate of the aggregate cost of Federal regulations. You stated that the estimate is based on previous estimates by Hopkins done in 1995, which itself was based on summary estimates done in 1991 and earlier, some dating all the way back to the 1970's. You noted only some of the underlying studies

were peer reviewed, and many were based on data collected anywhere from 10 to 30 years ago. But, in the OMB draft report of 2004, you cite the Crain and Hopkins study as a way to back up the solicitation of public comment on manufacturing regulations that should be reformed.

Do you stand by the comments that you gave to the committee last year in assessing those problems with the Crain and Hopkins estimate, and, if so, why do we find them being relied upon in this report?

Mr. GRAHAM. Good question. We do think that there is softness in the technical underpinnings of that particular report, even though it is the best available overall study of the economic impact of regulation in this country. However, our concerns are with the absolute magnitude of the estimates of costs, not the relative magnitude by sector of the economy. The only way we are using that particular report to justify the manufacturing initiative is the evidence comparing different sectors of the economy. We have no reason to believe that their conclusion is any way invalid that the manufacturing sector is hardest hit, compared to other sectors, by regulation.

Mr. TIERNEY. Thank you, Mr. Chairman.

Mr. OSE. Mr. Schrock.

Mr. SCHROCK. Thank you, Mr. Chairman.

Thank you, Dr. Graham and Mr. Sullivan for being here. Let me make a couple comments on the opening comments you made, Dr. Graham. You talked about a moratorium. Probably not a good idea because some regulations are beneficial. There are some bad actors out there, no question about it, but your comment smart regulation is what really struck me, and that is the key. If it boggles my mind, it should boggle the mind of every person in this room. That 80,000 new regulations have never been looked at is just obscene, and why we allow that to happen is a mystery to me.

you talked about the least regulated countries having a better overall environment, and I know that to be the case. During my Navy career, I visited one country in Europe in particular, and as a Congressman have visited there, and have visited a manufacturing plant just recently, was overwhelmed at how clean things are and how well things are done to protect their environment, which is one of the best in the world, without all the regulators hanging over their backs all the time doing things. So, I think we have lost jobs because of that. I think regulations in this country have caused people to move out of there, and businessmen will come and tell you that. It might not have impacted the small business community as much as large business, but it is going to come, and we have to be very careful that we don't allow that to happen.

Mr. Sullivan, the law requires OMB to submit not only a regulatory accounting statement, but also an associated report on the impacts of Federal rules and paperwork on selected groups, such, of course, as small business, and last year OMB did not submit this required element in both its February draft and the final report in September. On October 24th last year, as the subcommittee chair in the Small Business Committee, I wrote OMB that by law every regulation that is certified to have a significant impact on a substantial number of small entities is required to develop a regu-

latory flexibility analysis, but that each of the initial and final versions of this agency analysis is a statement of the potential impact of the rule on small business.

I notice in Mr. Sullivan's written testimony he says, "The draft OMB report would also benefit from small business impact analyses that should be prepared for rules reviewed by OIRA." Of course, OMB's just-issued draft report includes a less than three-page discussion of impacts on small businesses.

That being said, did the administration review each of the agency's regulatory flexibility analyses for its rolling 10-year period? If they did fine; if not, why not?

Mr. GRAHAM. Let me start by just getting a couple facts for the record straight. If you look at the draft report, we do have a section, as you indicate, several pages long on small business impact. But, we have a much more expanded section this year on the role of regulation on economic growth, and that is the section that reviews the World Bank studies, the OECD studies, and how the United States is relatively less regulated, compared to other countries around the world.

One of the key conclusions of that body of research is less regulation leads to more economic growth, because it is easier in those countries to start a small business, to gain the capital you need to launch a small business, and to get whatever permits you need to operate whatever kind of facility you need to operate. So, the economic growth section, which I would encourage people to look at, has a very strong small business focus and is featured in the report.

You also asked about the regulatory flexibility analyses. We do review those regularly when we review regulatory packages. But, to be quite candid with you, we don't consider ourselves at OMB the experts on small business. The gentleman to my left and his staff is where we go when we want a critical evaluation of an agency's package with respect to impact on small business.

Mr. SCHROCK. OK.

Do you want to make a comment, Mr. Sullivan?

Mr. SULLIVAN. Certainly, Mr. Schrock. The way my office has approached this draft report is really in a two-step process. The first step that we look at is whether or not there is cost-benefit analysis of rules effects on the employer community overall. And what we found was that type of analysis, that type of transparency that would allow any interested party to comment on rules, is lacking in the draft report. Our second step is to look even further. If there is in fact a detailed economic analysis on a major rule, then underneath that it would be nice to have the small business impact analysis flushed out. Now, what we had hoped was with the Regulatory Flexibility Act, greater partnership with Dr. Graham's office, with an Executive order by the President enforcing the Reg Flex Act, what we had hoped was that the better analysis on small business would then be immediately transferred into the agencies' submittals to Dr. Graham's office in preparation for this draft report.

Now, unfortunately, it doesn't look as though that has happened, so we have to work even more closely together to make sure that when the agencies fill out the A–4 Circular, that information does

translate next year in the draft report to a better analysis of the small business impacts.

Mr. SCHROCK. Do you want to comment on that?

Mr. GRAHAM. Yes. One thing I think we should also give good marks for is the fact that SBA Advocacy themselves produces an annual report on the impacts on small business of regulation.

Mr. SCHROCK. Do they comply with the A–4?

Mr. GRAHAM. I think that we should be careful that we don't lose sight of the fact that we do have a substantial amount of this information being generated already.

Mr. SCHROCK. Has OMB, though, asked the agencies about the impact it has had on them?

Mr. GRAHAM. Yes. In fact, the structure we have for this draft report is OMB has prepared it in its first form, but now it is available not only for agency comment, but for public comment, so SBA Advocacy, as well as all the agencies, have an opportunity to provide their information. So, we are in the process now of receiving that type of input. And, I can assure you that SBA Advocacy is not bashful about informing Dr. Graham about how they would like to see small business issues handled either in this report or in specific rulemaking contexts.

Mr. SCHROCK. Hurray for SBA.

My time is up, Mr. Chairman.

Mr. OSE. I thank the gentleman.

I want to go back to something that Mr. Tierney asked about, this Crain-Hopkins report. As I understand it, you entered into a contract to update that report?

Mr. SULLIVAN. That is accurate. Yes.

Mr. OSE. What is the schedule for completion of that?

Mr. SULLIVAN. We are hoping that it be completed as we approach this fall. I also want to add to some of the statements of discussion about the Crain-Hopkins report. Similar to the progression of the seven reports coming out of Dr. Graham's office, the Office of Advocacy has also engaged in a progression of each Crain-Hopkins report, examination of how regulatory burden affects small business is getting better. So, what we expect is a more detailed analysis of a better sector-specific analysis on how regulations impact small business. Then we leave it up to other interested parties, certainly those involved in the second panel this morning, to compare how regulatory impact and the costs associated to different economic cycles and time periods that Congressman Tierney associated with.

Mr. OSE. Thank you.

Dr. Graham, the A–4 Circular on regulatory analysis, as I understand it, attempted to lay a framework down for calculating cost and benefit of an agency action. First of all, I think that standardization of the analyses is a great step forward, and I compliment you on that. What I am trying to make sure is that the requirement to use the standards within the circular actually are enforced. Have you received any submittals from the agencies under the revised standard? Have they complied with the standard or have they not complied with the standard?

Mr. GRAHAM. Mr. Chairman, the OMB Circular A–4 took effect for proposed rules on January 1st of this year, and it takes effect

for final rules on January 1st of next year. And, my understanding is that we are now receiving the first packages from agencies that have sufficient economic impact to trigger the requirements of Circular A–4. So, my staff are literally in the process of reviewing the first packages that are subject to Circular A–4, and we intend to use all the available authorities we have to make sure that agencies comply with Circular A–4.

Mr. OSE. Well, I know that in the past you have used these prompt letters, which I thought was, frankly, a creative use of the ability to drive something forward properly, so you don't have to go back and do it over and over and over again. One of the things I am concerned about is that having the A–4 come out, having set the standard, I want to make sure that we get apples versus apples versus apples, rather than apples versus oranges versus tomatoes. So I know that the circumstances may come up, but to the extent that you must or have to, or whatever vernacular you care to use, return submittals for further review, so to speak, I think you will find that your effort to standardize the submittal of information will garner great support up here. So my point in saying that is don't be bashful in saying, look, you are not complying with the requirements of the A–4. I am trying to give you some support here.

Mr. GRAHAM. I appreciate it.

Mr. OSE. I give you enough criticism; I want to give you some support.

Mr. GRAHAM. Right. Well, we wouldn't mind a hearing at some point where we actually went through a couple of these agency analyses and whether they complied with A–4. I don't think that would be an unconstructive activity.

Mr. OSE. All right. We may very well followup on that. My only point is that if they don't comply, I am encouraging you to, in fact, exercise your return authority.

Mr. GRAHAM. Return authority, right.

Mr. OSE. Tom, Mr. Sullivan, do you have any input on that?

Mr. SULLIVAN. Doug, Mr. Chairman.

Mr. OSE. You come here one more time, I think we can legally claim you as a dependent.

Mr. SULLIVAN. I would actually like to add to Dr. Graham's comments, and that is how the returns and prompts are used. I think that there has been some mischaracterization of the draft report, the return letters, the prompt letters as targeting rules, compromising valuable protections, and nothing could be further from the truth. It is all about transparency. And I would like to actually share with the committee one example of how this review of regulations and actual activity by Dr. Graham's office can actually lead to supporting a new regulation.

Two years ago, when Dr. Graham's office put out the draft report, a number of small businesses commented on an OSHA standard, an OSHA standard having to do with the slings used in constructionsites. Their comment was not do away with the rule; their comment was that the small business industry is so far ahead of where Government is. Government has to catch up and proactively put out a modern sling standard. So, it is opposite from what some of the mischaracterizations have been about eliminating

rules; it simply called for the Government to keep up with the entrepreneurial speed of small business.

And, thanks to the activism of Dr. Graham's office, OSHA is in fact following up on a number of draft reports and recommendations, and revising that OSHA standard. That is within Dr. Graham's authority, but it didn't cause a prompt letter, it didn't cause a return letter, but it is a positive example of actually calling for a rule through the review of regulations, not simply calling to eliminate all rules.

Mr. OSE. Thank you.

Mr. Schrock.

Mr. SCHROCK. Mr. Chairman, I just have one other question I want to ask Mr. Sullivan, and it involves the review of OMB's small business impacts report.

In 2002, on March 19th, you signed a 3-year memorandum of understanding with Dr. Graham to institutionalize your office's working relationship. That stated purpose was, "to achieve a reduction in unnecessary regulatory burden for small entities." Did OMB ask you to review its less than three-page small business impact discussion in its just-released draft report? And, if so, when? And, if so, did OMB reject any recommendations by you for a more thorough analysis?

Mr. SULLIVAN. Congressman Schrock, Dr. Graham's office did not ask for us to review the section on small business impact in the OMB draft report.

Mr. GRAHAM. And, let me be clear. If we were to offer SBA Advocacy the opportunity to review our draft, we would have the Department of Health and Human Services, the Environmental Protection Agency, and the Labor Department. They would all like to be entitled to review a draft of OMB's report before we release it. The agency comment process is underway now that the draft report is available, so SBA Advocacy, like all other Federal agencies, has an opportunity to provide comments so that our final report has the benefit of SBA Advocacy's input.

Mr. SCHROCK. I would almost think SBA should be separate and apart from the big agencies you just mentioned.

Mr. GRAHAM. Because it is small? Well, it is potent, though.

Mr. SCHROCK. Well, it is potent, but I can see why you don't want all the big agencies doing that.

Mr. GRAHAM. Well, the reports that they have released, including the SBA commissioned Crain-Hopkins report, play a prominent role in the material that we have submitted in our draft report. That was commissioned by SBA Advocacy, so we are certainly open to input at any time from SBA Advocacy. In terms of formal interagency review and comment, however, that is a process that we like to treat all agencies the same. And, as important as SBA Advocacy is, it is one of the other Federal agencies.

Mr. SCHROCK. Thank you.

I yield back, Mr. Chairman. Thank you.

Mr. OSE. I have one final question.

Dr. Graham, I am a little bit confused on this 10-year window that you are looking at for analysis. I can't cite you chapter and verse, but it is my impression that we have major rules that predate that 10-year window that are still in effect.

Mr. GRAHAM. That is certainly true.

Mr. OSE. And, what I am trying to understand is why is it, as I interpret the report, why is it we are only looking at that 10-year window in the calculation of costs and benefits?

Mr. GRAHAM. The question is for an estimate of the costs and benefits that was prepared before a rule was adopted, how long after that estimate was prepared should it still be considered to be sufficiently valid for inclusion in OMB's report? We have made a professional judgment that once the estimate is more than 10 years old, given the dynamics in our economy, and the way firms react to regulation, that it is no longer realistic to consider those estimates as valid. So, the challenge we have in front of us is how do we get updated estimates of the current costs and benefits of regulations that were adopted more than 10 years ago. I think that is a very substantial analytic and research challenge not just for the Federal Government, but for the academic community and for the think tank community, as well. We are not comfortable publishing estimates prepared more than 10 years ago as resembling anything about what really is happening today.

Mr. OSE. The thought being that things have evolved to the point that this or that iteration, that report might not be accurate?

Mr. GRAHAM. The agencies' estimates that were made prior to issuing the regulation would be at least 10 years old, and usually probably 11 or 12 years old, given how the actual studies are done. So, we are very sensitive to the technical quality of the information that we are putting out in this report, and we think when the estimates are more than 10 years old, maybe we really ought to just draw a line.

Mr. OSE. Well, I know we have had this conversation before. I am trying to figure out the basis on which the line was drawn at 10 versus, you know, 30 or whatever.

Mr. GRAHAM. Five?

Mr. OSE. Five, two, whatever. Pick a number. I am trying to figure out. I think your phrase was professional judgment. Is it statutory?

Mr. GRAHAM. It is not a legal issue, it is the professional judgment of our staff analysts that we need to, at some point, say that an estimate that was made by an agency so many years ago is just simply no longer considered to be an appropriate estimate for what is going on today. If a subsequent study has been done that has validated those earlier estimates, then, of course, we would have no problem including those estimates.

Mr. OSE. This is the dynamic that I am trying to get at it. As I understand the law, there is no provision saying you can exclude prior to 10 years for any reason; it says OMB or your office will calculate the cost-benefit analysis in the aggregate on older rules, younger rules, new rules, whatever.

Mr. GRAHAM. Now, if you are going to move on the legal requirement question, you are talking to a very amateur attorney.

Mr. OSE. But, my point gets back to the statutory requirement. I am trying to figure out what is the basis on which we draw that line at 10 years?

Mr. GRAHAM. Right. Well, one thing to keep in mind is the Office of Management and Budget is covered by the Paperwork Reduction

Act and by the new data quality law passed by the Congress, and signed by the President. We are accountable for the information we disseminate in this report. Our analysts are not comfortable suggesting to people that an estimate that an agency produced 10 years ago on a major regulation is a valid estimate of either the costs or the benefits of that regulation today.

Mr. OSE. So we are caught in a little bit of a box here between the comfort level of the analysts looking at this 10-year-old data and perhaps a statutory requirement to include it, or the lack of definition as to whether it should be included?

Mr. GRAHAM. Well, if you give us a written question, I am sure we can have our lawyers pour over these statutes. We may be able to find a legal position that the statute doesn't in fact when you consider all issues, absolutely state that we have to do it that way.

Mr. OSE. I am trying to noodle this through.

Mr. GRAHAM. I think that would be unfortunate, though, because I think that we are trying to put cost-benefit analysis on as strong a technical and scientific footing as possible. For us to be including in an official report like this, coming out of the Executive Office of the President, information that is over a decade old, given the way our economy changes, I just think is not a wise territory for us to be exploring.

Mr. OSE. From a scientific standpoint, I can understand your point, and I accept it. My problem is do those costs and benefits then get excluded in their entirety from any analysis? Or, conversely, when you have a much older rule that still have significant impact, does it just get ignored?

Mr. GRAHAM. I think we ended up in between those two. This was the first year that we had the rollover effect, where we had a year's worth of regulations that we did not include in those calculations, roughly 1992–1993. We did report them in an appendix, but we did not put them in the main report. The information is still there for people who want to access it, but we did not put it in the main report.

Mr. OSE. Well, I tell you what, I think I am going to give some additional thought to this, and I will probably put a question to you in writing, because I do think this is important to flush out.

Mr. GRAHAM. It is very important.

Mr. OSE. Because there are rules that predate where that 10-year line might be drawn, or the 5-year line, or whatever it is.

Mr. GRAHAM. Right. Obviously, we could have picked a different number. It is a professional judgment call in how far you go back.

Mr. OSE. I understand.

All right, the balance of my questions I am happy to submit in writing.

Mr. Schrock, do you have anything further?

Mr. SCHROCK. Nothing further, thank you.

Mr. OSE. I want to thank you both for coming up today. I hope you don't have to walk back. Dr. Graham got to walk up here this morning. I do appreciate your taking the time to provide your testimony and your feedback. We will leave the record open for 10 days for the written questions to you. Obviously, as in the past, we have appreciated your timely responses, and we would again thank you both.

We will take a 5-minute recess.

Mr. GRAHAM. Thank you.

[Recess.]

Mr. OSE. OK, we are going to go back into session. Our second panel is joining us today. As you saw in the first panel, our standard procedure is we swear everybody in. I will first introduce everybody, and then we will have the swearing in ceremony.

We are joined on the second panel by Mr. William Kovacs, the vice president for Environment, Technology, and Regulatory Affairs at the U.S. Chamber of Commerce; our second witness is Ms. Susan Dudley, who is the director of the regulatory studies program of Mercatus Center at George Mason University; also joined by Dr. Richard Belzer, who is the president at Regulatory Checkbook Organization; we are again joined by the president of Public Citizen, Ms. Joan Claybrook; and I believe a new witness to our committee this morning is Robert Verchick, who is the Ruby Hulen professor of law, the University of Missouri at Kansas City School of Law, Center for Progressive Regulation. Welcome to all of you.

Now, if you would all rise. I am not picking on you; we do this for everybody.

[Witnesses sworn.]

Mr. OSE. Let the record show the witnesses all answered in the affirmative.

Now, as you saw in the first panel, what we do is we just go from my left to my right on testimony; everybody gets 5 minutes. I have a heavy gavel on the time requirement; that is why we started on time. We do have, I think, Dr. Belzer, you have a 12:30 plane you have to get?

Mr. BELZER. Two.

Mr. OSE. Two o'clock. OK. Well, let me just tell you we are not able to violate this timeline. I am advised that the gentleman has a daughter being married. Tell her this committee congratulates her.

OK, our first witness is Mr. William Kovacs from the Chamber of Commerce. Mr. Kovacs, you are recognized for 5 minutes.

STATEMENTS OF WILLIAM KOVACS, VICE PRESIDENT, ENVIRONMENT, TECHNOLOGY AND REGULATORY AFFAIRS, U.S. CHAMBER OF COMMERCE; SUSAN DUDLEY, DIRECTOR, REGULATORY STUDIES PROGRAM, MERCATUS CENTER, GEORGE MASON UNIVERSITY; RICHARD B. BELZER, PRESIDENT, REGULATORY CHECKBOOK; JOAN CLAYBROOK, PRESIDENT, PUBLIC CITIZEN; AND ROBERT R.M. VERCHICK, RUBY M. HULEN PROFESSOR OF LAW, UNIVERSITY OF MISSOURI AT KANSAS CITY SCHOOL OF LAW, CENTER FOR PROGRESSIVE REGULATION

Mr. KOVACS. Thank you, Mr. Chairman and members of the committee. The first thing I want to do is commend you and Dr. Graham for taking on this very important subject. Some people in the Washington community would consider it tedious or complex or arcane. But, unlike Congress, the regulatory agencies never take a break, they don't have a recess, so every year you see 4,000 regulations; it just never stops. And, the reason the Chamber cares, and why we are so concerned, whether it be regulatory accounting or

a budget or cost-benefit, is you need to put it in perspective. If you looked at all the discretionary spending in 2003 for the Congress, it was $825 billion. The Hopkins-Crain report has the cost of the regulatory programs at about $843 billion annually and the cost of environmental programs around $250 billion annually. And, to put this in one last perspective, all of the corporate income taxes paid in the year 2002 only total $211 billion. So, when you have this kind of a burden and you realize that, for a small business, they have a 60 percent premium, we care, because well over 90 percent of our businesses are small businesses.

The cost-benefit analysis is really a tool. It is a tool that helps us determine what particular regulations are worth expending public or private funds, which are always limited. But, cost/benefit is one of many tools. We have other tools: we have data quality, we have data access, peer review, sound science, and transparency in the regulatory process. And, the purpose of using these tools is really so that we use our money and our resources to protect and to get maximum protection both for health and safety and the environment.

Now, we have been very honest and have said that the current cost-benefit approach has a number of problems. It is extremely confusing and it is extremely complex, and, even though I have read Circular A–4, we have to be honest with ourselves. It is a complex issue, and when you have the numbers coming out with such great disparities between where OMB is coming, at a relatively minor number for the cost of regulation, and then you have the Crain-Hopkins report at $843 billion, what happens to the public is they really dismiss it. If you are working in the field and you are a small businessman, you know that regulators have real costs. But when you see these discrepancies, it is easier for someone to say, well, we are just going to put them aside because it is just politics.

And, in addition to that, the OMB looks at a limited number of rules; its static versus dynamic system. Agencies game the system. I will just give you an example on the TMDL rules. EPA, no matter what it was told, said the cost of the rules are $25 million annually. The States did their own study and they found that it was $670 million to $1.2 billion annually. Also, this committee has done a lot of work on agency guidance documents. So we are not just dealing with rules. Every year agencies puts out hundreds of guidance documents which, in effect, operate as rules. And, in this instance EPA, over a 4-year period, put out about 2,300 and OSHA put out about 2,500. So it is a very complex system.

And, one of the things, as I run out of time, is that what we need, and A–4 is starting this, is some kind of consistency within a model, where we need to understand the uncertainties of the issue and we need to clearly state these are uncertainties. And, the best example that we can give is what EPA is doing right now with a particulate matter rule. Everyone says, well, there are all these health benefits. Well, there are studies on both sides. Some of the studies indicate that there is absolutely no link between the mortality rates and particulate matter. Now, whether that is true or not, I don't know, but in John Graham's studies EPA accounts for

about 60 percent of all the costs and benefits in the environmental section.

So, what we are talking about is not the 4,000 rules and not all the rules going back 10 years. What we are talking about is for a cost/benefit analysis to be conducted for those major rules that have major impact. For those rules we need to do an honest study, find the right economists, the right scientists, and integrate science and data into the rule so we can do it right. And, we have just, at the Chamber, gone through this on the technology side because the industry lost $2 trillion in market capital, a lot of which was due to regulation. So, when we did this, we scoured the United States, and it is very hard to find a group of people who can do one of these studies.

So, what our recommendation would be to the committee is that you proceed with the cost/benefit analysis. This is very valuable; we have to do it. But, we take one or two rules and we do it right so that we can begin developing the model.

Thank you very much.

[The prepared statement of Mr. Kovacs follows:]

Statement of the U.S. Chamber of Commerce

ON: THE SUBJECT OF THE OMB DRAFT 2004 ANNUAL REPORT TO CONGRESS ON THE COSTS AND BENEFITS OF REGULATIONS

TO: HOUSE SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS

BY: WILLIAM L. KOVACS

DATE: FEBRUARY 25, 2004

The Chamber's mission is to advance human progress through an economic, political and social system based on individual freedom, incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing more than three million businesses and organizations of every size, sector, and region.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 71 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross-section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business -- manufacturing, retailing, services, construction, wholesaling, and finance – is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 95 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross-section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

STATEMENT OF WILLIAM P. KOVACS
VICE PRESIDENT
U.S. CHAMBER OF COMMERCE
BEFORE THE
SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS
U.S. HOUSE OF REPRESENTATIVES
ON THE SUBJECT OF THE DRAFT 2004 OMB ANNUAL REPORT TO CONGRESS ON THE COSTS AND BENEFITS OF REGULATIONS
FEBRUARY 25, 2004

Mr. Chairman and members of the subcommittee, thank you for inviting me to this hearing to discuss the *Draft 2004 OMB Annual Report to Congress on the Costs and Benefits of Regulations* (draft report) and how to improve regulatory accounting. I am William Kovacs, Vice President of Environment, Technology and Regulatory Affairs for the U.S. Chamber of Commerce (U.S. Chamber). The U.S. Chamber is the world's largest business organization representing more than three million businesses of every size, sector, and region. More than 96% of our members also qualify as small businesses.

The U.S. Chamber cares deeply about the regulatory process including cost-benefit analysis and the accounting methods used to assess it, because the costs and impacts of regulations on the nation's economy are staggering. In 2003, federal discretionary spending was $825 billion, and the total of all individual income taxes paid in 2002 was $1.037 trillion.[1] Compare these two observations with the annual cost of *all* federal regulations, which are presently estimated at about $843 billion.[2] As another measure of comparison, the annual cost of

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[1] *Treasury Department Gross Tax Collections: Amount Collected by Quarter and Fiscal Year, 1987–2003.* SOI Bulletin, Historical Table. Excel ver. 4. Issued Quarterly, Internal Revenue Service, Statistics of Income Division. [See Table 8.7 - Outlays for Discretionary Programs: 1962–2009; Budget of the United States Government--Fiscal Year 2005, Historical Tables.]

[2] W. Crain and T. Hopkins, *The Impact of Regulatory Costs on Small Firms*, Report RFP No. SBAHQ-00-R-0027 for The Office of Advocacy, U.S. Small Business Administration (July 2001).

environmental regulation is about $197 billion[3], while the total of all corporate income taxes paid in 2002 was $211 billion[4]. The role of the Office of Management and Budget's (OMB), Office of Information and Regulatory Affairs (OIRA) in seeking to improve regulatory actions therefore has great significance to the business community and to small business in particular, since federal regulation costs small business $6,975 per employee, almost 60% more per employee than a large company[5].

Administrator John Graham and his OIRA staff are performing admirably in advancing the discussion of how to ensure that regulations are based on reliable information. The undertaking is also critical to establish the soundness, usefulness, and effectiveness of regulations. The U.S. Chamber encourages OIRA to continue with this effort and seek further improvements in the regulatory assessment process.

In simple terms, cost-benefit analyses are used to help determine if a particular regulatory action is worth the expenditure of public and private resources in relation to the benefits to be received. A reliable assessment that uncovers the advantages (or disadvantages) of regulatory options is essential when funding and other resources are limited, as they are in the real world. While U.S. Chamber policy recognizes that federal regulations play an important role in assuring public health, safety, and protection of the environment, the U.S. Chamber also believes that rules and standards must be based on scientifically sound, transparent, and peer-reviewed science. Moreover, federal agencies must utilize appropriate risk assessment and management protocols in developing their regulatory programs. This approach, along with reliable cost-benefit analyses should be used to prioritize regulatory objectives, identify appropriate regulatory options, and target resource allocations to address the most important

[3] *Ibid*; Page 25.
[4] Footnote 1. *Ibid.*
[5] Footnote 2. *Ibid.* Page 3.

problems. Without such informed prioritization it will be difficult to ensure that the greatest public benefit will be achieved in the most efficient manner. Cost-benefit analysis, therefore, is not an end in itself. Rather, it is one of several decisional tools that policymakers must rely upon to assess regulatory options. In this respect, we are encouraged by OMB's effort to improve the cost-benefit methodology used by government agencies.

Each of OIRA's Annual Reports to Congress has been an improvement over the preceding year's report. The latest revision to OMB Circular A-4, Regulatory Analysis (September 17, 2003), represents a significant step forward by providing uniform guidance to all federal agencies for the development of cost-benefit analyses. In addition, OIRA's Information Quality Guidelines, as well as its recently proposed Peer Review Bulletin, will provide the foundation needed for developing methodologies that allow us to develop more reliable cost-benefit analyses, and are necessary for ensuring that government decisions are sound, transparent, and open to the public.

The U.S. Chamber is not opposed to regulations per se and recognizes that many regulations are sound, sensible, and well founded. In fact, in many instances, regulations function as good business practices. That observation notwithstanding, because aggregate regulatory costs are so enormous, it is absolutely essential that federal agencies fully understand the real world costs and benefits of their regulatory actions and that resource expenditures be prioritized so that we as a nation achieve the maximum protection of human health and the environment with the public and private funds expended. As one of the tools needed to accomplish this task, cost-benefit analysis methodology must be made as reliable as possible.

THE CURRENT PROCESS IS COMPLEX AND CONFUSING TO THE PUBLIC

Unfortunately, measuring the costs and benefits of regulations is an extremely difficult and complex undertaking. Consequently and not surprisingly, many stakeholders have expressed various concerns about OMB's Annual Report to Congress, its regulatory accounting methodology, and Circular A-4.

One criticism is that the economic modeling methodology used for assessing the costs and benefits of regulations, especially in the aggregate, is inadequate and does not present the public with a reasonable and true account of the costs of regulatory impacts. The Crain and Hopkins study commissioned by the Small Business Administration's Office of Advocacy is widely cited in support of this observation.[6] While Crain and Hopkins conclude that the true cost of *all* federal government regulations was an estimated $843 billion in 2000, OMB, which examines only a few major regulations, concludes that regulatory cost burdens are much smaller, for example only about $1.9 billion in fiscal year 2003 for the six major regulations examined. These numbers are difficult to compare, as they are derived from different bases (all regulations versus a few major regulations) and in different timeframes. However, differences in accounting methods notwithstanding, the "message" that is conveyed to the public about the size of regulatory impacts is very misleading. Certainly there is little doubt that there is a large discrepancy in the information that has been developed, and much public confusion as a result. OMB must resolve this issue in a manner that clarifies any uncertainties. If it does not, then neither Congress nor the public will be able to fully appreciate the true cost impacts of federal regulations on business and industry.

Organizations such as the AEI-Brookings Joint Center for Regulatory Studies and the Mercatus Center at George Mason University have made similar observations. These groups

[6] *Ibid.*

have concluded that assessment approaches and modeling methodologies must be further improved to reliably and transparently calculate the cost-benefit impacts of government regulations. Absent such an initiative, stakeholder confidence in cost-benefit estimates will be weak, and rightly so. The lack of reliable modeling methodologies has resulted in extremely wide cost-benefit disparities between studies, and the disparities can be so great that they can literally render the results so subjective as to be useless.

Another concern is that OMB's Report only provides a "snapshot" of certain regulatory costs and benefits, mainly those associated with major rules and regulations, and at that, only a few of these are in fact considered in any great detail. For example, OMB's 2004 draft report is based on individual agency cost-benefit estimates for only six major regulations out of a total of 37 "major" rules 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. This situation is particularly troublesome, because as OMB notes, the *...total costs and benefits of all Federal rules now in effect (major and non-major, including those adopted more than 10 years ago) could easily be a factor of ten or more larger than the sum of the costs and benefits reported...*[7]

LACK OF CONSISTENCY, BENCHMARKING, AND COMPREHENSIVENESS

Furthermore, neither OMB nor government agencies have made any significant attempt to retrospectively re-assess initial cost-benefit projections. As a result, OMB's reported information, which is based on agency projections of costs and benefits, is not benchmarked against what actually occurred after the regulations were implemented. This is an unacceptable situation. At a minimum, government agencies should be required to periodically revise and recalculate their earlier estimates based on what actually occurred after regulations have been

[7] *Draft 2004 OMB Report to Congress on the Costs and Benefits of Regulations*, page 6.

implemented. Such an undertaking could perhaps be limited in the future should such recalculations convincingly demonstrate that original cost-benefit estimates in fact presented reasonable approximations of what actually transpired once the regulations were implemented.

As a further consideration, some methodological approach should be established that can enable OMB to more reliably gauge the impact of all federal rules that are in effect, not just those major rules promulgated over the previous ten years or some other arbitrarily established timeframe that fails to capture the full cost and benefit impacts of regulations on the public. The assertion that rules promulgated more than ten years ago are not presently of significant consequence should be convincingly demonstrated and not just stated as a matter of fact.

An additional concern is that many so-called "minor" rules might in fact really be "major" in their impact. Despite this possibility, OMB excludes cost and benefit estimates for all "non-major" rules. Is this a problem? It may be, but this is not clear at present. For one thing, it is the individual government agencies themselves that determine, absent oversight, which rules are "major" and therefore require preparation of a regulatory impact analysis. How, under these circumstances, can the public have any confidence in the assessed impacts? Are some agencies "gaming" the system, for example, by purposefully understating costs or benefits of proposed regulations to avoid having to perform a regulatory impact analysis? An example of an agency gaming the system is the U.S. Environmental Protection Agency's (EPA) determination that its extremely controversial Total Maximum Daily Load (TMDL) standard only had an annual impact of $25 million[8]; yet state studies estimated the cost of implementing the TMDL standards at $670 million to $1.2 billion annually[9]. It will take more than 15 years to complete the

[8] 64 *Fed. Reg.* 46043 (August 23, 1999).
[9] Testimony of David Holm, President, Association of State and Interstate Water Pollution Control Administrators before the House Subcommittee on Water Resources and the Environment, Page 3 (February 10, 2000).

estimated 40,000 TMDLs that would have to be performed, so there are likely comparable recurring costs in this time period.

Another way agencies avoid the preparation of regulatory impact analyses altogether is by proposing de facto regulations through the issuance of guidance documents, or by using consent decrees to avoid rulemaking procedures and OMB or public scrutiny. A good example of this "guidance" problem is EPA's Environmental Justice Program, which establishes an entire administrative program that is spelled out through guidance documents.[10] This problem is rampant throughout the federal government, with agencies such as EPA and the Occupational Safety & Health Administration (OSHA), in particular, issuing countless numbers of guidance documents in lieu of regulation. Between March 1996 and October 2000, EPA issued 2,653 guidance documents, and OSHA issued 3,374 guidance documents.[11] Not all guidance documents act as regulations, but the sheer numbers issued by agencies become a vehicle for avoiding the preparation of cost-benefit analyses. Unless questions such as these can be answered now, closer scrutiny of regulatory practices at individual federal agencies is warranted.

Equally problematic, the various government agencies use manifold different cost-benefit assessment methods. As a result, it's fair to say 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. OMB's revised Circular A-4 may improve this situation, especially by promoting transparency, ensuring more consistent practices across federal agencies, and allowing better cross agency comparisons. Such efforts aimed at improving the

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[10] W. Kovacs, U.S. Chamber of Commerce, "Comments to the Office of Management and Budget (OMB) concerning OMB's Draft 2003 Report to Congress on the Costs and Benefits of Federal Regulations" (May 5, 2003).
[11] *Non-Binding Legal Effect of Agency Guidance Documents*, Seventh Report by the Committee on Government Reform, House Report 106-1009, U.S. House of Representatives (October 26, 2000).

inter-consistency of the individual government agency cost-benefit assessments should be encouraged.

NEED FOR SOUND SCIENCE AND RELIABLE ASSESSMENT METHODOLOGY

Underlying all these expressed concerns is the need for sounder science and improved modeling methodology. Although OMB has made great strides in this area, much progress remains to be accomplished. Too many regulatory actions are still based on unsound data, poor analyses, and use of inadequate scientific and economic modeling methods. Given the great magnitude of aggregate regulatory cost estimates, this is an intolerable situation.

As but one example, EPA's regulatory activities aimed at addressing fine particulate matter encompass the major portion of the costs and benefits included in OMB's aggregated estimate of the impact of regulations promulgated over the past decade. That this is true is particularly alarming, as there is persuasive evidence that the underlying science of particulate matter does not support EPA's regulatory stance. This observation has most recently been brought to the fore in a peer-reviewed science journal article written by academic researchers Gary Koop and Lise Tole of the University of Leicester, Leicester, UK[12]. In their article entitled, *Measuring the health effects of air pollution: to what extent can we really say that people are dying from bad air?*, the authors conclude that uncertainties about air pollution-mortality impacts are so large as to question the plausibility of previously measured links between air pollution and mortality.

A key assumption made by EPA in its cost-benefit analysis of the regulatory impact of its environmental regulations is that inhalation of fine particles is *causally* associated with a risk of premature death at concentrations near those experienced by most Americans on a daily basis.

[12] G. Koop and L. Tole. *Measuring the health effects of air pollution: to what extent can we really say that people are dying from bad air?, Journal of Environmental Economics and Management*, Vol. 47, 2004, pp. 30-54.

If in fact, however, there is no plausible link, one has to wonder in all seriousness about the veracity of EPA's fine particulate matter cost-benefit estimates, which are far from inconsequential. For example, in the past decade, 60 percent of all the benefits and costs of all the major federal rules analyzed by OMB in its annual reports to Congress are accounted for by major rules issued by EPA, and it should not go unnoticed that the majority of the benefits calculated by EPA derive from reductions in exposure to particulate matter.

Simply put, the public and regulators must establish and incorporate an improved understanding of the influence of uncertainties in both risk and cost-benefit impact analyses. The U.S. Chamber made more extensive comments concerning this specific issue to EPA in January, noting especially EPA's marked bias in its treatment and assessment of scientific information concerning particulate matter. In sum, the U.S. Chamber firmly believes that sound science, quality data, reliable environmental and economic modeling methodologies, and transparent weight-of-evidence techniques must be used in assessing health impacts. Without such underlying attention to scientific details, cost-benefit estimates are doomed to fail.

COST/BENEFIT ANALYSIS MUST CONSIDER LOST OPPORTUNITY COSTS

Another concern is that current cost-benefit analyses do not address what societal needs are ignored when a decision is made to implement a regulation. Consider, for example, a hypothetical decision to implement a regulation aimed at reducing carbon dioxide emissions by limiting the use of carbon-based energy resources. One may rightly ask, will making this decision to have a carbon-free energy environment result in the diversion of resources from other initiatives, such as for pre-natal health screenings, medical treatment for the uninsured, medical or biotechnology research, or toward progress in developing advanced materials or communications systems? Clearly, the use of funds to accomplish specific regulatory objectives

can have unintended consequences, such as benefits not realized. This problem must be addressed and points to the need to *prioritize* regulatory objectives based on a balanced assessment of the benefits and costs of *all* regulatory options.

Simply put, the public will be best served when it gets the most bang for the bucks that are expended. This will be accomplished when those regulations that are implemented are in fact those regulations that are really needed, and when those regulations that are implemented are those regulations that are the most efficient and have the least amount of unintended consequences.

A REGULATORY ACCOUNTING PILOT STUDY IS ADVISABLE

The Chamber recommends that Congress begin to address some of the above noted issues and concerns by funding a pilot study program aimed at assessing how to improve cost-benefit impact assessment methodologies and to integrate these improved assessment approaches into the consideration of, and establishment of, regulatory and budgetary priorities. This undertaking should be fully transparent and subject to open peer-review. Given the likely complexities of such an undertaking, perhaps only one or two specific areas impacted by regulatory activity should be addressed, such as workplace safety, air quality, or technology development.

Relevant to and in support of this proposed initiative, various institutions and think tanks, as well as some federal government agencies, have already conducted, or are conducting, detailed studies of the costs and benefits of regulatory programs. These undertakings should all be made fully transparent and publicly available to stimulate further public awareness and debate in this area. In particular, it is essential that the public and government agencies gain an improved understanding of the risks of regulatory options, how they are influenced by

uncertainties, and how this information can be better used to craft and use improved cost-benefit assessments to prioritize regulatory and budgetary initiatives.

At the end of the day, the public has a right to an honest assessment of regulatory options. Every private or corporate dollar spent on an unnecessary regulation is one that could instead have gone toward providing workers with better wages, better pensions, or improved health care. Likewise, public dollars spent on developing and enforcing ill-founded regulations are dollars that could have been used on improving medial research, education, or transportation infrastructure.

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Finally, the Chamber is grateful to have this opportunity to present its recommendations for your consideration concerning *Draft 2004 OMB Annual Report to Congress on the Costs and Benefits of Regulations* and how to improve regulatory accounting. During its debate over the nature of cost-benefit analyses and accounting methods Congress has a significant opportunity to identify measures that can strengthen and improve regulatory assessment procedures and their application in a manner that can provide greater and more efficient protection of human health and the environment while doing so in a cost-effective, scientifically sound, prioritized manner. The Chamber appreciates being able to be a part of this debate.

Mr. OSE. Thank you, Mr. Kovacs.

Our next witness has been with us before, Ms. Susan Dudley, who is the director of regulatory studies at the Mercatus Center from George Mason University. Welcome. You are recognized for 5 minutes.

Ms. DUDLEY. Thank you. Thank you, Mr. Chairman and Mr. Schrock for having me here to talk about the important issue of regulatory accounting. I am also an adjunct professor at George Mason University School of Law, but my comments today reflect my own views, not an official position of either the University or the Center.

You have my written testimony, but today I would like to focus on the similarities and differences between regulatory accounting and the fiscal budget.

American citizens generally know how much they pay in taxes each year, but taxes and subsequent spending are just one way that the Federal Government diverts resources to achieve broader public goals. The other is through regulation. While taxes and associated spending are tracked annually through the fiscal budget, there is no corresponding mechanism for keeping track of the off-budget spending accomplished through regulation.

These annual regulatory accounting reports that you have required represent an important step toward tracking these off-budget taxes and expenditures. These reports can be valuable not only for informing Americans generally about the costs and benefits of regulation, but also for helping policymakers allocate limited resources to those activities that provide the greatest net benefit to American citizens.

A better understanding of regulatory performance and results will help appropriators allocate budgets toward those agencies and activities that produce the greatest net social benefit. I think you will find that what OMB has done with the Government Performance and Results Act, by integrating that into the budget, has proved valuable.

These reports and other executive and legislative branch activities, along with extensive academic research, have improved our understanding over the years of the impact regulations have on consumers, workers, and companies. However, the reports are still far from perfect, and we still lack a reliable mechanism analogous to the fiscal budget process for tracking regulatory expenditures and ensuring they produce desired outcomes. So, I have three recommendations.

First, OMB can improve the quality of information in future reports by holding agencies accountable for complying with new guidelines. Second, a legislative branch review body could provide a more independent assessment of regulatory costs and benefits. And, third, Congress could explore further ways to treat regulatory expenditures in a manner similar to on-budget expenditures. And, I would mention that H.R. 2432 does this.

Let me go back and talk a little bit about each of those three recommendations.

The increased transparency that is reflected in OMB's review procedures and in this report are welcomed improvements to the regulatory process, but the benefit and cost estimates in the draft

report do not offer the American people an accurate picture of the impact of regulation. To be comparable in value to the fiscal budget figures, OMB's estimates must reflect an independent assessment of regulatory costs and benefits, and not simply provide a summation of agency estimates. Such an approach would be unthinkable in the fiscal budget process.

Over the coming year, OMB will be in a better position to hold agencies accountable for conducting analysis to ensure that the resulting benefits and costs are reliable and robust. Last September, OMB issued guidelines for regulatory analysis that reflect generally accepted principles, and it also is developing guidelines for peer review and data quality. Over the coming year, in the course of Executive Order 12866 review, OMB should be able to hold agencies accountable for these new guidelines. And, if draft regulations do not comport, OMB should return regulations to agencies. If it does return regulations whose analysis don't comport with the new guidelines, I think it will be able to rely on agency estimates with more confidence.

While I think OMB should continue its review procedures under Executive Order 12866, and hold agencies accountable for ensuring that proposed regulations do more good than harm, Americans may also benefit from a legislative branch agency. Indeed, Congress has authorized a congressional office of regulatory analysis to be housed in the General Accounting Office, but it hasn't been funded. Such a body could provide Congress and U.S. citizens with an independent assessment of the total costs and benefits of regulation, and also help ensure that statutes are being implemented so that the benefits to Americans outweigh the costs.

An annual regulatory accounting report issued with the Federal budget is an important first step toward providing the same scrutiny to regulatory impacts as on-budget impacts. Mr. Chairman, H.R. 2432 would explore ways to treat regulatory expenditures in a manner similar to on-budget expenditures, recognizing that regulations, like on-budget fiscal programs funded by taxes, divert private resources to broader national goals. I applaud you for this. A more explicit recognition of the expected costs, as well as expected benefits, of achieving regulatory goals will help policymakers allocate scarce resources to activities that will produce the greatest net social benefits. Thank you.

[The prepared statement of Ms. Dudley follows:]

UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON GOVERNMENT REFORM
SUBCOMMITTEE ON ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS

REGULATORY ACCOUNTING

February 25, 2004

Testimony of Susan E. Dudley

Director, Regulatory Studies Program,
Mercatus Center, George Mason University
Adjunct Professor, George Mason University School of Law[1]

Chairman Ose and Members of the Subcommittee, thank you for inviting me to testify on the important issue of regulatory accounting.

American citizens generally know how much they pay in taxes each year. But taxes, and subsequent spending, are but one way the federal government diverts resources from the private sector to accomplish its goals. The other is through regulation of private entities – businesses, workers, and consumers. While taxes, and associated spending, are tracked annually through the fiscal budget, there is no corresponding mechanism for keeping track of the off-budget spending accomplished through regulation.

The annual "Regulatory Accounting Reports" required by Congress represent an important step toward tracking these off-budget taxes and expenditures. These reports can be valuable, not only for informing Americans generally about the costs and benefits of regulation, but also for helping policy makers allocate limited resources to those activities that provide the greatest net benefit to American citizens.

The annual reports could be integrated more fully into the fiscal budget process.

A better understanding of regulatory performance and results will help appropriators allocate budgets toward those agencies and activities that produce the greatest net social benefits. Studies reveal that a reallocation of current spending from lower risk to higher risk hazards could greatly increase the life-saving benefits of regulations designed to reduce health and safety risks and achieve other social goals. If agencies and Congress better understand the benefits and costs of different programs, they can then assess how to reallocate resources from initiatives that are less effective to those that are more effective.

[1] These remarks do not represent an official position of George Mason University.

Congress and the Executive branch must always consider, implicitly if not explicitly, the costs and benefits of different programs as part of the budget process. Just as integrating Government Performance and Results Act measures into the fiscal budget process shows promise for improving accountability and outcomes, integrating OMB's Regulatory Accounting Report will allow policymakers and appropriators to allocate our nation's resources more efficiently and effectively to achieve greater benefits from our regulatory programs.

Comments on 2004 draft report

I strongly support efforts by OMB and the respective agencies to assess regulatory costs and benefits, and am encouraged by the transparency with which OMB has presented the regulation-by-regulation estimates back to 1993. I also found the literature review and discussion of the relationship between regulation, freedom, and economic growth interesting and valuable. However, the data as presented are still inconsistent and fragmentary and may not offer the American public an accurate picture of the benefits and costs of regulation.

The draft report estimates that the annual benefits of regulations issued between October 1, 2002 and September 30, 2003 range from $1.6 billion to $4.5 billion. Annual costs for regulations issued over this period are estimated at $1.9 billion. The draft report estimates that for regulations issued over the last ten years (October 1, 1993 to September 30, 2003), annual benefits range from $62.1 billion to $168.1 billion, and annual costs range from $34.2 billion and $39.0 billion.

These figures will be reported in the press without caveat, even though the report states that its "citation of, or reliance on, agency data in this report should not be taken as an OMB endorsement of all the varied methodologies used to derive benefits and cost estimates."[2]

I have several concerns with the reported estimates.

The estimates cover a small fraction of federal regulation.

The benefits and costs for fiscal year 2003 are based on agency estimates for only six regulations, or one-tenth of one percent of the final rules published in the Federal Register during the year. Of the 37 economically significant rules reviewed by OMB during the 12-month period, OMB classifies the vast majority (25) as "transfers," and suggest they simply shift money from one segment of society to another without imposing any net social costs or benefits. Of the remaining twelve "social regulations," issuing agencies estimated benefits or costs for only six.

These statistics highlight several problems with relying solely on information reported by agencies. The most obvious is the lack of information on the impacts (costs and benefits) of the major rules issued last year. By definition, an economically significant or major

[2] Draft Report 2004, p. 6.

on individual rules. In the course of its own reviews of significant regulations under Executive Order 12866, OMB analysts identify strengths and weaknesses of the methodologies agencies use to estimate benefits and costs. At a minimum, it should include those observations in this report in the form of a "report card" that highlights strengths and weaknesses of each analysis.

The reported benefits and costs are dominated by environmental regulations controlling a single pollutant.

EPA's estimates of the benefits and costs of its regulations comprise over 60 percent of the total benefits and costs reported for the 10-year period (and over 75 percent of the reported upper-bound benefits). The majority of EPA's benefits derive from reductions in exposure to one pollutant – particulate matter (PM). The draft report summarizes the uncertainties associated with benefits attributed to PM reductions, and many commentators have questioned the methodology EPA uses to derive these high benefits.[5] The fact that the benefits reported by OMB are so dominated by the questionable analytical approach used to value reductions in one pollutant illustrates the problem with relying uncritically on agency estimates.[6]

It is understandable that agencies try to portray their programs and initiatives in the best possible light. Because health-benefits estimation is subject to considerable uncertainty, there is typically a wide margin between what an agency thinks is "best" for public relations and what a statistician would define as a "best estimate" (most reliable estimate) for scientific purposes. OMB must work to eliminate these biases, which have a disturbing tendency to persist and "bioaccumulate," even as caveats and footnotes tend to disappear.

Conclusions and Recommendations for Improving Regulatory Accounting

In conclusion, for over thirty years, the White House has maintained, in one form or another, a centralized mechanism for executive branch oversight of regulations issued by federal agencies. President Clinton's Executive Order 12866 and legislative initiatives over the last decade have continued this tradition, reinforcing the philosophy that

[5] In our comments on OMB's 2001 report to Congress, we highlighted problems with EPA's estimates of these benefits, including (1) an unrealistic baseline, (2) uncertainties in the magnitude and causation of effects, (3) improper accounting for latency of effects, and (4) exaggerated valuation of health benefits. Public Interest Comment available at: http://www.mercatus.org/article.php/69.html.

[6] The Congress needs an accurate picture of the benefits and costs of regulation; not only to evaluate the performance of existing regulatory programs, but also to make important decisions about future legislation. On its web page for the Clear Skies initiative, EPA continues to promote a highly questionable estimate of benefits based on the same flawed analysis of the health effects of PM, claiming that: "The monetized benefits of Clear Skies would total approximately $113 billion annually by 2020, substantially outweighing the annual costs of $6.3 billion." On further reading, one learns that $110 billion of this is from an estimate of health effects, that an alternative estimate of these same health effects in only $21 billion, and (in a footnote) that even the $21 billion may be too high. See http://www.epa.gov/air/clearskies/benefits.html , accessed February, 18, 2004.

rule has an annual impact of $100,000,000 or more,[3] yet costs are presented for only fifteen percent of these rules. If each of the 31 rules not included in OMB's total imposed the minimum cost of $100,000,000 per year, the totals would be understated by $31 billion.

Furthermore, there are real costs associated with regulations that effect large "transfers" from one group to another. 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." At the very least, OMB should estimate the deadweight loss associated with these transfers. OMB has estimated the "excess burden of taxation," including the federal administrative costs and taxpayer burden, at 25 percent of revenues. It would be surprising if transfers effected by regulation had a deadweight loss any less than that. In addition, regulations that transfer wealth are typically the product of lobbying and other rent-seeking behavior on the part of the beneficiaries. Such rent-seeking will dissipate the benefits, so that costs assumed to be transfers may in fact represent real resource costs.[4] OMB should investigate and report these costs.

The reported benefits and costs are not based on an independent assessment.

As in previous years, OMB offers no independent assessment of the quality or usefulness of agency analyses, and correspondingly, the estimates presented in this report. 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. There is little value added in simply compiling the unverified representations of agency management. Such an approach would be unthinkable when dealing with budget expenditures; OMB should make an effort to impose some discipline on agencies' estimates of regulatory expenditures.

OMB's reports to Congress should also provide more detailed information about the assumptions underlying the benefit and cost estimates of the individual regulations that comprise the aggregate figures. OMB is in a unique position to provide some useful analysis; it has access to agency analyses, interagency discussions, and public comments

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[3] E.O. 12866 (available at: http://www.whitehouse.gov/omb/inforeg/eo12866.pdf) defines a significant regulatory action as one that "is likely to result in a rule that may:

(1) 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;

(2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;

(3) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or

(4) Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in this Executive order.

[4] Gordon Tullock. "The Welfare Costs of Tariffs, Monopolies and Theft" *Western Economic Journal*, 5, pp. 224-232. (1967).

regulations should be based on an analysis of the costs and benefits of all available alternatives, and that agencies should select the regulatory approach that maximizes net benefits to society, consistent with the law.

These executive and legislative branch actions, along with extensive academic research, have improved our understanding of the impact regulations have on consumers, workers and companies. However, we still lack a reliable mechanism, analogous to the fiscal budget process, for tracking regulatory expenditures and ensuring they produce desired outcomes.

I have three key recommendations for improving regulatory accounting.

- **OMB can improve the quality of information in future reports by holding agencies accountable for complying with new guidelines.**

First, though the increased transparency reflected in OMB's review procedures and in the report itself are welcome improvements to the regulatory process, the benefit and cost estimates in the draft report do not offer the American public an accurate picture of the impact of regulation. To be comparable in value to the fiscal budget figures, OMB's estimates must reflect an independent assessment of regulatory costs and benefits, and not simply provide a summation of agency estimates.

Over the coming year, OMB will be in a better position to hold agencies accountable for conducting analysis to ensure that the resulting benefit and cost estimates are reliable and robust. In September 2003, OMB issued guidelines for regulatory analysis that reflect generally accepted principles for evaluating the impacts of regulation. It is also developing guidelines for meaningful peer review. In the course of E.O. 12866 review, OMB should hold agencies accountable for following these guidelines, and return to agencies regulations not supported by analyses that comport with these guidelines. If it does, it may then be able to rely on agency estimates with confidence.

In the mean time, OMB should identify, in a concise but comprehensive manner, variations in agency methodologies used to estimate benefits and costs of individual regulations. It should present a "report card" for agency analyses that highlights their strengths and weaknesses.

- **A legislative branch review body could provide a more independent assessment of regulatory costs and benefits.**

It is not clear that the Office of Information and Regulatory Affairs, from its location within the Executive branch, is in a position to provide the necessary check or independent assessment of costs and benefits. A Congressional or other outside review body might be in a better position to report benefits and costs honestly and without deliberate bias.

While OMB should continue to enforce the principles of Executive Order 12866 and hold agencies accountable for ensuring proposed regulations do more good than harm, Americans may also benefit from a legislative branch oversight body. Indeed, Congress

has authorized a Congressional Office of Regulatory Analysis to be housed in the General Accounting Office, but it has not been funded. Such a body could provide Congress and U.S. citizens with an independent assessment of the total costs and benefits of regulation, and also help ensure that statutes are being implemented so that the benefits to Americans outweigh the costs.

- **Congress could explore further ways to treat regulatory expenditures in a manner similar to on-budget expenditures.**

An annual Regulatory Accounting Report issued with the federal budget is an important first step toward providing the same scrutiny to regulatory impacts as on-budget impacts. It may be fruitful to explore further the analogy between the budget process and regulatory process. For federal spending to be dedicated, Congress must first authorize an activity, and then appropriate the necessary resources. Regulatory spending (the cost consumers, workers and employers pay to comply with regulatory requirements), on the other hand, is authorized in statute – often in broad terms – with little follow-on action. In fact, regulatory spending is usually authorized in perpetuity, without a clear understanding of the commitments demanded or outcomes received.

As envisioned in H.R. 2432, Congress could explore ways to treat regulatory expenditures in a manner similar to on-budget expenditures, recognizing that regulations, like on-budget federal programs funded by taxes, divert private resources to broader national goals. A more explicit recognition of the expected costs as well as expected benefits of achieving regulatory goals will help policy makers allocate scarce resources to activities that will produce the greatest net social benefit.

Mr. OSE. Thank you, Ms. Dudley.

Our third witness is Dr. Belzer. He joins us as president of the Regulatory Checkbook Organization.

Sir, welcome to our committee. You are recognized for 5 minutes.

Mr. BELZER. I thank you, Mr. Chairman.

And, Mr. Schrock, it is true, my daughter will be getting married, and I appreciate your indulgence. I told her she is just going to have to postpone it; this is more important.

Mr. OSE. This is Congress. You can say things like that on the floor.

Mr. BELZER. I will pay.

Yes, thank you, sir. I am Dr. Richard Belzer, president of Regulatory Checkbook. Regulatory Checkbook is a nonpartisan and nonprofit organization whose mission is to advance the use of high-quality and policy-neutral science and economics to inform regulatory decisionmaking. Since earning my doctorate, I have over 15 years of experience performing and reviewing regulatory analyses, including a 10-year stint as a career economist in OMB's Office of Information and Regulatory Affairs.

I will briefly summarize for you the three points that I have made in greater depth in my written testimony.

First, the estimates of costs and benefits that are contained in OMB's draft report are unreliable and probably misleading. The estimates reported for individual regulations are unreliable because the agencies that prepared them had incentives to underestimate costs and overestimate benefits. The draft report consists of agency estimates and not those of OMB.

Estimates of the total benefits and total costs of Federal regulation have little or no informational value to me. Aggregation only magnifies the biases that are embedded in agency estimates for individual regulations, so the more regulations OMB includes in its reports, the more unreliable and misleading the totals become, particularly the net benefit estimate.

Congress should create incentives for higher quality estimates to be produced and reported, and I think substantial progress must first be made to improve the reliability of estimates for individual rules. Only then will it be possible to derive the useful estimates of the total estimates and costs of individual regulatory programs.

Second, I see no evidence of a trend indicating that the quality of regulatory analysis is improving. Although the methods of benefit-cost analysis continue to improve, its fundamental principles do not change. The most troubling problem I see with agency analyses isn't that they don't follow what are called best practices; rather, it is agencies too often do not abide by fundamental benefit-cost principles.

OMB's 2003 regulatory impact analysis guidelines differs little from previous editions issued in 1990, 1996, and in 2000. Agencies did not adhere to these principles as a general rule in these earlier guidance documents, and it is safe to predict, I think, that they will also fail to adhere to the principles set forth in the 2003 edition.

I am troubled by some language in OMB's draft report that it seems to excuse a low standard of agency performance. OMB should not make excuses for substandard agency performance by

mischaracterizing fundamental principles of analysis as best practices.

Third, if Congress wants regulatory analysis to be performed well and wants the information to be usable, I think it needs to help create an environment in which that can happen. Each agency has a monopoly over the production of regulatory analysis and controls the benefit and cost estimates reported to Congress. As in every other market, the key to improving quality is competition; quality will not improve without it. The public comment process alone is not sufficient to improve quality.

Congress can help make this market for high quality analysis by breaking up these monopolies and injecting competition. Most of the country's competent regulatory analysts work outside the Government; they rarely contribute much because there is barely a market for their services. Create a market for high quality analysis and supply will respond to meet this demand.

Give OMB the authority, and not just the responsibility, for providing Congress with reliable estimates of benefits and costs. The Regulatory Right-to-Know Act doesn't give OMB any statutory authority to determine which estimates are most reliable. With a competitive supply of analyses and this authority, OMB would have all the tools it needs to make future reports for Congress and the public, reliable indicators of the impacts, both costs and benefits, of Federal regulation.

Thank you very much for your time. I will answer any questions that you might have.

[The prepared statement of Mr. Belzer follows:]

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TESTIMONY OF
RICHARD B. BELZER, PH.D.
BEFORE THE SUBCOMMITTEE ON
ENERGY POLICY, NATURAL RESOURCES AND REGULATORY AFFAIRS
OF THE COMMITTEE ON GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES
FEBRUARY 25, 2004

Mr. Chairman and Members of the Committee, I appreciate the opportunity to testify on OMB's latest draft report on the benefits and costs of Federal regulation. I am Dr. Richard Belzer, President of Regulatory Checkbook, a nonpartisan and nonprofit organization whose mission is advancing the use of high-quality, policy-neutral science and economics to inform regulatory decision making. I have over 15 years' experience performing and reviewing regulatory analyses, including a ten-year stint as a career economist in OMB's Office of Information and Regulatory Affairs.

I will briefly summarize now the three points made in greater depth in my written testimony.

First, estimates of costs and benefits contained in OMB's draft report are unreliable and probably misleading.

- Estimates reported for individual regulations are unreliable because the agencies that prepared them had incentives to underestimate costs and overestimate benefits. The draft report consists of agency estimates, not those of OMB.

- Estimates of the total benefits and costs of Federal regulation have little or no informational value. Aggregation only magnifies the biases embedded in agency estimates for individual regulations. The more regulations OMB includes, the more unreliable and misleading the totals become.

- Congress should create incentives for higher quality estimates to be produced and reported. Substantial progress must first be made to improve the reliability of estimates for individual rules. Only then will it be possible to derive useful estimates of the total benefits and costs regulatory programs.

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Second, I see no evidence of a trend indicating that the quality of regulatory analysis is improving.

- Although the methods of benefit-cost analysis continue to improve, its fundamental principles do not change. The most troubling problem with agency analyses isn't that they don't follow "best practices." Rather, it is that agencies too often do not abide by these fundamental principles.

- OMB's 2003 regulatory impact analysis guidance differs little from previous editions issued in 1990, 1996 and 2000. Agencies generally did not adhere to the principles set forth in these earlier guidance documents, and it is safe to predict that they also will fail to adhere to the principles set forth in OMB's 2003 edition.

- OMB's draft report contains language that excuses a low standard of agency performance. OMB should not make excuses for substandard agency performance by mischaracterizing fundamental principles as best practices.

Third, if Congress wants regulatory analysis to be performed well, then it needs to help create an environment in which that can happen.

- Each agency has a monopoly over the production of regulatory analysis and controls the benefit and cost estimates reported to Congress. As in every other market, the key to improving quality is competition. Quality will not improve without it. The public comment process alone is not sufficient.

- Congress can help "make the market" for high-quality analysis by breaking up these monopolies and injecting competition. Most of the country's competent regulatory analysts work outside the government. They rarely contribute much because there is barely a market for their services. Create a market for high-quality analysis, and supply will respond to meet this demand.

- Give OMB the *authority*, and not just the *responsibility*, for providing Congress with reliable estimates of the benefits and costs of regulation. The Regulatory Right-to-Know Act doesn't give OMB any statutory authority to determine which estimates are most reliable. With a competitive supply of analyses and this authority, OMB would have all the tools it needs to make future reports for Congress and the public.

OMB professionals are well-equipped to do this. One can imagine OMB using what's called "final-offer arbitration" to choose amongst competing estimates This procedure is

best known as the one used by Major League Baseball to decide whether the player's or the team's estimate of market value is most reasonable. For those who distrust OMB, final-offer arbitration has the advantage of denying OMB any authority to come up with its own estimates.

To sum up, OMB's draft report relies on agency analyses, and agency analyses are generally unreliable. Adding up dozens of individually unreliable estimates does not yield reliable estimates of the total impact of Federal regulation. Fundamental change is needed to improve this situation. Congress can foster competition and break up agency monopolies in the production of regulatory analysis. Second, Congress can really make OMB responsible by giving it the statutory authority to choose the best among competitors.

Thank you very much for the opportunity to testify today on this important subject. I would be happy to answer any questions you might have.

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1. Estimates of Costs and Benefits In OMB's Draft Report Are Biased, Unreliable and Misleading

As it has said in every preceding report to Congress, OMB states at least a dozen times that the benefit and cost estimates contained therein belong to the agencies themselves, and not to OMB.[1] For independent agencies exempt from review under Executive order 12866, OMB obtained cost and benefit estimates from the General Accounting Office, which itself simply reported what these agencies provided.[2]

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[1] See, e.g., "OMB used agency estimates where available" (p. 3); "OMB has not made any changes to monetized agency estimates other than converting them to annual equivalents" (p. 6); Table 4 title: "Summary of Agency Estimates for Final Rules" (pp. 10-19); Table 9 title: "Agency Estimates of Benefits and Costs of Major Rules" (pp. 41-49; "The adoption of a uniform format for annualizing agency estimates allows, at least for purposes of illustration, the aggregation of benefit and cost estimates across rules" (p. 32). Emphasis added in all cases. Note that OMB says its uniform format permits aggregation "at least for purposes of illustration" only.

[2] See, e.g.: "[OMB] also include[s] in this chapter a discussion of major rules issued by independent regulatory agencies, although OMB does not review these rules under Executive Order 12866. This discussion is based on data provided by these agencies to the

Former OIRA Administrator and OMB Director Dr. James Miller testified to this Subcommittee last year that "the major problem lies...in the unwillingness of the agencies to comply fully with OMB's request for relevant information."[3] He noted that the problem was rooted in perverse incentives:

> [N]ot all agencies have bothered to estimate benefits and costs of their proposed regulations, and those that do have not provided consistent estimates for their various activities... [M]ost of the deficiency arises from a lack of enthusiasm agencies have for meeting such requirements.[4]

As Dr. Miller explained, "the agencies have a bias to show high benefits and low costs of their work." While it is true that opponents of regulation have incentives to overstate costs and understate benefits, "the final determinations are made by the agencies, [so] the agency bias tends to dominate—that is, to inflate estimates of benefits and deflate estimates of costs".[5]

At only a few places in the draft report does OMB say that it doesn't endorse these agency estimates. For example, on page 37 OMB states that it "has not made any changes to agency monetized estimates," and that differences in agency estimation methods "remain embedded in the tables". On page 38 OMB washes its organizational hands of the entire endeavor, saying that it has "relied in many instances on agency practices" so "citation of, or reliance on, agency data in this report should not be taken as an OMB endorsement."[6]

General Accounting Office (GAO) under the Congressional Review Act" (p. 2, emphasis added).

[3] "Statement of James C. Miller III Before the Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs of the Committee on Government Reform, U.S. House of Representatives, March 11, 2003," p. 1.

[4] Miller (2003), p. 2.

[5] Miller (2003), pp. 2-3.

[6] OMB needs to do more to deter readers from "citing" or "relying" on these data as representing OMB's own views, which seems certain to happen. Given its lack of statutory authority to overrule agencies' cost and benefit determinations, OMB's only choice under its own information quality guidelines is to invoke the exception to the definition of "information" in Section V.5. This exception excludes material where the "presentation makes it clear that what is being offered is someone's opinion [in this case, the opinions of

VAST AREAS OF FEDERAL REGULATION ARE MISSING

The coverage of the OMB report is limited in fundamental ways distinct from methodological constraints.[7] The two most important of these reflect the limited scope of OMB's regulatory oversight. First, huge areas of formal regulation are missing from the report, such as regulations issued by independent commissions exempt from OMB review such as the Federal Communications Commission (FCC), the Securities Exchange Commission (SEC), the Federal Trade Commission (FTC), and several others.[8] Also missing is the regulatory effect of regulation by litigation, whether through anti-trust (*e.g.*, *U.S. v. Microsoft)* or the application of novel regulatory interpretations of existing environmental rules (*e.g.*, "New Source Review").

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federal agencies] rather than fact or the agency's [that is, OMB's] views." See 67 *Fed. Reg.* 8460. A clear statement should be added at the outset, and repeated in the Executive Summary and as footnotes to every table, stating that the estimates in the report reflect the opinions of the agencies and not those of OMB.

[7] The most obvious areas where methodological constraints apply involve homeland security and environmental and occupational health risk. Measuring the social benefits of efforts to deter terrorism is inherently difficult. In environmental and occupational health, estimates of risk are used as inputs into the value of risk reduction. The methods used to estimate these risks are purposefully biased in ways that exaggerate the scope and magnitude of baseline risk and the social benefits of regulatory intervention to reduce them.

[8] 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. The SEC has promulgated major regulations regarding corporate governance in securities and accounting. OMB's report discloses no costs or benefits from these regulations. By next year the SEC is expected to have issued major new regulations concerning mutual funds. Next year's report to Congress is likely to include no estimates of costs and benefits for these actions. The FTC's "Do Not Call List" regulation may be one of the most popular in American history, but estimates of its costs and benefits are limited.

Second, there is a massive body of underground regulation that occurs through what OMB has called "problematic" guidance.[9] These actions are not vetted by OMB nor are they generally subject to the due process requirements of the Administrative Procedure Act. The costs and benefits of problematic guidance are rarely, if ever, estimated. If an agency issues a nominally non-regulatory and draft opinion, such as a draft risk assessment for a chemical, the document often will lead to substantial real-world impacts that are neither estimated nor accounted for, and they will be missing from OMB's annual accounting statement.

Replacing problematic guidance with regulation does not necessarily remedy the regulatory accounting problem. For example, if an agency replaces guidance with a rule, impacts will appear minor if the agency uses as its analytic baseline the state of the world *after* substantial compliance with the guidance has occurred. The analytically correct baseline is the state of the world prior to the guidance, but little or no information may be available that sheds light on these effects.

OMB has authority under Executive order 12866 to review these actions. All *regulatory actions* are potentially subject to OMB review, where that term of art means "any substantive action ... that promulgates or is expected to lead to the promulgation of a final rule or regulation."[10] OMB exercises this authority very rarely, however.

WHY AGGREGATION OF COST AND BENEFIT ESTIMATES MAKES THE REPORT 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.[11]

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[9] OMB, "Informing Regulatory Decisions: 2003 Report to Congress on the Costs and Benefits of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities," September 2003.

[10] See 58 Fed. Reg. 51737-51738.

[11] It is widely believed that costs are easier to estimate than benefits, and that this asymmetric constraint leads to the underestimation of net social benefits. This belief is perpetuated by a fundamental misunderstanding of benefit-cost analysis. Properly understood, "cost" is not measured as dollars expended to comply. Rather, it is the value of

From its very first report OMB has warned Congress that aggregation yields information of limited value.[12] These warnings have not been heeded, and OMB has been persistently criticized for failing to accurately characterize the true consequences of regulation. The remedy many critics have sought is a more comprehensive report that includes more regulations. OMB has responded by providing exactly what these critics say they want.

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benefits foregone resulting from the regulatory reallocation of resources. Benefits foregone are generally larger than expenditures by the sum of consumers' surplus obtained from the original resource allocation. Therefore, if benefits are difficult to estimate then costs are doubly so—the analyst must first estimate what resources must be reallocated, and then estimate the social benefits foregone due to regulatory reallocation. Whenever this is not done, cost estimates are downwardly biased.

This is not to say that benefits are always *easier* to estimate than costs. As noted earlier, the benefits of deterring terrorism (and a host of other low-probability high-consequence events) are especially difficult to estimate. On the other hand, if opponents of some of these measures (*e.g.*, actions taken under the USA Patriot Act, Pub. L. 107-56) are correct in that they infringe on civil rights and other vital intangible values, costs could well be more difficult to estimate than benefits.

[12] In its 1997 Report to Congress, OMB warned that aggregation provided little or no useful information:

> [K]nowing the *total* costs and *total* benefits of all of the many and diverse regulations that the Federal government has issued provides little specific guidance for decisions on reforming regulatory programs.
>
> [A]n excessive amount of resources should not be devoted to estimating the total costs and benefits of all Federal regulations. To the extent that the costs and benefits of specific regulatory programs can easily be combined, some indication of the importance of regulatory reform can be inferred by the magnitude of these estimates, but knowing the exact amounts of total costs and benefits, even if that were possible, adds little of value.

See OMB, "Chapter II. Estimates of the Total Annual Costs and Benefits of Federal Regulatory Programs," Report to Congress on the Costs and Benefits of Federal Regulations, September 30, 1997.

While the critics' diagnosis is correct their prescription has been ill-advised. Making the report "more comprehensive" only makes aggregate estimates more misleading. The more regulations OMB includes, the more unreliable and misleading aggregate estimates become. Therefore, demanding that OMB to make its annual report to Congress more comprehensive is asking OMB to make it worse.

Congress could remedy this situation by reducing its emphasis on the aggregate costs and benefits of regulation and focus instead on securing reliable, unbiased and policy-neutral estimates for individual rulemakings. In section 3 I offer specific suggestions for how Congress can help make this happen.

2. The Problem of Unreliability in Regulatory Analysis Is Not Going Away

I see no reason to believe that agency regulatory analysis is going to improve. I was the principal author of the final draft of OMB's 1990 RIA Guidance, and I contributed to OMB's so-called "best practices" document issued in 1996. With rare exception, the 1996 document actually contains minimum standards for credible regulatory analysis. By incorrectly characterizing minimum standards as "best practices" OMB signaled to the agencies that it did not expect them to consistently adhere to minimum standards.[13]

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[13] In OMB's 1996 guidance titled "Economic Analysis of Federal Regulations Under Executive Order 12866," the phrase "best practices" appears only once in the body of the document in a technically complex section on the use of contingent valuation methods:

> **Principles and Methods for Valuing Goods That Are Not Traded Directly or Indirectly in Markets**. Some types of goods, such as preserving environmental or cultural amenities apart from their use and direct enjoyment by people, are not traded directly or indirectly in markets. The practical obstacles to accurate measurement are similar to (but generally more severe than) those arising with respect to indirect benefits, principally because there are few or no related market transactions to provide data for willingness-to-pay estimates.
>
> For many of these goods, particularly goods providing "nonuse" values, contingent-valuation methods may provide the only analytical approaches currently available for estimating values. The absence of observable and replicable behavior with respect to the good in question, combined with the complex and often unfamiliar nature of the goods being valued, argues for great care in the design and execution of surveys, rigorous

OMB's 2003 guidance does not commit this error, so one might reasonably have hoped that OMB now intends to enforce minimum performance standards. But OMB's draft Report to Congress contradicts this hope. On page 33 (Appendix A) and on page 3 (footnote 1), OMB says, "The guidance recommends what OMB considers to be 'best practice' in regulatory analysis, with a goal of strengthening the role of science, engineering, and economics in rulemaking." OMB fails to admit that this goal has been with us for a generation. Once again, minimum quality standards are being incorrectly characterized as "best practices". Once again, agencies are being told that they will not be expected to actually adhere to minimum standards.[14]

If Congress wants reliable estimates of the impacts of federal regulation, it needs to consider ways to help make that happen. Simply directing OMB to produce high-quality estimates will not work, and asking the General Accounting Office to do it is unlikely to be more effective. Note that OMB relies on GAO estimates for the costs and benefits of regulations issued by independent agencies exempt from OMB review. GAO, in turn, simply accepts at face value what the independent agencies say.

3. Congress Should Help Create the Incentives for High Quality Regulatory Analysis to be Produced

To be fair to OMB, it has very few "carrots" or "sticks" to motivate agencies to improve the quality of their regulatory analyses. OMB's only real stick is to rely on its Executive authority to "return to the agency for further consideration" draft regulations that do not adequately comply with the regulatory policy and principles set forth in Executive order 12866, including applicable guidance on the conduct of regulatory analysis. Many analysts, including myself when I worked in OIRA, longed for a day in which a high quality

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> analysis of the results, and a full characterization of the uncertainties in the estimates to meet best practices in the use of this method (emphasis added).

See §III.B.4. Most of the 1996 document consisted of minimum standards for performance, such as understanding market failure and other rationales for regulatory intervention; correctly distinguishing costs from benefits, distinguishing both from transfer payments, and estimating them from appropriate baselines; and discounting future effects (including discounting both future benefits and future costs by the same discount rate).

[14] Worse, compliance apparently depends on voluntary adherence to the guidelines: "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." This appears to be the triumph of hope over more than 20 years' experience.

standard was consistently and apolitically enforced by using this stick as frequently as necessary.

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.[15] 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.

Let's also be clear that if OMB were to return for further consideration every draft regulation whose analysis failed to meet the minimum standards set forth in Circular A-4, very few regulations would ever be published. And it would cause a firestorm.

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[15] "[W]e have sent clear signals to agencies that we care about regulatory analysis, QUALITY regulatory analysis. We are using both the carrot and the stick. The carrot we have offered is more deferential OMB review of proposals that agencies have voluntarily subjected to independent peer review. Administrator Whitman's recent decision on arsenic, whether you like it or not, was supported by just that type of review. The Bush Administration recognizes that we should consider and account for the consensus views of the leadership of the scientific community, regardless of whether it leads to a pro- or anti-regulation result. The stick has been a revival of the dreaded 'return letter'. In the last three years of the Clinton Administration, there were exactly zero return letters sent to agencies for poor quality analysis. I have signed more than a dozen such return letters in the last six months and they are available for scrutiny on OMB's web site. Recently we have witnessed some agencies simply withdrawing rules rather than face a public return letter. Knowing that we care, agencies are beginning to invite OMB into the early stages of regulatory deliberations, where our analytical approach can have a much bigger impact" (emphasis added). See John D. Graham, "Presidential Management of the Regulatory State," Speech to Weidenbaum Center Forum, "Executive Regulatory Review: Surveying the Record, Marking It Work," National Press Club, Washington, DC, December 17, 2001, online at http://www.whitehouse.gov/omb/inforeg/graham_speech121701.html.

CAN PEER REVIEW HELP?

Some would argue that peer review of agency regulatory analyses is the key to improving quality. In fact, OMB has proposed a government-wide program of peer review for highly influential information,[16] and regulatory analysis is the category of information that would be most seriously affected. That's because regulatory analyses are almost never peer reviewed except by OMB career analysts. At the same time, I have grave doubts concerning whether agency-sponsored peer review would ever be adequately independent,[17] or genuinely effective in improving quality as long as agencies retain the discretion to adopt or reject the advice they receive.[18] Furthermore, there is a serious risk that some agencies would use peer review to hamstring the career analysts at OMB. That would be a huge step backwards. Peer review has an important role to play, but it is a mistake to think that by itself it will be sufficient.[19]

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[16] Office of Management and Budget, "Proposed Bulletin on Peer Review and Information Quality", 68 *Fed. Reg.* 54023-54029.

[17] Independence is inherently problematic when the sponsor of peer review 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. If agency regulatory analyses are subjected to external and independent peer review, OMB ought to have a substantial role in selecting the reviewers and writing the Charge, for no agency or office of the Executive branch is as independent from the agencies as OMB.

[18] Congress could require agencies to adhere to the technical recommendations of peer review panels that review regulatory analysis. Adhering to these recommendations would not compromise an agency's decision making discretion. Also, Congress could give OMB statutory authority to determine whether agency adherence has been sufficient.

[19] This is precisely what happened in 1997 prior to the transmittal by the Environmental Protection Agency's first retrospective Report to Congress on the benefits and costs of the Clean Air Act (*Benefits and Costs of the Clean Air Act, 1970-1990,* also called the *"812 Retrospective"*). This report had been extensively peer reviewed by a committee of the EPA's Science Advisory Board, which after several requests for significant changes finally gave up. When career economists from OMB and other federal agencies identified fatal analytic flaws that egregiously exaggerated estimated benefits—some of which had been noted by the SAB—EPA refused to correct errors on the ground that the SAB had already approved the report and there was a judicial deadline mandating transmittal. The

WHAT ABOUT A REGULATIORY BUDGET?

In his testimony last year Dr. Miller said, "OMB should be given a stronger role in policing this bias by replacing agency reports of benefits and costs with more objective estimates..."[20] Whereas Dr. Miller would implement this through a regulatory budget, I am less sanguine about the likely effectiveness of such an approach. Nothing in the concept of regulatory budgeting overcomes the perverse incentives agencies have to understate costs.

In my judgment, a regulatory budget would exacerbate these perverse incentives. 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. In principle, once an agency's budget is reached it would be done for the fiscal year

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resulting impasse led to an historic event—the administration declined to support EPA's estimates:

> A final, brief interagency review, pursuant to Circular A-19, was organized in August 1997 by the Office of Management and Budget and conducted following the completion of the extensive expert panel peer review by the SAB Council. During the course of the final interagency discussions, it became clear that several agencies held different views pertaining to several key assumptions in this study as well as to the best techniques to apply in the context of environmental program benefit-cost analyses, including the present study. The concerns include: (1) the extent to which air quality would have deteriorated from 1970 to 1990 in the absence of the Clean Air Act, (2) the methods used to estimate the number of premature deaths and illnesses avoided due to the CAA, (3) the methods used to estimate the value that individuals place on avoiding those risks, and (4) the methods used to value non-health related benefits. However, due to the court deadline the resulting concerns were not resolved during this final, brief interagency re-view. Therefore, this report reflects the findings of EPA and not necessarily other agencies in the Administration. Interagency discussion of some of these issues will continue in the context of the future prospective section 812 studies and potential regulatory actions (emphasis added).

See *812 Retrospective*, p. ES-2.

[20] Miller (2003), p. 3.

just as if it had spent its budget appropriations. Excess fiscal spending is controlled by the Anti-Deficiency Act, and additional budget dollars cannot simply be conjured up. It is difficult to imagine how to craft, much less enforce, an Anti-Deficiency Act for regulatory costs.

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.

IMPROVING QUALITY BY INJECTING COMPETITION

A better approach is for Congress to create incentives for the preparation of high quality analyses to be produced. As in every other market, competition is the key to improving quality. When it comes to regulatory analysis, each federal agency has monopoly power over what information is finalized and disseminated. As every freshman economics student learns, monopolies do not foster quality. Whether they work for industry or advocacy groups, outside experts can submit public comments to their hearts' content, but as Dr. Miller testified last year, the final determinations are made by the agencies. These final agency determinations are what OMB submits in its Reports to Congress, but at least in part that's because OMB doesn't have competitive information from alternative sources.

Congress could help "make the market" for high-quality regulatory analyses. by breaking up these agency monopolies and injecting in each one a therapeutic dose of competition. Federal agencies may have monopolies to decide how much social benefits and costs to report, but they do not have a corner on expertise. Indeed, there are many competent professionals outside the government who are exquisitely well-trained to perform regulatory analysis. Open the door to competition by creating a market for high-quality, policy-neutral, and independent regulatory analysis and they will respond. The agencies also will respond—first by trying to undermine the legitimacy of their competitors, and once that fails getting to work, by improving the quality of their own work to avoid being driven out of the regulatory analysis business.

The Regulatory Right-to-Know Act 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. Subjecting the agencies to the perils of competition requires Congress to remedy this asymmetry by giving OMB the *statutory authority*, and not just the *reporting responsibility*, to make these determinations. If for whatever reason you do not have sufficient trust in OMB's judgment,

ask the General Accounting Office to evaluate the same information and reach its own conclusions. Even OMB can benefit from some competition. [21]

"Final-offer arbitration" (FOA) is probably the best available tool for OMB (or GAO) to use in determining which competing analysis is best. 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.[22] 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 others'.

For Congress, FOA would reduce the gaps among competing regulatory analyses and narrow the range of uncertainty concerning the likely benefits and costs of individual regulatory actions. Once a large fraction of regulations issued under a given regulatory program have been subjected to the FOA process, Congress can realistically develop greater confidence that estimates of programmatic benefits and costs are reliable.

With a minor amount of training in FOA methods, OMB career analysts would be well-equipped to choose from an array of competing estimates which one best adheres to the fundamental principles of benefit-cost analysis and Circular A-4. For those who for whatever reason distrust OMB, FOA also has the advantage of requiring OMB to choose from the estimates provided and denying OMB any authority to come up with its own, unsubstantiated figures.

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[21] Some may argue that third parties should not prepare regulatory analyses because it is an inherently governmental function. This is true 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.

[22] A key to the success of FOA in Major League Baseball is an agreement by both sides to respect the outcome. In political environments such as Federal regulation, this would likely be more difficult.

Mr. OSE. Thank you, Dr. Belzer.

Our next witness is the president of the Public Citizen Organization, Ms. Joan Claybrook.

Ma'am, welcome again.

Ms. CLAYBROOK. Thank you very much, Mr. Chairman. I appreciate the opportunity to be here, and the invitation.

My name is Joan Claybrook, and I am president of Public Citizen, which is a national public interest organization representing consumer interests, and I am here to talk about the regulatory accounting legislation and the draft report for 2004 to the Congress on the costs and benefits of Federal regulation.

We strongly object to the use of regulatory accounting because we believe that, when you look at the facts, it is not able to support itself scientifically or intellectually. The notion of a regulatory budget in which Federal agencies have to compete with each other in order to pose a cost on industry in the private sector is highly improper, we believe, and inappropriate. The goal to control regulation that some agency rules might have been eliminated and new ones not issued, no matter how pressing the need, it seems to me, is morally repugnant.

The pilot projects called for in the Paperwork and Regulatory Improvements Act that you have would be the first step toward establishing a regulatory budget, and a requirement that is not supportable, we believe, that all agencies conduct cost-benefit analysis.

I would refer you in my full testimony, which I would hope would be submitted for the record, that the court of appeals, when we challenged the tire monitoring rule that OMB adjusted a change and degraded, they said that NHTSA was to be reminded that "cheapest is best" is contrary to Supreme Court precedent, and the agency is supposed to place "a thumb on the safety side of the scale." So the courts, at least, very recently in this case, do not agree that cost-benefit analysis is just a numerical calculation.

I would like to comment for just 1 second on the whole idea of the 10-year issue which you raised in this report. The major problem with it is not is it 5 years or 10 years or 15 years, in our view; it is that once a rule has been issued and the regulatory analysis done, then what happens is industry, which has complained bitterly about the costs, and often exaggerated the costs in its submissions to the agencies, then goes about implementing the rule if it is issued; and, when they do that, you see a dramatic reduction in the cost. And, so the estimates that are made, that are used by OMB, where they just assemble all the information that was evaluated when the rule was being considered, is now completely inaccurate.

And, I would like to submit for the record a report that has just come out this month by Ruth Ruttenberg, who is an economist, called "Not Too Costly, After All: An Examination of the Inflated Cost-Estimates of Health, Safety and Environmental Protections."

Mr. OSE. Without objection.

Ms. CLAYBROOK. Thank you.

There is a growing body of evidence that establishes that regulatory accounting suffers from fatal flaws; it requires a pretense that accurate and reliable data are presented on both sides, which we all know is not accurate. It is very hard to get benefit data; it

is far easier to get cost data. And, as I just mentioned, cost data changes dramatically when a rule takes effect.

The committee is familiar with the groundbreaking work, I believe, of Professor Lisa Heinzerling, who demonstrated that studies claiming regulations caused statistical murder were based on fictional regulations, they were never in fact ever issued, which I would like to submit a summary for the record.

Another new book called "Grading the Government," by Professor Richard Parker, examines three influential studies often cited to support regulatory accounting by John Morrall, John Graham, and Tammy Tengs and Robert Hahn; and all of these are rife with errors, avoidable errors such as undisclosed data, non-replicable calculations, guesses presented as facts, and gross underestimates of the numbers of lives saved.

One of the major issues that I think that the committee needs to consider, in addition to the fact that the small business agency represents only, in its study, the costs, the Crain study only talks about costs, but never about benefits. Why wouldn't the committee ask for the benefits as well? It seems to me that is a major issue. No manufacturer would go and spend money to build a factory and not consider the benefits of building the factory, only the costs. It is just irrational. And, so I hope that the committee will ask that the Crain study consider benefits as well.

But, the other issue is that when you look at the regulations that you are looking at before this committee, mostly health, safety, and environmental regulations, you have 40,000 deaths a year on the highway, 42,000 to be exact; you have close to 50,000 from occupational safety and health problems; you have close to 100,000 adverse reactions under the Food and Drug Administration rules and laws; you have environmental deaths that are almost incalculable, or injuries or sufferings, such as from bad air, that is clear. And, so my question is when you are looking at all these deaths and then you consider homeland security or you consider the Defense Department costs for protecting this Nation, there is no relationship; the deaths for just the military are far exceeded on the highway, just on the highway, than they are in foreign lands.

So, I think that it is totally skewed in terms of the imposition of these requirements when you don't have a balancing here of where the harm is occurring in this Nation; it is like having doctors treat a minor disease instead of treating a major disease. And that, it seems to me, is what is happening with this focus on regulatory accounting, which costs the Government a lot; it takes a lot of agency work and time to do these analyses and to produce a regulatory accounting that I think I have made pretty clear is inaccurate.

I would like a chance to answer some questions, perhaps, Mr. Chairman. I see I am out of time, and there is much more to say. Thank you so much.

[The prepared statement of Ms. Claybrook follows:]

Statement of Joan Claybrook,
President, Public Citizen,
On Regulatory Accounting and the
Office of Management and Budget's 2004 Draft Annual Report
to Congress on the Costs and Benefits of Federal Regulations

United State House of Representatives
Committee on Government Reform
Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs
Washington, D.C.
February 25, 2004

Mr. Chairman and Members of the Committee:

I am pleased to offer this testimony on regulatory accounting and the Office of Management and Budget's (OMB's) 2004 Draft Annual Report to Congress on the Costs and Benefits of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities. I am President of Public Citizen, a national public interest organization with 160,000 members nationwide that represents consumer interests through lobbying, litigation, regulatory oversight, research and public education. For 33 years, Public Citizen has had direct, practical involvement with a wide variety of federal health and safety protections and has represented consumer groups, labor unions, worker groups, and public health organizations in standard-setting proceedings and in litigation involving the Occupational Safety and Health Administration [OSHA], the Environmental Protection Agency [EPA], the Food and Drug Administration [FDA], the Consumer Product Safety Commission [CPSC], the U.S. Department of Agriculture [USDA], the National Highway Traffic Safety Administration [NHTSA], the Federal Motor Carrier Safety Administration [FMCSA] and other health and safety agencies.

The subject of my testimony today is the 2004 draft annual Report to Congress by the Office of Information and Regulatory Affairs [OIRA] within the Office of Management and Budget on the Costs and Benefits of Federal Regulations. The Report continues to be published despite a growing body of evidence that establishes the utter bankruptcy of regulatory accounting as a useful tool for public policy. Public Citizen continues to object to the use of regulatory accounting and views each successive cost/benefit Report to Congress as increasingly hostile to good government and the well-being of the public.

In support of these objections, I will cite four major new publications and studies that should both significantly enhance public understanding of the factual deficiencies and conceptual fallacies that underlie cost/benefit accounting, and expose the distortion of scientific information that is increasingly poisoning regulatory analysis. Next, I will describe what is missing from OMB's Reports to Congress, information without which neither Congress nor the public can fairly evaluate the effects of federal regulatory activity. Finally, I will conclude my testimony by expressing our opposition to OMB's solicitation of nominations for changes to regulations affecting the manufacturing sector.

We believe this is nothing more than a deregulatory "hit list" similar to the discredited effort of two years ago.

I. The Track Record of Regulatory Accounting Shows It is a Resounding Failure.

In prior testimony, I described our opposition to the practice of regulatory accounting. This practice involves monetizing and totaling both the costs and benefits of disparate public protections and then subtracting one from the other. The result is presented as a "net sum" which assesses the worth of all federal health, environmental and safety protections.

Because of the inherent and highly subjective limitations of cost/benefit methodology, it can never provide meaningful information. While this Subcommittee may want to insist on a more comprehensive accounting, we believe such a project is deeply misguided as well as a practical impossibility. Energy would be better directed toward agencies' fulfillment of their statutory duties to the public as assigned by Congress.

Proponents of regulatory accounting would use aggregated cost and benefit figures as the first step towards a "regulatory budget," in which federal agencies would have to compete with each other in order to impose a tightly-controlled amount of costs upon the private sector. If costs to the private sector exceed the cap established in the budget, it is suggested, some agency rules might have to be eliminated and new rules could not be issued, no matter how pressing the need.

The pilot projects called for in H.R. 2432, the Paperwork and Regulatory Improvements Act of 2003, would be the first step toward establishing the regulatory budget. This is a deeply mistaken effort that should end even before it begins. One need look no further for the underlying purpose of the project than to notice that the agencies singled out for the pilot projects are those that protect the environment and promote safety in the workplace and on the highways. The public in overwhelming majorities supports these consumer and environmental protections.

Yet, as has been repeatedly demonstrated, corporations will act in their own short-term best interests to maximize profit. Governmental regulation has always been and remains necessary to stop the unfettered despoilment of public lands and to protect the public health and safety from corporate negligence.

Regulatory accounting suffers from fatal flaws that make it useless for any purpose other than lending a false appearance of technical objectivity to a political decision to benefit regulated interests over the public's interest. Among the more fundamental of those flaws are the following:

- It involves a pretense that accurate and reliable data are presented on both sides of the ledger, when they are not and cannot be.

- Its intellectual underpinnings are dishonest. Authors of the most fundamental studies advanced in support of cost/benefit analysis substituted their own numbers in place of government data and/or included estimates of fictional regulations that were never enacted or, in some cases, never even proposed by any government agency to reach the desired conclusion.

- The conclusions are highly manipulable because they are based on a raft of often unsupported assumptions, a change in any one of which could affect the outcome.

- It is biased toward eliminating regulations opposed by industry because cost calculations are based on estimates provided by industry that are often highly inflated and rarely retrospectively or concurrently validated by the agencies.

- It is historically incorrect: regulation can produce benefits that help industry by limiting the risk, and forcing the development of, innovative products and processes.

- Both costs and benefits must be quantified, with the result that the many unquantifiable benefits are simply eliminated from consideration - even when those are the very benefits that the government action was intended to produce.

- In an effort to "monetize" all benefits, it devalues the longest lasting benefits and produces results repugnant to a democratic society, such as assigning different dollar values to the lives of different categories of citizens and disregarding responsibility for succeeding generations.

- It is a significant waste of public resources, particularly for those agencies charged with protecting the public health, which are already starved for funds.

- The practice is profoundly out-of-step with the necessary protective role of government as a check upon market excesses, which the American public has witnessed in abundance in recent years.

Even with all the intrinsic distortions of regulatory accounting, OMB's Reports to Congress have established one thing: the benefits of federal regulations far outweigh the costs. If the point was to assess the value produced by federal regulatory activity, we could stop now, confident in the effectiveness of a framework under which Congress establishes public policy and the agencies, with public participation, work out the necessary details of implementation. Unfortunately, the real objective appears to be to subvert that framework.

A. OMB's 2004 Draft Report to Congress Perpetuates the Underlying Limitations of Regulatory Accounting and Demonstrates the Manipulability of the Numbers.

As has become customary with OMB's Reports to Congress, the 2004 draft

Report begins by perfunctorily acknowledging its serious shortcomings:

- Monetized costs and benefits could be calculated for only six rules, half of the 12 "social regulations" to which OMB has chosen to limit its report.[1]
- In many instances, agencies were unable to quantify all benefits and costs. The monetized estimates that OMB presents necessarily exclude the unquantified benefits.[2]
- It is difficult to estimate and aggregate the costs and benefits of different regulations over long time periods and across many agencies using different methodologies. Any such aggregation involves the assemblage of benefit and cost estimates that are not strictly comparable.[3]
- The benefits of a reduced risk of terrorism have proven very difficult to quantify and monetize.[4]

Despite its admission of the incompleteness and unreliability of the data, OMB nonetheless proceeds to present what it calls "Estimates of the Total Annual Benefits and Costs of Major Federal Rules" for two time periods, the year ending in September 2003 and the ten year period from October 1993 to September 2003. What is perhaps most remarkable about these aggregate numbers is how different the 10 year benefit total is in the 2004 Report in comparison to the 10 year total presented in the 2003 Report to Congress.

2004 Report: October 1993 to September 2003 (in millions of dollars)
Benefits: $62,091 - $168,098 Costs: $34,156 - $38,958[5]

2003 Report: October 1992 to September 2002 (in millions of dollars)
Benefits: $146,812 - $230,896 Costs: $36,625 - $42,813[6]

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[1] "Informing Regulatory Decisions: 2004 Draft Report to Congress on the Costs and Benefits of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities" [2004 draft Report], p. 3.

[2] Id. For example, nonmonetized benefits of EPA's Standards for Concentrated Animal Feeding Operations include reduced contamination of coastal and estuarine waters, reduced pathogen contamination of groundwater, reduced human and ecological risks from antibiotics, hormones, metals, and salts, improved soil properties, etc. Id., p. 15, Table 4.

[3] Id. OMB states that it expects costs and benefits to become more comparable across agencies and programs as agencies adopt the recommended best practices in the regulatory analysis that took effect on January 1, 2004. If this happens, it will merely represent a consistent use of a defective calculus. Moreover, instead of helping agencies understand how to meet existing analytical requirements, OMB has introduced a new level of complexity. For rules involving annual economic effects of $1 billion, agencies will now be required to "try to provide some estimate of the probability distribution of regulatory benefits and costs." OMB Circular A-4, Regulatory Analysis, p. 40. Strikingly, a note of caution was sounded by anti-regulation law professor Kip Viscusi who, in the role of peer reviewer, expressed concern that the emphasis on probability distribution "may lead to dismissal of risks that cannot be proven conclusively" and made the point that "[i]f risks are required to be shown to be statistically significant based on classical tests, then we should close down our homeland security operation because its policies will never pass such a test."

[4] Id., p. 5.

[5] Id., p. 5, Table 2.

[6] "Informing Regulatory Decisions: 2003 Report to Congress on the Costs and Benefits of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities," Office of Management and

For the 10 year period covered in the 2004 draft Report, the cost figures are roughly comparable, but the benefits have decreased dramatically. OMB accomplished this drastic reduction on the benefit side by eliminating the $80 billion per year of benefits produced by the sulfur dioxide limits of the acid rain rules. OMB's explanation for dropping these benefits is that the rule dates to 1992 and so now falls outside the 10 year period that OMB has chosen to include in its report.

Of course, the rule did not abruptly stop producing benefits on September 30, 1993. This highlights one of the analytical problems with this process. Costs are often incurred in a relatively short period of time and are comparatively measurable. Benefits, on the other hand, can be experienced over a considerable period of time. Thus, presenting cost/benefit information in 10 year intervals can weight costs more heavily and cause benefits to disappear. What is the point of the 2004 "total" cost/benefit table except to mislead the public about the relative benefits produced by federal regulatory activity?

The malleability of the numbers produced by regulatory accounting is also highlighted by OIRA Administrator Dr. John Graham's about-face regarding the cost estimates produced by Mark Crain and Thomas Hopkins[7], which are cited in Finding 5 of H.R. 2432 and used in the 2004 Draft Report to justify OMB's invitation to create a new "hit list" of regulations affecting the manufacturing sector that should be delayed, weakened or killed.

When he appeared before the Committee in July, 2003, Dr. Graham left no doubt about his opinion of the usefulness of the Crain and Hopkins study. To support his argument, with which we agree, that it is not workable to require an estimate of the costs and benefits of all existing rules and paperwork requirements, Dr. Graham criticized the study in these terms:

> The fact that attempts to estimate the aggregate costs of regulations have been made in the past, such as the Crain and Hopkins estimate of $843 billion mentioned in Finding 5, is not an indication that such estimates are appropriate or accurate enough for regulatory accounting. Although the Crain and Hopkins estimate is the best available for its purpose, it is a rough indicator of regulatory activity, best viewed as an overall measure of the magnitude of the overall impact of regulatory activity on the macro economy. The estimate, which was produced in 2001 under contract for the Office of Advocacy of the Small Business Administration, is based on a previous estimate by Hopkins done in 1995, which itself was based on summary estimates done in 1991 and earlier, as far back as the 1970s. The

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Budget, Office of Information and Regulatory Affairs, p. 7.

[7] W. Mark Crain and Thomas D. Hopkins, "The Impact of Regulatory Costs on Small Firms", Report for The Office of Advocacy, U.S. Small Business Administration," RFP No. SBAHQ-00-R-0027 [Crain and Hopkins Study].

> underlying studies were mainly done by academics using a variety of techniques, some peer reviewed and some not. Most importantly, they were based on data collected ten, twenty, and even thirty years ago. Much has changed in those years and those estimates may no longer be sufficiently accurate or appropriate for an official accounting statement. Moreover, the cost estimates used in these aggregate estimates combine diverse types of regulations, including financial, communications, and environmental, some of which impose real costs and others that cause mainly transfers of income from one group to another. Information by agency and by program is spotty and benefit information is nonexistent. These estimates might not pass OMB's information quality guidelines.[8]

Amazingly, less than seven months later, this same report is described by Dr. Graham in the 2004 Draft Report as a "recently sponsored" study, "[a]mong the more recent and comprehensive sources of estimates of the overall burden of regulation on specific economic sectors."[9] Although Dr. Graham correctly points out that the Crain and Hopkins data do not indicate whether reducing regulatory requirements on small firms would produce net positive benefits, he nonetheless cites the study in support of his solicitation of nominations of regulations affecting the manufacturing sector to be cut back.

As Dr. Graham said last July, the only thing new or recent about the Crain and Hopkins study is that incomplete and inaccurate data from years ago has been updated to account for inflation. But this merely serves to exaggerate the underlying distortions that are embedded in this type of estimate. Moreover, even Dr. Graham's sweeping enumeration of the problems with the Crain and Hopkins study does not reveal all of its shortcomings. For example, the cost estimates on workplace regulations used by Crain and Hopkins come from a 2001 study by Joseph Johnson of the Mercatus Center.[10] In their painstaking and in-depth look behind the research on regulatory costs, Thomas McGarity and Ruth Ruttenberg found major weaknesses in Johnson's data.[11]

It turns out that the Johnson research begins with the original cost estimates provided to OSHA by representatives of affected industries, makes no attempt to evaluate these estimates retrospectively or adjust for possible bias in the source of information, and then subjects the resulting total to a "multiplier" of 5.55, meant to represent the additional cost of non-major regulations and fines imposed by OSHA. This "multiplier" in turn comes from a 1996 report by a postdoctoral fellow at the Center for the Study of American Business (now Weidenbaum Center) who took it from an unpublished and otherwise unavailable and undocumented 1974 estimate provided by the National Association of Manufacturers. Thus, a figure that includes fines paid for violating

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[8] H.R. 2432, Paperwork and Regulatory Improvements Act of 2003, July 22, 2003 Transcript, p. 21.
[9] 2004 Draft Report to Congress, pp. 26 and 52.
[10] Crain and Hopkins Study, p. 12.
[11] Thomas O. McGarity and Ruth Ruttenberg, "Counting the Cost of Health, Safety, and Environmental Regulation," 80 Tex. L. Rev. 1997 (2002), p. 2017.

existing law is now being put forward by the government as evidence of excessive regulatory burden.

B. There is a Growing Body of Evidence Establishing the Defects of Regulatory Analysis as it Is Currently Practiced Under OMB's Direction.

Four recent publications and studies document the inaccurate and ultimately meaningless data regarding regulatory costs, the specious rubric that underlies cost/benefit analysis, and the increasing threat to the integrity of the scientific information used by regulatory agencies.

1. Not Too Costly, After All: An Examination of the Inflated Cost-Estimates of Health, Safety and Environmental Protections.

In prior testimony, I referred to a pre-publication draft of an exhaustive study prepared by Ruth Ruttenberg and Associates, Inc.,[12] examining the reasons that federal agencies regularly and admittedly overestimate regulatory costs, thus weighting the scales of cost-benefit analysis against regulation. The report is now complete and I am pleased to provide the Committee with copies of "Not Too Costly, After All: An Examination of the Inflated Cost-Estimates of Health, Safety and Environmental Protections."[13]

Looking back over a thirty year period, Ms. Ruttenberg examines over 28 regulations and finds that cost exaggerations are the result of three inherent flaws in agency practice. First, cost information is normally provided to agencies by regulated industry, which has financial incentives to skew the cost-benefit analysis against the proposed regulation. Informational surveys on cost are often limited to a small number of companies, meaning that the results may not be representative of industry as a whole. This problem is compounded by the fact that industry data sources are often confidential, making it difficult or impossible to verify their factual validity. Moreover, there are very limited sources, other than regulated industries, from which agencies can obtain cost information and it is costly to acquire.

The second major flaw is the agencies' tendency to base estimates on conservative and/or inappropriate assumptions. Numerous problems present themselves in attempting to determine cost, the resolution of which invariably reflects the decision maker's bias. For example, it may be difficult to distinguish regulatory compliance costs and other capital expenditures by the company, or to avoid double counting regulatory costs when more than one regulation is involved. Problems also arise in measuring incremental cost differences between what would have been spent prior to regulation and

[12] Ruth Ruttenberg, Ph.D., is an economist with 28 years of experience on the economics of regulation. She has been a senior economist at OSHA, a consultant to OSHA, EPA and the Congressional Office of Technology Assessment, and regularly testifies before the U.S. Congress and federal regulatory agencies and advisory bodies.

[13] Ruth Ruttenberg and Associates, Inc., "Not Too Costly, After All: An Examination of the Inflated Cost-Estimates of Health, Safety and Environmental Protections," Public Citizen Foundation, Inc., 2004 ["Not Too Costly"].

what must be spent after regulation.

Finally, agencies apply only static market analysis, failing to consider new and innovative ways that industry can, and regularly does, comply with new regulations. Yet there is substantial evidence that new processes and improved products are the result of new regulation and create subsequent new profits for the company. Also, cost estimates often fail to consider the offsetting economic gains caused, for example, by the license and sale of pollution abatement equipment or the avoidance of problems arising later in the marketplace. Similarly, cost savings resulting from safer substitutes and the elimination of hazards are often omitted from regulatory cost estimates.

All of these omissions and distortions impoverish the usefulness of cost-benefit analysis and result in cost figures that are significantly inflated.

2. Priceless: On Knowing the Price of Everything and the Value of Nothing

A most welcome addition to the literature about regulatory analysis is the newly published book by law professor Lisa Heinzerling and economist Frank Ackerman.[14] For too long, Professor Heinzerling's groundbreaking work has been known only to a limited audience of academics, and others professionally concerned with regulatory affairs. Confident that they can continue to beguile the public with the appearance of technical expertise, proponents of regulatory accounting have continued to press their case despite Professor Heinzerling's revelations.

In this accessible book written with elegance and humor, Professors Heinzerling and Ackerman make it possible for a wider audience to learn about the myths that underlie cost/benefit analysis. Now, when the assertion is made that federal regulations are causing the "statistical murder" of 60,000 Americans every year, more people will be equipped with the knowledge that 79 of the 90 regulatory measures included in the Tengs and Graham study that is the source of that mythical number never actually existed.

The authors explain how OMB forced the Environmental Protection Agency (EPA) to engage in a bizarre attempt to monetize the fish in the sea in order to justify requiring power plants to incur costs to reduce the number of fish killed by their intake cooling systems. In order to present a cost/benefit analysis, EPA had to find a dollar value for the fish. Only a small number of the fish, those that were caught and sold in the marketplace, had a readily ascertainable commercial value. Others, through a tortured process, could be assigned a value to represent their worth to recreational fishers. Just this quantifiable catch figured in EPA's analysis. No value at all was assigned to fish that

[14] Frank Ackerman & Lisa Heinzerling, "Priceless: On Knowing the Price of Everything and the Value of Nothing," [Priceless], The New Press, 2004. Lisa Heinzerling is a professor at Georgetown University Law Center specializing in environmental law. She was a law clerk to Judge Richard Posner and Justice William Brennan and has represented environmental groups and state agencies in numerous legal battles. Frank Ackerman is an economist at the Global Development and Environment Institute at Tufts Unversity, the author of "Why Do We Recycle?" and a contributing author to the 2001 report of the Intergovernmental Panel on Climate Change.

people do not try to catch or even to the commercially desirable fish that escaped capture, whose continuing existence ensures that there will be a catch next year.

A simple example is used to illustrate both the absurdity of treating human lives as if they were financial investments and the arbitrariness of the resulting numbers:

> If cancer were the same as money, one could equally say that one hundred cancer cases expected twenty years from now have a present value of only fifty-five cancers today at a 3 percent discount rate, or only twenty-six cancers today at 7 percent. Don't laugh yet: this is exactly what is done in contemporary cost-benefit analyses.[15]

People do not value human life this way. When the public became aware of the "senior death discount" (known to Dr. Graham as an "age-adjustment factor" used as part of alternative benefit analyses) their outrage was so great that OMB was forced to abandon the practice of assigning a lesser dollar value to older people.[16] It can be anticipated that Americans who read this book will be as offended by economists' dismissive assumptions and infuriated at their government's acceptance of such repugnant methodology.

3. Grading the Government

Building on Professor Heinzerling's pioneering work, law professor Richard W. Parker has taken a microscope to three influential sets of studies that are often cited in support of the argument that federal regulations are excessively costly.[17] Professor Parker uses the term "scorecard" to describe the presentation of regulatory cost and benefit information in summary statistical form, that is often reduced to a single "cost-per-life-saved" figure.

The three scorecards that Professor Parker exhaustively examines are: the 1987 table created by OMB economist John Morrall, suggesting a cost-per-life-saved of $72 billion; two studies by John Graham and Tammy Tengs at the Harvard Center for Risk Analysis, one showing a range of cost-per-life-saved from federal regulations of less than zero to $1 trillion; and the other positing that 60,000 additional lives could be saved each year if money were spent on different interventions; and Robert Hahn's 2000 update of his 1996 study claiming that fewer than half of all federal regulations pass "a neutral economist's benefit-cost test."

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[15] Id., p. 188.

[16] Memorandum to the President's Management Council from John D. Graham, Ph.D., May 30, 2003.

[17] Richard W. Parker, "Grading the Government," 70 U. Chi. L Rev. 1345 (2003). Richard W. Parker is a professor at the University of Connecticut School of Law, where he teaches Environmental Law, International Environmental Law, and the International Law of Trade and Environment. In addition to his career in teaching, Professor Parker has served as Special Counsel to the Deputy Administrator of the U.S. Environmental Protection Agency and Assistant General Counsel in the Office of the United States Trade Representative.

Professor Parker finds all three scorecards to be rife with errors, which he divides into two categories, avoidable errors and ones that are inherent in the process. In the avoidable error category, all three sets of studies are found to contain undisclosed data and non-replicable calculations, guesses presented as facts, and gross under-estimates of the number of lives saved and/or their value. Morrall altered agency estimates by several orders of magnitude in some cases. Hahn also adjusted agency figures, excluded many benefits, used his own discount rates, and set an arbitrary baseline year of 1996.

Professor Parker's requests for access to the Tengs/Graham worksheets were denied, making replication of their work impossible. Their sample was limited to studies for which estimates for full-implementation costs and benefits had been produced, with the result, for example, that only seven of thousands of regulated toxic chemicals were included.

The catalog of errors that "appear to be endemic to the scorecard enterprise," includes exclusion of unquantified costs and benefits (and of many quantified benefits, as well), disregard of distributive and equitable impacts, and failure to reveal the actual level of uncertainty in the analysis.

The annual OMB Reports to Congress present scorecards of this type and suffer from all the defects exposed in the article.

4. Scientific Integrity in Policymaking, An Investigation into the Bush Administration's Misuse of Science

When Dr. Graham appeared before the Committee last July, he disclosed a "strategy of trying to induce more sound science as a check on regulatory power" and said "[w]e have to have more science and peer review check from the outside community on the power at agencies ..."[18]

The Administration's strategy of using science to "check" agency power is the subject of a report released this month by the Union of Concerned Scientists.[19] In chapter after chapter, the report describes a pattern of suppression and distortion of scientific findings, manipulation of the scientific advisory system to silence opinion not in line with Administration policy, and censorship of government employees.

The scientists caution that distorting the scientific underpinnings of the policymaking process "runs the risk that decision makers will not have access to the factual information needed to help them make informed decisions that affect human health, public safety, and the wellbeing of our communities."[20]

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[18] H.R. 2432, Paperwork and Regulatory Improvements Act of 2003, July 22, 2003 Transcript, pp. 17 and 41.

[19] Union of Concerned Scientists, "Scientific Integrity in Policymaking, An Investigation into the Bush Administration's Misuse of Science," (2004), http://www.ucsusa.org/global_environment/rsi/report.html.

[20] Id., p. 4.

In furtherance of his stated goal of using peer review to "check" agency power, Dr. Graham issued a proposed Peer Review Bulletin in September 2003.[21] Peer review is a process commonly used to confirm that new research conforms to accepted scientific method. It is widely used in various forms by federal agencies that address scientific and technical research in their work.

What Dr. Graham has in mind, however, is a form of peer review unknown to the scientific community. His proposal would impose a new set of requirements on all federal agencies. All scientific and technical information would have to go through peer review before it could be disseminated to the public. The bulletin creates a new category of "especially significant information" that would have to be reviewed by external peer review panels, put together under selection criteria that are patently skewed in favor of industry-funded scientists and against publicly-funded scientists.

This is an unprecedented interference in the regulatory system that, if implemented, will effectively stymie all attempts to address both known and newly identified threats to societal wellbeing. Tellingly, Dr. Graham provides no assessment of the costs or purported benefits of his proposal and does not identify a single example of an agency action that would have been improved by the process he advocates.

In Ackerman and Heinzerling's words in the conclusion of Priceless:

> Cost-benefit analysis of health and environmental policies trivializes the very values that gave rise to those policies in the first place. Moreover, through opaque and intimidating concepts like willingness to pay, quality-adjusted life-years, and discounting, economic analysts have managed to hide the moral and political questions lying just under the surface of their precise and scientific-looking numbers. It is time to blow their cover.[22]

II. OMB's 2004 Draft OMB Report to Congress Ignores the Costs to the Public of Weakened and Blocked Regulations

Further undermining the usefulness of the cost/benefit Report as a picture of federal regulatory activity is its failure to account for the following:

- The use of regulatory analysis to delay and distort new safety protections, such as the tire pressure monitoring and hours of service rules discussed below (paralysis by analysis).
- OMB's use of its reviews of draft regulations to decrease public health and safety protections that were or might have been proposed by regulatory agencies.

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[21] Proposed Bulletin on Peer review and Information Quality, 68 Fed. Reg. 54023 (2003), http://www.ucsusa.org/global_environment/rsi/report.html

[22] Priceless, p. 234.

- The increasing harm to the public that is being caused by the systematic delay and weakening of scores of health, safety and environmental protections.

A. Regulatory Analysis is Being Used to Undermine Congressionally Mandated Public Safety Measures, but OMB Repeatedly Fails to Disclose the Mounting Costs to the Public.

1. The Tire Pressure Monitoring Systems Rule

Two years ago, I attached to my testimony before the Committee a copy of Public Citizen's letter to Dr. Graham objecting to his decision to "return" the draft final rule on tire pressure monitoring systems [TPMS] required by the TREAD Act. At that time, I informed Dr. Graham that his attempt to force NHTSA to adopt a proposed rule based on his manipulated analysis amounted to obstructing the intent of Congress. In August 2003, in a ruling in a case brought by Public Citizen and others, the Second Circuit Court of Appeals agreed.[23] Dr. Graham has not accounted for the costs of his interference in either the September 2003 Report to Congress or the draft 2004 Report. He does not mention the litigation in either report and leaves out of his accounting the injuries and loss of life that would have been prevented if he had not delayed the rule, as well as the squandering of agency and judicial resources occasioned by his meddling on behalf of the auto industry.

Congress enacted the TREAD Act in November 2000, following the recall of over 14 million Bridgestone/Firestone tires due to tread separation. The Act directed NHTSA to complete a rule *within one year* to require a warning system in new vehicles that would indicate when a tire is significantly underinflated. NHTSA issued a proposed rule for public comment in July, 2001 and submitted a draft final rule to OMB in December, 2001. The final rule would have allowed either direct or indirect systems for an interim period, but required that direct tire pressure monitoring systems be installed on all new vehicles after November 1, 2006. Direct systems can detect underinflation in any of four tires all of the time Indirect systems are capable of detecting underinflated tires only 50 percent as frequently as direct systems.

On February 12, 2002, Dr. Graham sent the final rule back to NHTSA. Performing the type of analytical leap that characterizes regulatory accounting, Dr. Graham told the agency "[W]e believe that an incentive to install anti-lock brakes should be considered as part of the regulatory solution" and noted that "[a]llowing indirect systems as well as direct systems effectively reduces the cost of installing anti-lock brakes by 22 percent." [24]

When NHTSA reissued its final rule in June 2002, it did not explicitly adopt Dr. Graham's suggested rationale for maintaining the considerably less effective indirect system. Rather, NHTSA properly pointed out that the TREAD Act directs the agency to

[23] *Public Citizen v. Mineta*, 340 F.3d 39 (2nd Cir. 2003).
[24] February 12, 2002, "Return Letter," http://www.whitehouse.gov/omb/inforeg/return/dot_revised_tire_rtnltr.pdf.

address tire safety, and noted that there is no reason to believe either that allowing indirect systems would lead to an increase in installation of anti-lock brakes or that anti-lock brakes reduce fatalities. Nevertheless, the agency backed down from its earlier decision to require that the fully effective direct systems be installed in all new cars after November 1, 2006. The post-OIRA version of the rule had no requirements for vehicles manufactured after October 31, 2006. Instead, NHTSA stated that: "[I]t is possible that the agency may obtain or receive new information that is sufficient to justify a continuation of the options established by this first part of this rule ..."[25]

This failure to complete the task assigned to the agency by Congress earned accolades from Dr. Graham, who wrote the agency that "OIRA appreciates the significant improvements NHTSA made in the regulatory analysis" and, ominously, that "OIRA wants to work closely with NHTSA to develop analysis sufficient to inform and support NHTSA's ultimate decision."[26] No mention was made of the egregious delay in implementing this lifesaving mandate from Congress. According to NHTSA's own figures, such delay has contributed to the needless deaths of 79 people, as well as thousands of unnecessary injuries, each year.

The Court that vacated the TPMS rule found that OIRA's interference had caused the agency to violate the intent of Congress by promulgating a rule that permitted either of two systems, despite the fact that one was 50 percent less safe than the other. In its decision, the Court reminded NHTSA that "cheapest is best" is contrary to Supreme Court precedent and that the agency is supposed to "place a thumb on the safety side of the scale."[27]

Though others recognized the ruling as a significant rebuke to Dr. Graham and a repudiation of OMB/OIRA's insistence on analysis of every conceivable alternative, Dr. Graham chose publicly to characterize the decision as an endorsement of cost-effectiveness analysis, telling a reporter "We were encouraged that the court recognized an important role for cost-effectiveness analysis in safety regulation."[28]

2. <u>The Hours of Service Rule</u>

Congress enacted the Motor Carrier Safety Improvement Act in 1999 due to the considerable alarm over mounting truck-crash fatalities, administrative delay in revising rules governing truck drivers' hours of service, and lax enforcement of existing regulations. The Act directs the Federal Motor Carrier Safety Administration [FMSCA] to "consider the assignment and maintenance of safety as the highest priority." [29]

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[25] 67 Fed. Reg. at 38704..

[26] June 28, 2002 letter from John D. Graham, Ph.D., Administrator, OIRA to Hon. Jeffrey W. Runge, M.D., Administrator, NHTSA

[27] *Public Citizen v. Mineta*, 340 F.3d 39, *[get quote cite]*, (2nd Cir. 2003).

[28] Cindy Skrzycki, "NHTSA Tries to Deal with the Pressure - Again," *Washington Post*, September 23, 2003.

[29] 49 U.S.C. §113(b).

Prior rules limited consecutive driving hours to 10 and required 8 off-duty hours, but allowed the off-duty time to be taken in split shifts if the driver rested in the truck's sleeper berth. The rules allowed work/rest cycles as short as 18 hours if drivers maximized driving time. In 2001, 409,000 large trucks were involved in crashes; truck crashes killed 5,082 people and injured 131,000.

Over a period of years, the agency accumulated research documenting the importance of uninterrupted blocks of sleep and the need for rest periods that accommodate the human body's 24-hour circadian rhythms, the widespread practice in the industry of falsifying logbooks, and the relationship between crash risk and hours of service violations. On the basis of this research, when FMCSA issued a notice of proposed rulemaking, it proposed allowing 12 on-duty hours, a minimum of 10 hours off-duty and a weekly recovery period of two nights and the intervening day, abolished split sleep schedules for solo drivers, and a requirement for electronic onboard recorders to verify compliance.

Using the grisly calculus of cost-benefit analysis, FMCSA estimated that its proposed rule would have benefits of "$6.8 billion," that is, 115 fewer fatalities and 2,995 fewer injuries annually. Because of the need for additional drivers, cost estimates were substantial, but the rule was projected to have enormous net benefits of approximately $3.4 billion over a period of ten years.[30]

The final rule that was issued on April 28, 2003 ignored the Congressional mandate and abandoned virtually every precept of the notice of proposed rulemaking. Incredibly, the rule still increased the number of permitted driving hours (from 10 to 11), increased the weekly driving time by 26-28 percent, abandoned the proposed system recognizing the need for a 24 hour circadian schedule, reduced the number of needed long-haul drivers by 58,500, did not require onboard electronic recorders, and fattened the trucking industry's bottom line by $1 billion annually.

Furthermore, although FMCSA is required by statute to ensure that driving "does not have a deleterious effect on the physical condition" of drivers, the final rule does not satisfy, or even acknowledge, this mandate.[31] The key question is: how did FMCSA move from trying to improve public safety to keeping rolling sweatshops on the highways?

The regulatory impact analysis (RIA) was outsourced to an independent contractor who met with industry representatives, but not safety organizations. The RIA excluded from its analysis the safety effects of increased daily and weekly driving hours. In legal briefs, FMCSA attempts to explain this away by claiming that it was reasonable to disregard the effect of time-on-task because there is no reliable data on the effect of driving 11 consecutive hours.

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[30] 65 FR 25567, *et seq.*, May 2, 2000.
[31] 49 U.S.C. §31136(a)(4).

But the reason there is no such data is because the law has prohibited truckers from driving more than 10 hours for decades. While many drivers did exceed the legal limit because of the built-in incentive of the industry's pay per mile-driven model, they certainly did not reflect this in their records or participate in research. Yet increasing the number of driving hours increases the exposure of every driver to additional crashes as research shows. Concern for industry productivity was allowed to trump both driver health and public safety.

FMCSA failed to include the RIA document in the public docket until after the rule was issued, thus denying the public any opportunity to comment on its faulty assumptions and unjustified conclusions. Public Citizen has since sued the agency on the merits of the rule and the case is now pending in federal court.

B. OIRA is Pressuring Agencies to Alter Draft Rules to Decrease Public Health and Safety Protections.

A recent report by the U.S. General Accounting Office [GAO] has documented the effect of OIRA's pre-publication review of new rules over a one year period from July 2001 through Jun 2002.[32] GAO examined 85 health, safety and environmental rules that were changed, returned, or withdrawn at the point of OIRA review and found that OIRA had significantly affected 25 of them. Among the effects of OIRA's intervention were the following:

- EPA delayed the compliance date for states to report on two types of emissions.
- EPA deleted provisions covering marine and highway motorcycle engines from a proposed rule on emissions from nonroad large spark-ignition engines.
- EPA eliminated manganese from the list of hazardous constituents in a hazardous waste rule.
- EPA lowered the performance standards of its proposed rule on pollutant discharge elimination systems at existing power generating facilities.[33]

The full effect of OIRA's intervention cannot be known. GAO found that clear and complete documentation of all the elements required by E.O. 12866 was available for only 45 - 65 percent of the rules examined.

C. Scores of Public Health, Safety and Environmental Protections Have Been Rolled Back, Weakened, or Delayed.

Scores of regulations that were benefiting Americans were rescinded, weakened or delayed over the last three years. Yet, in OMB's reports to Congress there is no accounting for these deregulatory actions that have affected critical safeguards designed to prevent the destruction of the ozone layer, reduce air pollution linked to asthma attacks, bronchitis, heart disease and premature deaths, prevent neurological harm to

[32] U.S. General Accounting Office, "Rulemaking, OMB's Role in Reviews of Agencies Draft Rules and the Transparency of Those Reviews," GAO-03-929 (2003).
[33] Id., pp. 76-77.

children, reduce public exposure to toxins and contaminants, protect the natural landscape, preserve crucial habitat for endangered species, provide clean drinking water, prevent flooding, and protect workers from occupational disease and injury. A partial listing of these deregulatory actions includes:

Public Health Protections

- Weakening New Source Review Rules, allowing coal-fired power plants to increase their emissions.
  - Air pollution from power plants triggers asthma attacks, bronchitis, and heart disease, and contributes to about 30,000 premature deaths a year.
- Failing to set emissions standards for mercury produced by chlorine plants.
  - Mercury is a potent neurotoxin that especially threatens the brains and nervous systems of fetuses and young children. A number of neurological diseases and problems are linked to mercury exposure, including learning and attention disabilities, and mental retardation.
- Lifting the ban on the sale of land contaminated with polychlorinated biphenyls (PCBs).
  - PCBs are recognized by the government as probable carcinogens, and studies have found them to damage the liver, kidney, stomach and thyroid gland.[34]
  - It will be more difficult to track the sale of contaminated sites and to ensure that buyers don't spread contamination by developing property before it is cleaned up.
- Seeking exemptions from the Montreal Protocol on Substances that Deplete the Ozone Layer for Methyl Bromide.
  - The treaty aims at phasing out substances destroying the ozone layer, which protects the earth from ultraviolet radiation which can lead to health problems such as skin cancer, cataracts, and suppression of the immune system.
- Creating only a weak proposal to limit diesel emissions from ships and tankers.
  - These vessels are a growing source of air pollution around coastal cities, producing about 273,000 tons of nitrogen oxide per year. Nitrogen oxides can harm the environment by contributing to acid rain formation, which harms buildings, lakes, streams and plant communities.
- Blocking protection of soil and drinking water from manganese.
  - Manganese is an industrial by-product linked to numerous health problems, including respiratory problems, nervous system issues, mental and emotional disturbances, as well as manganism, a disease with symptoms similar to Parkinson's.
- Relaxing Standards for Nursing Home Care.
  - The rule allows workers with only one day of training to assist residents in eating and drinking.

Food Safety Protections

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[34] OMB Watch, *EPA Allows Sales of PCB-Contaminated Sites* (September 8, 2003), *available at*: http://www.ombwatch.org/article/articleview/1781/1/4/; Agency for Toxic Substances and Disease Registry, *Public Health Statement for Polychlorinated Biphenyls (PCBs)* (November, 2000), *available at*: http://atsdr1.atsdr.cdc.gov/ToxProfiles/phs8821.html.

- Making it easier for food companies to claim that that their products help prevent, treat or cure disease.
- Lifting requirements that foods with olestra state that the substance can cause stomach problems.
  - The FDA has logged more complaints—close to 20,000—about olestra than it has about all other food additives in history combined.
  - The cases submitted to the FDA include "[R]eports of diarrhea, fecal incontinence, cramping, bleeding ... Several of the victims required hospitalization, surgery, or other invasive or expensive procedures like colonoscopies."[35]
- Delaying and then refusing to issue an effective standard to control listeria.
  - Listeria is a dangerous food borne bacterium often found in ready-to-eat foods that can lead to death, meningitis, miscarriages and premature births.

Clean Water Protections

- Weakening environmental protections for hard rock mining.
  - According to EPA, the hard-rock mining industry was the largest toxic polluter in 2000, producing 3.4 billion pounds of toxic pollutants that year.[36] The industry has polluted 40 percent of Western watersheds.
- Changing the definition of "fill material" under the Clean Water Act to allow coal mining companies to dump dirt and rock waste into rivers and streams.
  - The valley-fills created by mountaintop removal bury streams and aquatic habitat under piles of rubble hundreds of feet high, destroying the entire surrounding ecosystem and often creating floods that destroy neighboring communities.
- Not limiting construction runoff.
  - Construction runoff accounts for 55 percent of the pollution in coastal waters and 46 percent in estuaries. It is the leading cause of beach closures and advisories. EPA estimates that construction sites annually discharge 80 million tons of solids into US waterways.
- Issuing only very weak rules addressing pollution from factory farms.
  - Factory farms produce around 2.7 trillion pounds of waste per year. Often this waste leaks into rivers and streams, contaminating drinking water and spreading disease. Hog, chicken and cattle waste has polluted 35,000 miles of rivers in 22 states and contaminated groundwater in 17 states.[37]
- Relaxing nationwide permit requirements, making it easier to claim that developing on wetlands will have no adverse effects on the environment.
  - The new rules promote the destruction of wetlands, which filter pollutants from water, mitigate flood damage, and provide critical habitat for thousands of species—many of which are threatened or endangered.

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[35] Center for Science in the Public Interest, *New Olestra Complaints Bring Total Close To 20,000—More Than All Other Food Additive Complaints In History Combined* (April 16, 2002), *available at: http://www.cspinet.org/new/olestrapr_041602.html*.

[36] EPA Toxic Release Inventory.

[37] Sierra Club, *Clean Water and Factory Farms*, *available at:* http://www.sierraclub.org/factoryfarms/ (last visited February 20, 2004).

Public Lands Protections

- Exempting the Tongass National Forest from the Roadless Rule.
  - Roadless areas are havens for fish and wildlife, whose habitat in many other forest areas has been fragmented or entirely destroyed. They provide habitat for threatened, endangered or sensitive plant and animal species, and include watersheds that supply clean drinking water, unpolluted by development.
- Further opening public land for the dumping of mining waste by concluding that there is no limit to the number of five-acre mill sites that each 20-acre mining claims can use.
- Allowing the continued use of snowmobiles in Yellowstone and Grand Teton National Parks.
  - Impacts include haze at Old Faithful, more engine noise, health problems for employees and visitors with sensitive respiratory systems, and chronic disruption of wildlife.

Worker Safety Protections

- Weakening protections for miners exposed to diesel particulate matter.
  - Miners' high exposure puts them at excess risk of a variety of adverse health effects, including lung cancer.
- Weakening the requirements for recording hearing loss.
  - OSHA estimates that 135,000 fewer cases will be recorded each year, denying workers and employers an important tool for identifying and preventing work-related hearing loss.
- Abandoning a rulemaking that would have required employers to protect workers from tuberculosis.

III. Instead of Inviting Nominations for a New Regulatory "Hit List," OIRA Should Make it Easier for Agencies to Issue the Many Health and Safety Protections Whose Need Has Already Been Identified.

In 2001, when OIRA invited the public to nominate regulations for rescission or change, its motivation was totally political. Of the 23 "nominations" that OMB labeled "high priority," 14 came from the corporate-funded Mercatus Center alone. Now, at a time when the disappearance of manufacturing jobs has become a heated political issue, OIRA is soliciting nominations for a new "hit list" of regulations that affect manufacturing. Stripping American workers and the American public of hard-won health, safety and environmental protections is not sound manufacturing policy.

Instead of cynically using the very real issue of job loss as an occasion to further its anti-regulatory agenda, OIRA should be pushing for enhanced health and safety protections and making a priority of regulatory actions that save lives.

For example, although motor vehicle crashes are the leading cause of death for Americans aged 4 to 34, OMB has remained largely silent on this key priority, and has even undermined pending rules, as discussed above. Yet automobile crashes cost 260

billion dollars a year in lost productivity and other direct costs in year 2000 dollars, or $802 for every man, woman and child in America. And these numbers omit the incalculable suffering of family and friends. NHTSA does not, as a practice, place a dollar value on human life.

There are key safety standards which could reduce these astounding costs and unneeded suffering. Below is a list of some of the long-standing needs which should be addressed by new safeguards, particularly given the burgeoning population of sports utility vehicles and pick-up trucks as vehicles for family transportation:

- An occupant ejection safety standard that takes into account advanced window glazing, side curtain and side impact airbags and increases the strength of door locks and latches.
- A vehicle compatibility safety standard, including a standard rating metric to evaluate vehicle mismatch and to increase the compatibility of all passenger vehicles by establishing compatible bumper heights and mitigating harm done by "aggressive" design.
- A rollover crashworthiness safety standard, including a dynamic roof strength standard that requires improved seat structure and safety belt design (including belt rollover pretensioners), side impact head protection airbags and roof injury prevention padding.
- A rollover prevention safety standard to increase vehicle resistance to rollover.
- The coverage of 15-passenger vans by all NHTSA safety standards applicable to light trucks and SUVs and inclusion in the New Car Assessment Consumer Information Program.

Instead of helping to ensure that these protections are enacted, the Statement of Administration Policy on the pending transportation bill signed by Secretary Mineta is on record as opposing all of them on cost-benefit grounds. The Administration's anti-regulatory bias, and hypocrisy when it comes to lifesaving rules, could not be more clear. Yet these proposals address a major problem: 10,600 lost lives a year, or 25 percent of all highway deaths, result from rollover crashes.

It is particularly ironic that crash-mitigation and prevention rules would meet with such opposition, when comparative studies by Dr. Graham and others repeatedly highlight injury prevention measures as the most cost-effective type of rules. Where industrial interests may be disserved by these conclusions, however, it appears that they are quickly and conveniently shunted aside.

IV. Conclusion

If OIRA does proceed with its compilation of a new regulatory hit list, it should, at a minimum, require that any nomination of a rule for modification or rescission must be accompanied by an analysis of the effect of the proposed rule change on public health, safety and the environment.

Most importantly, however, we hope that the dubious practice of regulatory accounting is soon resigned to the dustbin of history, where it belongs. Its intellectual pretense at objectivity is little more than pretense. It does not bear up under scrutiny of any rigor, and has only been perpetuated by academic fraud on the part of self-interested corporate front groups and mouthpieces. The bare language of economics turns out to be a very impoverished substitute for the morally rich and democratic discourse and consensus which gives rise to health, safety and environmental protections.

We must never forget that cost-benefit analysis, where applied, comes very late in the process. Enormous and substantial proof of ongoing harm and risk to life and health has propelled action by Congress or the regulatory agencies. Factual testimony and hearings, agency dockets and public discussion, media investigations, and the experience of thousands or even millions of Americans has been the driving force for development of a remedy. In the face of such evidence, the cost-benefit sophists still maneuver to defeat or delay the public good. Neither Congress nor the American people should be fooled.

Mr. OSE. We thank you for your participation today.

Our final witness in the second panel joins us from the University of Missouri Kansas City School of Law, and that would be Robert Verchick. He is the Ruby Hulen professor of law and comes to us from the Center for Progressive Regulation.

Welcome, sir. Nice to see you. You are recognized for 5 minutes.

Mr. VERCHICK. Good morning. Mr. Chairman, members of the subcommittee, my name is Rob Verchick. I am the Ruby Hulen professor of law at the University of Missouri Kansas City. I have also been a visiting professor of law at Aarhus University in Denmark and a guest professor at Beijing University in China.

I would like to offer my written comments for the record, but today I am a scholar at the Center of Progressive Regulation, and I have only three points I want to make that are fairly important.

The first, and I am going to collapse a lot of this but I would be happy to answer questions on it later, is that OMB's estimates of costs and benefits of Federal regulation are often arbitrary in this report and its previous ones, and are skewed against regulations to protect health, safety, and the environment. A few examples: OMB's tables, for instances, suggest comparisons among agencies where the figures don't support such comparisons because of inconsistent methodologies it admits to; OMB minimizes regulatory benefits by leaving some benefits, even monetizable benefits, out of its calculations. This is a point that Representative Tierney made about the factory farms that is very well taken. OMB also excludes deregulatory actions from cost-benefit analysis. It has done that in the past. Again, this study, to cite one example, excludes the final rules from the so-called "Healthy Forest Initiative" from any cost-benefit analysis; and, also OMB excludes transfer rules from cost-benefit analysis, such as billions of dollars in farm subsidies, which have the practical effect of regulation.

My second point that I want to spend a little more time on has to do with all these international studies, because this is something that has been discussed a bit today and is new for OMB. OMB attempts to make an international case for deregulation; it asserts that, globally speaking, economic growth is associated with less regulation. But, its use of these studies, I am sorry to say, after looking very carefully at them, is, at best, very careless. I am going to focus on the World Bank study, because that is the study that OMB focuses mostly on. But, let us just take a few things just to see some problems here with the study.

First, the World Bank study ignores other means of market intervention which wealthy countries use in place of direct regulation. Denmark, a country praised in OMB's report, and a country that I have lived in, imposes heavy taxes on industrial practices that pollute and waste energy as a replacement for direct regulation. I don't read the OMB report to be advocating that sort of a replacement. Norway and Sweden, incidentally, do the same thing.

Also, if you take a look, the World Bank study, if you look at the methodology, does not even concern itself with many of the regulations that the OMB is studying in this report. For instance, in comparing regulations affecting market entry, the World Bank assumes that a business is, among other things, not using heavily polluting production processes, is not subject to industry-specific

regulations, such as environmental regulations, and that the business is operating in the country's most populous city, like Tokyo or New York, where service sectors often dominate. The bottom line is you can tell very little about what countries like Denmark, Sweden, Singapore do environmentally, or for public health, by looking at a study like this.

The other thing, and OMB has done this before, and I have written about this, as Lisa Heinzerling has also written about this, is that OMB also makes the mistake of understanding wealth to be well-being, when in fact those things are very different. For instance, the OMB report chides the five OECD countries that it claims have the most regulation: Greece, Italy, Portugal, Ireland, and France. All of those countries have lower infant mortality rates than the United States does. All of those countries but Portugal have higher left expectancies at birth than the United States does. If you want to look at countries with similar infant mortality rate or life expectancy to the United States, one of the closest examples you will find is Cuba, one of the most repressed and regulated nations on Earth.

My point is not to suggest that Sweden and Singapore or the United States is Cuba, but my point here is that, if you focus on any single characteristic about a country and then cross over 130 countries, you can prove virtually anything that you want to prove. These studies, for the use that OMB is using them, are flawed because they suggest that regulation has something to do with all of these things as a primary factor, when in fact they don't.

I am running out of time, but I do want to say that I think that there is very little evidence to suggest that we need to look at manufacturing regulatory reform. There are other things, like greenhouse gases and asthma and pollution and sewage problems, which cost billions of dollars a year. We know we already have these problems. These are the problems that need some regulatory reform.

Thank you very much, and I am willing to answer questions.

[The prepared statement of Mr. Verchick follows:]

Testimony of

Robert R.M. Verchick

Ruby M. Hulen Professor of Law
University of Missouri at Kansas City

Scholar,
Center for Progressive Regulation

Before the
SUBCOMITTEE ON ENERGY POLICY,
NATURAL RESOURCES
AND REGULATORY AFFAIRS
Committee on Government Reform
U.S. House of Representatives

Hearing on

Regulatory Accounting

February 25, 2004

TESTIMONY OF

ROBERT R.M. VERCHICK

RUBY M. HULEN PROFESSOR OF LAW
UNIVERSITY OF MISSOURI AT KANSAS CITY

SCHOLAR,
CENTER FOR PROGRESSIVE REGULATION

BEFORE THE
SUBCOMITTEE ON ENERGY POLICY,
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AND REGULATORY AFFAIRS
COMMITTEE ON GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

FEBRUARY 25, 2004

Thank you for the opportunity to testify before you today. My name is Robert R.M. Verchick. I am the Ruby M. Hulen Professor of Law at the University of Missouri at Kansas City. I have also been a visiting professor of law at Aarhus University in Denmark and a guest professor at Beijing University in China. I hold an A.B. degree from Stanford University and a J.D. degree from the Harvard Law School. My expertise is in environmental law and property law. I am the Chair-Elect of the Environmental Law Section of the Association of American Law Schools and a Fellow at the Schloss Leopoldskron Center in Salzburg, Austria. Also, I am a Scholar at the Center for Progressive Regulation ("CPR").

CPR is a nonprofit research and educational organization of university-affiliated academics with expertise in the legal, economic, and scientific issues related to regulation of health, safety, and the environment, and rejects the conservative view that government's only function is to increase the economic efficiency of private markets.

Through research and commentary, CPR seeks to inform policy debates, critique anti-regulatory research, enhance public understanding of the issues, and open the regulatory process to public scrutiny.

My testimony today concerns the Office of Management and Budget's Draft 2004 Report to Congress on the Costs and Benefits of Federal Regulations ("Draft Report")[1] The Draft Report raises issues in four broad areas. Briefly, the report:

1) estimates the total costs and benefits of federal regulation for the period 1993-2003;

2) discusses some of the international literature on the effects of regulation on national economic growth and suggests that as a general rule regulation hinders economic growth;

3) discusses the impact of federal regulation on manufacturers and on the economy; and

4) invites commentators to identify potential regulatory reforms concerning the manufacturing industry.

My specific conclusions about the Draft Report can be summarized as follows:

1) OMB's estimates of the costs and benefits of federal regulation are confusing, sometimes arbitrary, and often skewed against regulations designed to protect health, safety, and the environment.

2) OMB's review of the international literature on the effects of regulation on national economic growth is oversimplified and does not support the conclusions it draws.

3) OMB's public invitation to identify potential regulatory reforms concerning the manufacturing industry is not based on any evidence suggesting a need and suggests a bias against regulations designed to protect health, safety, and the environment.

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[1] The 2004 Draft Report is available at <http://www.whitehouse.gov/omb/inforeg/regpol-reports_congress.html>.

Far from using cost-benefit analysis as a neutral tool to evaluate public policy (a task which I believe is probably futile), OMB instead uses cost-benefit analysis to attack regulations the administration does not like. Yet OMB has declined to employ cost-benefit analysis to evaluate policies (such as reforms of the "New Source Review" program) that the administration favors for other reasons. The point is not that cost-benefit analysis should be used more extensively—it should not be. But the administration's double standard concerning cost-benefit analysis belies the objective purposes OMB has asserted in defending this type of analysis. Given the biases in the Draft Report, OMB's incantations of "sound science" must be met with skepticism.

I. OMB's Estimates of the Costs and Benefits of Federal Regulation

OMB's estimates of the costs and benefits of federal regulation are confusing, sometimes arbitrary, and often skewed against regulations designed to protect health, safety, and the environment. Specifically, (1) OMB's tables suggest comparisons among agencies and rules which the facts do not substantiate; (2) OMB arbitrarily minimizes regulatory benefits; (3) OMB arbitrarily excludes deregulatory actions from cost-benefit review; and (4) OMB arbitrarily excludes agency "transfer rules" from cost-benefit review.

A. OMB's Tables Suggest Comparisons among Agencies and Rules Which the Facts Do Not Substantiate.

The Draft Report's cost-benefit tables invite readers to compare efficiencies among regulatory agencies and among individual rules. Estimates for the Department of Health & Human Services, listed on Table 3, for instance, are meant to be compared with

those of the Departments of Labor or Transportation, which appear immediately below. Unfortunately, as OMB later admits, such comparisons are illusory.

In reality, the wide variations among agencies in their methodology, render comparisons across agencies virtually meaningless. OMB concedes that its data reflects troublesome variations, including, "different monetized values for effects, different baselines in terms of the regulations and controls already in place, [and] different treatments of uncertainty." To choose just one example, OMB notes in Appendix A that some amortizations of aggregate benefits may reflect OMB's preferred 7% discount rate, while others (when performed by the agency itself) may reflect a presumably lower rate. The difference is hardly trivial: the ratio between future benefits thirty years out, calculated using a 3% discount rate and a 7% discount rate is more than 3 to 1.[2]

It is true that OMB does not completely dismiss this point. Citing the many methodological variations, OMB warns that aggregate costs and benefits are "not strictly comparable." But that, to put it mildly, is an understatement. Without any information about assigned monetary values and discount rates used for each rule, the figures are not comparable at all. Nor can OMB save face by suggesting that its tables are intended for "purposes of illustration" only. What valid relationship could these tables possibly illustrate? The comparisons cannot even show which rules save or cost more money than other rules, let alone by how much. They establish no relationship whatsoever between one agency or rule and another.

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[2] For easy calculations involving discount rates, see Center for Progressive Regulation, "Honey, I Shrunk the Future," Pricing the Priceless: Cost-Benefit Analysis of Health, Safety, and Environmental Protection, *available at* <http://www.progressiveregulation.org/perspectives/costbenefit.cfm> .

B. OMB Arbitrarily Minimizes Regulatory Benefits.

At times, OMB appears to present and shape its data in ways that arbitrarily downplay the benefits of regulations designed to protect health, safety, and the environment. Two examples make the point. First, in presenting estimates for "Light Truck CAFÉ for Model Years 2005-2007" (Table 4), OMB accepts cost and benefit estimates drawn from "a baseline of each manufacture's production plans for a single model year." Yet as it admits, this decision underestimates costs and benefits because manufacturers will almost certainly incorporate greater fuel economy standards early, in anticipation of increasing standards in the future. What OMB does not admit is that this behavior could, if its listed figures imply a trend, result in a greater ratio of benefits compared to costs. Thus, a decision to ignore the early compliance could result in a net omission of regulatory benefits.

OMB's analysis of the "National Pollutant Discharge Permits and Standards for Concentrated Animal Feeding Lots" (Table 4) raises a similar point. The estimates of monetized costs and benefits appear roughly even, though the OMB notes that the monetized benefits do not include *all* of the predicted benefits which could have been monetized, such as "eutrophication and pathogen contamination of coastal and estuarine waters, reduced pathogen contamination of groundwater, reduced human and ecological risks from antibiotics, hormones, metals and salts, improved soil properties, and reduced costs of commercial fertilizers for non-CAFO operations."

Yet OMB dismisses these omissions with a single sentence: "Only the first of these [eutrophication and pathogen contamination of coastal and estuarine waters] would likely significantly affect the benefits estimates if monetized." This frail statement just

begs more questions. If the benefits of less eutrophication and water contamination are significant and can be monetized, why weren't they? How would the addition of this significant benefit affect the cost-benefit ratio? What does it mean to say that another unmonetized benefit would not "likely significantly affect" the benefits tally? Is it possible that the rest of the unmonetized benefits could, if monetized, "likely significantly affect" the benefits tally if *added together*? Such dismissals of regulatory benefits appear at best cavalier and, at worst, biased against public protection.

C. OMB Arbitrarily Excludes Deregulatory Actions from Cost-Benefit Review

This year, readers again look in vain for the many regulatory rollbacks that have so dominated the news in that last few years. By subjecting regulatory actions to cost-benefit review while allowing deregulatory actions a free pass, OMB shows a clear bias toward administrative rollbacks and against government intervention.

Surely the final rule on expedited appeals packaged within the so-called "Healthy Forest Initiative," and the Department of Interior's hardrock mining rules deserve the kind of regulatory scrutiny OMB gives to other regulatory initiatives. To its credit, OMB does mention in a footnote at least one deregulatory initiative, the EPA's Prevention of Significant Deterioration and Nonattainment New Source Review: Routine Maintenance and Repair Final Rule, an initiative it apparently has already reviewed. But it withholds its estimates on the grounds that the Court of Appeals for the District of Columbia has stayed its effective date. This excuse is unconvincing. OMB has in the past included

rules subject to legal challenge in its analysis.[3] One would think OMB would have every interest in presenting its data on a high-profile initiative now under court review. Such withholding of data simply raises more questions about OMB's neutrality with regard to regulatory review.

D. OMB Arbitrarily Excludes Agency "Transfer Rules" from Cost-Benefit Review

The Draft Report does not report the costs and benefits of what it calls agency "transfer rules," or rules that transfer money from the federal government to private parties. Indeed the Draft Report does not even list such rules if they were issued before October 1, 2002; it lists only such rules issued after that date. (Draft Report, Table 5). For transfer rules issued between October 1, 2002, and September 30, 2002, OMB provides only a brief description of the rules without any estimate of their economic costs or benefits. In its 2002 report to Congress, OMB explained why it had not analyzed the costs and benefits of transfer rules: "Rules that transfer Federal dollars among parties are not included because transfers are not social costs or benefits. If included, the would add equal amounts to benefits and costs."[4]

The transfer rules listed in the 2004 Draft Report include many very expensive government programs. The money spent on these programs is, by definition, unavailable for other purposes. Such expenditures are opportunity costs in the classic sense. If, for

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[3] OFFICE OF MANAGEMENT AND BUDGET, STIMULATING SMARTER REGULATION: 2002 REPORT TO CONGRESS ON THE COSTS AND BENEFITS OF REGULATIONS AND UNFUNDED MANDATES ON STATE, LOCAL, AND TRIBAL ENTITIES, at Table 9 (hereinafter "2002 FINAL REPORT") (listing costs and benefits of roadless area conservation area); *id.* at 104 (noting that the implementation of this rule had been enjoined by federal district court).
[4] *Id.* at 36 n.30.

instance, the federal government chose not to spend an estimated $1.2 billion[5] to buy out peanut farmers' government quotas, that money could, presumably be used for something else. In OMB's 2003 final report, OMB states that one of its purposes in conducting cost-benefit analysis is to assess the opportunity costs of federal government programs.[6] In addition, OMB's guidelines for cost-benefit analysis, issued last year, explicitly require agencies to assess the distributional effects of transfer payments.[7] OMB's failure to consider the opportunity costs and distributional consequences of the transfer rules in Table 5 flouts OMB's own policy statements.

Further, OMB provides no principled definition of a transfer rule. Technically speaking, the transfer rules that lie outside the scope of conventional cost-benefit analysis are those rules that do not attempt to change, or have the effect of changing, the nature or level of economic goods or services provided by private economic actors. They simply transfer money from one entity to another after market actors have chosen the nature and level of goods and services to be provided.

The agency rules OMB includes within the category of transfer rules do not all meet this definition. For example, OMB includes as transfer rules agricultural subsidy programs that clearly affect the nature and level of agricultural goods provided in the United States. There can be little doubt, for example, that the agency rules associated with the 2003 farm bill's dairy-support program (Table 5) will influence the production

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[5] Environmental Working Group, Farm Subsidy Data Base, *available at* <http://www.ewg.org/farm/progdetail.php?fips=00000&progcode=peanuts >(using figures for 2002).

[6] OFFICE OF MANAGEMENT AND BUDGET, INFORMING REGULATORY DECISIONS: 2003 REPORT TO CONGRESS ON THE COSTS AND BENEFITS OF FEDERAL REGULATIONS AND UNFUNDED MANDATES ON STATE, LOCAL, AND TRIBAL ENTITIES.

[7] *Id.*

of milk and thus affect the primary behavior of market actors. Yet OMB does not explain why these rules are "transfer rules" rather than rules that are properly subject to economic analysis. If the federal government chose to influence milk production through more conventional regulation – say, by tightening environmental standards for dairy farms – the costs associated with such regulation would appear in OMB's cost-benefit tables. To characterize dairy-farm price supports as "transfer rules" simply because they influence market behavior by other means can only be described as arbitrary.

At the very least, OMB should: (1) provide a clear definition of the term "transfer rule"; (2) explain why the rules on Table 5 meet this definition; and (3) list the economic costs of the transfer rules it deems not subject to cost-benefit analysis, so readers can at least judge the relative expenses associated with the unevaluated transfer rules.

II. OMB'S USE OF INTERNATIONAL STUDIES TO QUESTION REGULATIONS DESIGNED TO PROTECT HEALTH, SAFETY, AND THE ENVIRONMENT

OMB attempts to make an international case for deregulation. First, it asserts that, globally speaking, economic growth is associated with less regulation. In support, OMB offers a preliminary report from the World Bank, a study from Canada's conservative Fraser Institute, and a study co-authored by the conservative Heritage Foundation and the Wall Street Journal. OMB argues that the correlation between deregulation and economic growth forms, in fact, a causal relationship. Second, OMB suggests that its own regulatory agenda, described in its 2002 Final Report, matches "fairly closely" the pro-growth regulatory reforms praised in the World Bank's preliminary report. Both claims have problems.

A. OMB's Review of the Literature is Oversimplified and Does Not Make the Case for Less Regulation in the United States.

OMB relies mainly on the World Bank report to conclude that national wealth, productivity, and employment rates are all positively correlated with less regulation. (It correctly faults the Fraser and Heritage-WSJ studies for failing to isolate the effects of regulation from other influential factors like trade policies.) The World Bank report examines "five of the fundamental regulatory aspects of a firm's life cycle": starting a business, hiring and firing workers, enforcing contracts, getting credit, and closing a business. Describing the World Bank's findings, OMB states:

> Australia, Canada, Denmark, the Netherlands, New Zealand, Norway, Singapore, Sweden, the United Kingdom, and the United States, among the richest countries in the world, are the least regulated. The study also finds that common law and Nordic countries regulate less than countries whose legal systems are based on French, German, and socialist origins. (Draft Report at 30)

There are many problems with the use to which OMB would put this report. I will concentrate on four. First, these simple conclusions ignore other means of market interventions which some wealthy countries use in place of direct regulation. Denmark, a country praised in OMB's Draft Report and in which I have lived, imposes heavy taxes on industrial practices disfavored by the government, particularly in pursuit of environmental protection. The same is true in Norway and Sweden. Yet in its use of such examples OMB does not appear to be advocating elaborate taxes to achieve the benefits of direct regulation.

Second, OMB appears to assume, without citing any persuasive evidence, that the rewards of "economic freedom" accrue equally at every stage of deregulation. This

defies common sense. No one can dispute that Bolivia, whose inhabitants are buried in a jungle of bureaucracy and red tape, would do well to take a machete to its regulatory programs. (See Draft Report at text accompanying note 13.) Bolivia and similar countries could make vast economic improvements by simplifying business regulations. Of course, as the World Bank suggests, regulations should allow for property rights, contract enforcement, and the like. But what does this say about the United States, a country that has guaranteed such rights since its inception? For wealthy countries already classified as "economically free," the benefits (or costs) of each felled regulation are highly individualized. The World Bank's study can do little to inform regulatory evaluations on the margin.

Third, and related to the point above, the World Bank study does not even concern itself with many of the types of regulations OMB is most concerned about. A careful look at the World Bank study shows that its broad, transnational comparisons rely on some startling assumptions. For instance, in comparing regulations affecting market entry, the World Bank assumes a business that, among other things, (1) "is not using heavily polluting production processes," (2) is not subject to industry-specific regulations (such as many environmental regulations), and that (3) is operating in the country's "most populous city."[8]

Whatever the study says about regulation in general, its comparisons say nothing about heavily polluting industries, those subject to special rules, or those operating outside cities like Tokyo and New York. This point is key because wealthy countries are, perhaps, the most likely to have specialized rules, directed toward specific industries or

[8] The World Bank Group, Doing Business: Methodology—Starting a Business, *available at* <http://rru.worldbank.org:80/DoingBusiness/Methodology/EntryRegulations.aspx>.

specific pollution threats; and their large industries are less likely to reside in their country's most populous city, which is likely to be dominated instead by the service sector.

Finally, OMB, as it so often does, mistakes wealth for well-being. The two should not be equated.[9] Consider two possible measures of well-being, average infant mortality and average life expectancy at birth. While it is true that some "less regulated" nations, such as Sweden and Singapore, rank among the best in international comparisons, other less regulated nations, such as the United States, do not.[10] Indeed the five OECD countries that OMB describes as having the most regulation -- Greece, Italy, Portugal, Ireland, and France -- *all* have lower infant mortality rates than the United States.[11] All of those countries, with the exception of Portugal, have higher average life expectancy figures too.[12] Among all nations, the country whose figures are among the

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[9] For more discussion, see Robert R.M. Verchick, *Feathers or Gold? A Civic Economics for Environmental Law*, 25 HARVARD ENVIRONMENTAL LAW REVIEW 95, 109-15 (2001).
[10] Sweden's infant mortality rate of 3.42 deaths per 1,000 live births is the world's second lowest. U.S. CENTRAL INTELLIGENCE AGENCY, THE WORLD FACT BOOK, "Rank Order: Infant Mortality," (2003), *available at* <http://www.odci.gov/cia/publications/factbook/rankorder/2091rank.html> [hereinafter, "Infant Mortality"]. Sweden's average life expectancy at birth, 79.97, places it ninth in the world. U.S. CENTRAL INTELLIGENCE AGENCY, THE WORLD FACT BOOK, "Rank Order: Life Expectancy at Birth," *available at* <http://www.odci.gov/cia/publications/factbook/rankorder/2102rank.html> [hereinafter, "Life Expectancy"]. Singapore's infant mortality rate of 3.57 deaths per 1,000 live births is the world's fourth lowest. "Infant Mortality," *supra*. Singapore's average life expectancy at birth, 80.42, places it fifth in the world. "Life Expectancy," *supra*. The United States' infant mortality rate of 6.75 deaths per 1,000 live births is the world's forty-second lowest. "Infant Mortality, *supra*. The United States' average life expectancy at birth, 77.14, places it forty-eighth in the world. "Life Expectancy," *supra*.
[11] *See* "Infant Mortality," *supra* note 10.
[12] *See* "Life Expectancy," *supra* note 10.

closest to U.S. figures is Cuba, one of the most repressed and regulated nations on earth.[13]

My point is not that life in Sweden is the same as life in Singapore, or that life in America, for that matter is comparable to life in Cuba. Rather my point is that one cannot generalize among countries on any single axis without arriving at conclusions that often make one laugh. OMB should abandon its quest for a regulatory Theory of Everything, and instead focus on studies appropriately tuned to the effects of regulation in the United States.

B. OMB's Regulatory Agenda Does Not Follow from the World Bank Study

OMB apparently hopes to earn points for its own regulatory agenda by suggesting it matches the World Bank's recommendations "fairly closely." Indeed, it cites its own 2002 Final Report, Chapter 1 as evidence of its compatibility with World Bank analysis. This is, at best, a case of wishful thinking. The World Bank's preliminary conclusions – which are addressed to countries of all levels of wealth and with myriad forms of government – is pretty simple: avoid unnecessary interference with competitive markets, enhance property rights, expand technology, reduce court involvement in business matters, and make reform a continuous process.

Most Americans, including those at OMB, would no doubt agree that centralized management of the economy, especially when its intended

[13] Cuba's infant mortality rate of 7.15 deaths per 1,000 live births is the world's forty-fourth lowest. "Infant Mortality," *supra*. Cuba's average life expectancy at birth, 76.8, places it fifty-first in the world. "Life Expectancy," *supra*. For U.S. figures, see *supra* note 10.

effect is to shield business from competition, is not a good idea. But OMB's regulatory agenda, as expressed in the 2002 Final Report, recommends something very different. OMB's report prominently argues for strongly centralized regulatory oversight, a Baroque system of outside peer review, and an expanded bureaucratic staff.[14] These elements, of course, are not recommended in the World Bank Report. Indeed some of the OMB's agenda appears at odds with the World Bank's general injunction against unnecessary bureaucracy and red-tape, to which the OMB's own system of review contributes.[15]

III. OMB'S PUBLIC INVITATION TO IDENTIFY POTENTIAL REGULATORY REFORMS CONCERNING THE MANUFACTURING INDUSTRY

OMB invites comments on regulatory reforms concerning the manufacturing industry. Specifically, it seeks proposals that might reduce unnecessary costs, increase effectiveness, enhance competitiveness, reduce uncertainty, and increase flexibility. Yet OMB makes no case that current regulations significantly contribute to unnecessary costs, ineffectiveness, losses in productivity, or inflexibility. OMB is pedaling a solution (deregulation) in search of a problem. What accounts for this? According to OMB it is because manufacturing industry is heavily regulated. But many industries are.

OMB would do better to invite comments on regulations that could address problems that we *know* we have. We know that greenhouse gases, unregulated under

[14] 2002 FINAL REPORT, *supra* at note 3, chap. 1.
[15] For more on OMB's increased, centralized power, see *See* FRANK ACKERMAN & LISA HEINZERLING, PRICELESS: ON KNOWING THE PRICE OF EVERYTHING AND THE VALUE OF NOTHING 42, 110-11, 168-69, 195, 207-08 (2003).

federal law, threaten America's future health, productivity, and even national security.[16] We know that asthma, a disease related to urban air pollution, has become the number one childhood illness in the United States.[17] We know that sewage pollution costs Americans billions of dollars annually in medical care, lost productivity, and property damage.[18] Yet on these subjects, OMB remains silent. Regulations protecting health, safety, and the environment are vital to our nation's interests. OMB should not downplay this truth any longer.

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[16] *See* Mark Townsend and Paul Harris, *Now the Pentagon Tells Bush: Climate Change Will Destroy Us*, GUARDIAN (U.K.), Feb. 22, 2004, *available at* <http://www.guardian.co.uk/usa/story/0,12271,1153531,00.html>.
[17] EnviroHealthAction, Children's Environmental Health, *available at* <http://www.envirohealthaction.org/children/asthma/>.
[18] Natural Resources Defense Council, Press Release, Aging U.S. Sewer Systems Threaten Public Health, New Report Finds, *available at* <http://www.nrdc.org/media/pressreleases/040219a.asp>

Mr. OSE. Thank you, Mr. Verchick.

All right, as we did in the previous panel, the manner in which we will proceed is that I will ask questions, then Mr. Tierney will have his round of questions, then Mr. Schrock will have his round, and, if we have multiple questions, we will have multiple rounds.

I have broken my questions out in two ways. I want to focus on the bill itself first.

Mr. Kovacs, you heard the discussion in part, I believe, about including "as part of" the President's budget the regulatory accounting statement and its associated report, as opposed to including that report "with" the President's budget. In other words, is it in the document or is it accompanying the document.

Now, one of the difficulties we had this spring was that the regulatory accounting statement was not with the President's budget; it was 11 days late. And one of the difficulties we have up here is that we are required to provide feedback to other committees about the President's budget on a certain timeline, and, if we don't have the accompanying documents, it is awful hard to provide whatever insights we may have.

My legislation would require that the regulatory accounting statement be integrated into the President's budget documents. Do you support that requirement?

Mr. KOVACS. Let me see if I can give it to you in three parts as simply as I can. One is the Chamber supports regulatory accounting; two, in the perfect world, we would like to see it concurrent with the President's budget; but, three, in the practical world, we are here to get the regulatory accounting and the regulatory cost-benefit analysis straight. We think there are deficiencies in the process now. Until we really sit down and take it seriously, and whatever you get in terms of a regulatory budget is going to end up being a range. It has to be a range because regulatory accounting is a dynamic process, it is not a static process. Also, as part of the process you need to consider the kind of data that is going in. The Data Quality Act is only about a year old, and you need to make sure that the agencies incorporate sound science, that the process is transparent, that it is peer reviewed; and then I think you get to the point where you actually understand what the regulations are going to do and the range of impacts.

So, we think it is a three-step process.

Mr. OSE. OK, using your phrase, "in a perfect world," should the regulatory accounting statement be part of the President's submittal or should it be in an accompanying document?

Mr. KOVACS. We would like to see it as part of a submittal, because what the agencies are going to do as part of their budget is certainly going to have an impact on regulation.

Mr. OSE. All right.

Ms. Dudley, any comments on that?

Ms. DUDLEY. No, I would agree, and I think the analogy to the Government Performance and Results Act is helpful there. We have seen that in recent years, GPRA measures have been part of the budget; not alongside the budget, but part of the budget, and I think it is helping improve accountability and performance.

Mr. OSE. Dr. Belzer, you have been 10 years at OMB in one form or another. What is your feedback on this?

Mr. BELZER. Well, I applaud the idea. I think that is useful to be careful about what we think we want to get out of it. Ideally, what I would like to be able to see, and maybe you would like to see, is within the budget to be able to quickly discern, when you are looking at some obscure regulatory outpost in the Government that issues regulations, what were the costs and benefits of the regulations that it issued; and to be able to have that information handy within the document.

To make that work for you, though, those estimates have to have gone through a pretty careful validation exercise so that they are not simply reported estimates or suggested estimates or draft estimates, or something of that form. And, from my 10 years of experience at OMB, my concern would be that the numbers that right now would go into such a document would not be OMB's numbers, and I think that is part of the reason for some concern about incorporating them.

Mr. OSE. Well, you questioned the validity of some of the numbers on the basis that they hadn't been checked, is the way I interpreted your remarks, and that there existed, probably on the private side, the better part of wisdom in the regulatory analysis industry. Given the difficulties here, you have been on both sides, who will compress this so we have the information in a timely fashion?

Mr. BELZER. Well, I believe that it speaks to the question of the quality of the information that we are dealing with, as well as the reporting timing. If you were to incorporate within the budget document a final accounting statement, I think that is perfectly helpful. A draft accounting statement would be problematic. ,But the underlying problem I have still is that the numbers that OMB is reporting are not OMB's numbers. I do find it a little amusing to find OMB criticized for the numbers when they really don't belong to OMB; they have simply repackaged the agencies' estimates and in some cases made the simple conversions to make them a little bit more comparable. But, the problem is that the agency estimates are coming in to this process without any real thorough review, except by OMB, but without any competitive estimates from other parties, from whichever interest group might want to provide a credible policy-neutral, compliant estimate, compliant with Circular A–4.

Mr. OSE. Mr. Tierney.

Mr. TIERNEY. My initial approach to this whole thing is that the agencies ought to be worried about the cost it takes them to do all of this work and making all these comparisons, when it seems the benefit of their work isn't that obvious to many of us, since it seems so difficult to measure the benefit side of it; and I am not sure there is a value to what they actually end up with in the end.

Mr. Verchick, maybe you can tell us a little bit. How can we ever be comfortable that somebody is giving a fair assessment of the value of a benefit like a health factor or environmental factor or safety factor? How comfortable can we be that any calculation that tries to measure those aspects is in any way accurate and gives us a clear picture of what it is?

Mr. VERCHICK. I think that they can't give you a clear picture if what you want to do is look at losses of money, which can be meas-

ured, and then also try to incorporate losses of life or injury, harm, this sort of thing. Those are value judgments, and those value judgments, in my view, should be made by the people in an open process, rather than economists deciding whether to discount a life by 3 percent or 7 percent into the future. Those are value judgments too, but those are judgments that are made by unelected people applying economic practical to moral ideas that they weren't intended to affect.

Mr. TIERNEY. I guess we are just reiterating a point that I made in my opening remarks. This is a lot of common sense. If you have a dollars matter, we ought not to start putting in relations without any consideration for their costs, but, in the end, there are some things that are just common sense. And, you can't measure the things that you and I were just discussing, but you have to factor them in then make a decision, and that may make it sometimes more difficult to sit in these chairs, but that is what you do on that.

Ms. Claybrook, I was concerned about OIRA's increasing interference in agency rulemaking decisions. I think there is a real trend in that. GAO stated in a report last September that there is a clear indication of OIRA's new gatekeeper role, and that is the office's increased use of return letters. GAO reported that, between 2001 and 2002, 23 letters were returned, far more than the number returned the previous years. Do you share that concern? And, would you talk a little bit about that?

Ms. CLAYBROOK. I do have concern about it. It seems to me that the major role of the Office of Management and Budget in the regulatory sphere is to look at the overall impact, but not to try and get into the nitty-gritty. In the tire rule, the rule that required an indicator on the dashboard about whether your tires were inflated or under-inflated, they got into proposing an alternative method for measuring the system to be used by industry, and the original proposal by the Department of Transportation was that it be a direct measurement of each tire and that it be a dashboard light. What OMB said is, well, there are some vehicles that have these analog brakes, and, when you have analog brakes, you can measure it on the analog brake itself. But, of course, the problem with that was that you only measure one tire. Now, most people want to know about all four tires in their car. You can only measure it when the tire is moving. But, when I am at the gas station at the pump, I want to know, while I am there, whether or not I have an under-inflated tire and which one it is.

So, they proposed an almost ridiculous alternative proposal, and it was a little bit cheaper, but in terms of cost-benefit analysis it really wasn't cheaper, even if you did it that way. And, we sued the Department of Transportation after OMB forced the agency to change the rule, and we won, and I quoted to you from what the court said. So it seems to me that should not be the role of citizen groups, to have to sue OMB when it interferes with a particular rule in that level of detail.

The other issue, of course, is that the way that OMB looks at the overall costs and benefits is really inappropriate because you cannot measure the decisionmaking process of someone who is charged by Federal statute to save lives, reduce injuries, or protect the environment. You cannot look at it in purely monetary terms. And,

I don't think anybody in this panel would want that to happen. You may want to understand it. I was a Federal regulator; I wanted to know the numbers, I wanted to understand it. But that should not be the guideline that determines how you set that rule or what it is. There is no industry in America that I know of that has been put out of business because of some Federal regulation. I don't see that there is a case that has been made for a regulatory accounting or an absolutist cost-benefit analysis because of the harm that has been done to any company.

In addition, there are all sorts of ways of mitigating the cost to industry, which agencies take into account all the time. For example, how long the industry has to implement a rule. If, for example, in the auto safety area, if you issue a regulation and say to the company you have 2 years to do this, it is going to cost the companies a lot more than if you give them 5 or 6 years to implement it. And, agencies give them more time all the time. Companies ask for that, they do that. So, the cost to the company is vastly reduced. But, that doesn't mean that you shouldn't issue the safety standard.

Mr. TIERNEY. Thank you.

Mr. OSE. Mr. Schrock.

Mr. SCHROCK. Thank you, Mr. Chairman.

I was interested, Ms. Claybrook, you said you objected to regulatory accounting, but how do you respond to the 80,000 new regs that Dr. Graham talked about that have never been looked at? Doesn't that deserve some oversight?

Ms. CLAYBROOK. Well, if you are going to go back and look at past rules that have been issued, I think you have to take half the Federal budget to do that.

Mr. SCHROCK. What?

Ms. CLAYBROOK. Take maybe half the Federal budget to do that, because the data that exists is out of date now for the past rules, it is totally out of date. So, you would have to do brand new evaluations. I think that if you look at the report that we submitted for the record today by Ruth Ruttenberg, you will see that, once a rule is actually implemented, the costs are far less than what companies said when the proposal was on the table, before it had been issued. And, so, you would have to go and do an evaluation of that.

The other issue that I think is really important on the cost side is that there is no accounting by a Federal agency. When a company says it is going to cost us $25 million to implement this rule, the agencies don't have the resources to go look at the factories and the cost estimates made by the industry; they just accept the complaints by the companies. And, so, if you are going to really evaluate this, there is a huge, huge amount of work to look at even a few, not even the 80,000. I don't think that it is possible to do that.

Mr. SCHROCK. Did I understand you to say that some of the regulations are really not applicable anymore? But, businesses think they are applicable and they are trying to adhere to what it says. You know, for instance, this telephone is applicable today; 2 months from now it won't be. In 2 months the new one won't be and in 2 months the new, new one won't be. So some of these regulations these poor folks are trying to adhere to have no applicability to anything, as I hear you saying. And, this lady who wrote this

"Not Too Costly After All," I would like to have a copy of that, by the way.

Ms. CLAYBROOK. Yes, of course.

Mr. SCHROCK. I think there are some businesses who would differ with you. In the district I represent in Norfolk and Virginia Beach, VA, I think they would differ with that, because I think some of them have gone out of business because they said it is just not worth it, the regulations are too costly. And, I know some of the regulators in this town have dropped in on certain business people and made their life a living hell for a couple hours, and they say it is just not worth it anymore.

Ms. CLAYBROOK. Well, I didn't say that they weren't applicable anymore, but I am sure there are some that are.

Mr. SCHROCK. Oh, I am sure.

Ms. CLAYBROOK. I am sure that there are. And you have a table here of three organizations, particularly the Chamber of Congress, which is supposed to represent small business, that I am sure is petitioning agencies all the time on behalf of their small business members, and you have a Government agency on small business that just testified that certainly has the capacity to go to Government agencies and say these standards are no longer applicable.

I would point out that most health, safety, environmental regulations are performance regulations. They don't tell them how to design the product, they don't tell them that they have to do it this way or that way; they actually measure the performance of the activity and say you can't die in a frontal crash at 25 miles an hour with an air bag, the air bag has to protect you so you don't die. That is an example. So that means that the regulations are able to go with the new generation of a product, because it is a performance standard.

But, in terms of the impact on small business, I don't want to argue, and I will not argue, that for smaller companies it isn't more complicated to comply with regulations than with larger companies. But let us take lead smelting. I mean, that can really harm people, both in the workplace and in the community. You have issues of environmental justice, for example, which is that a lot of companies are located in low-income areas, and so children in low-income areas are more subject to harmful environmental impacts.

I don't think anyone in this room would want to live in the maquiladora area, which is just south of our border into Mexico, where children are born with all kinds of harm, brain damage and limb damage and other things, because of the environmental impacts that they face. Some of those are small companies down there.

Mr. SCHROCK. And, Ms. Claybrook, I understand that, but the bad actors like that ought to be taken to the woodshed. But, I don't think we make everybody pay because there are a couple of bad actors. But, I know there has to be a balance there somewhere.

Mr. Kovacs, I know you want to comment on that.

Mr. KOVACS. Sure. First of all, the position of the Chamber is, as you said, Congressman, if there is a bad actor, they should just go to jail. I mean, we are not even here talking about that. That is really the first thing.

The second thing is most regulations are not necessarily performance standards, they are mandates and they are controls, and they are the most difficult ones. And we can go down the list, whether it be ergonomics or mercury standards or whatever. We can give you thousands of those. And there are processes, like Section 610 of the Regulatory Flexibility Act, which requires the agencies on a 10-year basis to actually go over and look at the rules to see which ones no longer apply, and there are far more in the breach than in compliance. So there are mechanisms.

But, what we are trying to say, and why we really appreciate so much what this committee is doing, is this is the beginning of let us get a handle on what is there. You have a mechanism in 610. Why aren't the agencies doing this on a 10-year basis? Second, we have a way to check the system. Let us just take the regulations that are out there where we do a cost-benefit analysis, and let us just, after 4 or 5 years, have the agency go back and check to see how closely they came.

You know, we from the industrial sector and the business sector pay for most of these regulations. Frankly, the consumers end up paying, and they sometimes pay not just in cost of product, but in lost jobs which is contrary to what Ms. Claybrook was saying, that there has been no effect on, let us say, the manufacturing industry. My recollection is correct, over the last 30 years, the manufacturing sector of this country has been cut in half in terms of jobs. So, it is real. It is real, and no one is going to disagree that, where you have property rights and certainty of regulation, you have more investment in technology; and in a lot of areas across this country, the technology sector, the biotech sector, the biogenics, all of those, our regulations are forcing companies and the most advanced technologies in the world to go to Korea or Ireland. We are now 13th in the world in Internet. So these are real consequences to regulations. So let us not kid ourselves. And, the opportunity that we lose by not being able to advance our regulation into the modern era is huge.

So, we do have options. We can look at regulations retroactively, using Section 610. We are not saying that every regulation is bad or we should look at it, because there are 4,000 a year, that is impossible. We might look, at 20 or 30 in the course of a year.

And, then, finally, a lot of the regulations are just good business practices and we do need them. So you have to understand what kind of regulations you want. But, if you want to look at regulations that cost a lot of money, just look at the Federal income tax laws. You have a lot of places for change that are very common sense, and that is what we are saying. Let us not sit here as a panel and say regulations are all good or bad; let us get a handle on the process and what it really costs, and get science into the program.

Mr. SCHROCK. I think everybody agrees with that.

I know my time is up, Mr. Chairman. I am sorry. You have been banging for a while.

Mr. OSE. I want to followup on Mr. Kovacs' comment. On page 3 of your testimony you make this exact point, about how do you know which ones to emphasize if you don't know their relative costs and benefits.

Mr. KOVACS. Well, you do. You really do. Because let us just take TMDLs, which is total maximum daily loads, which is a water standard. The agency walks in and says, look, this regulation is going to cost $25 million a year; let us go back to Mr. Tierney, common sense. You are asking the entire country to analyze 40,000 water bodies and to come up with a statement and then come into effect with a plan to treat it. And, so, even if you took it at $1 million a water body for the analysis for treatment and everything else, you are at $40 billion. And, that is what one study had. GAO had it a little over $1 billion annually; the States had it $670 million annually to about $1.2 billion annually; EPA said it is $25 million.

Mr. OSE. I didn't state my question very well. I understand your point about the common sense issue in that respect. What I am more interested in is that Mr. Schrock, Mr. Tierney and I and our colleagues, we only have X amount of resources. I am trying to figure out the way in which we take those resources and we maximize the benefit to the country as a whole, from a cost-benefit perspective. Your testimony here is that, absent some sort of measurement, we are not going to be able to do that.

Mr. KOVACS. That is correct.

Mr. OSE. So, you would support something such as in Section 6 that allows improvements to regulatory accounting, the objective of which is to get us to a point where we can say this impact has a cost-benefit ratio of X; this one has a cost-benefit ratio of Y; this one has a cost-benefit ratio of Z, and allow the policymakers up here to decide which one should have priority? Is that your point?

Mr. KOVACS. No. I think Congress makes the law and it decides whatever the priorities are, but when the agency is implementing the law, they have tools at their disposal. They should always be using the best science. They should always be using the best data. And, from that they are going to begin to understand, and I will make a quick point.

Ten years ago, when Bill Riley was the head of the EPA, he did an internal study, and he asked the scientists and the public what are the most serious risks; the public put Superfund at No. 1. He then asked the scientists what are the most serious risk to public health, and they would select certain aspects of air quality. If you looked at the list, they were almost absolutely the opposite of each other. What the public perceived and the scientists perceived as a serious risk were completely different. What we need to begin doing is realigning that. And, you have the tools.

You have already given the agencies the tools with data quality and data access and sound science. It is now up to them to really begin in a rigorous process, and that is why I suggested a pilot study, because this is a rigorous process, this isn't an easy thing. We have to take these options, look at a dynamic system, look at the true health, honestly evaluate what it is, because at the end of the day, if the agency spends its money on the most serious public health problems, we are all going to be better off. But they have the tools now.

Mr. OSE. Ms. Dudley, do you agree with that?

Ms. DUDLEY. Yes. Let me just add one more thing to the study that he mentioned. I thought the most interesting thing about that

was that our resources were being devoted to the public's ranking of risks, rather than what experts think is the more real ranking of risk. And, that is your point, isn't it, that we aren't sending our resources to the most effectively to activities that will produce the greatest good. I know Alexandra Teitz and I have had a conversation, and she was shocked that I didn't think that cost-benefit analysis was the answer to everything; and I think it is not, but I think it does provide information that allows you to make more informed decisions.

Mr. OSE. Dr. Belzer, do you have any input on this?

Mr. BELZER. Well, I have been practicing benefit-cost analysis for so long, I can't remember when it wasn't the way that I made decisions. I chose whether to have a heart surgery based on cost-benefit analysis.

Mr. OSE. What was the result of your study?

Mr. BELZER. I lived.

Cost-benefit analysis is nothing different than what people do in their daily lives when they make mundane decisions; they do it intuitively. It is exactly what common sense is all about. When you get into complicated issues with valuing very difficult commodities, it can get technical. This is what professionals do, they try to do the technical part and then simplify it for other people.

I should point out the common myth is that costs are easier to estimate than benefits. All things held constant, I really don't think that is true, because costs, properly understood, the costs of a regulation are the benefits that one must forego in order to have the benefits of the regulation. So really you are giving something up, not just dollars, you are giving something up in order to get the benefits of a regulation. What exactly are you giving up? Well, if somebody tells you it costs $1 million or $2 million or $3 million, I don't really care about the dollars, what I care about is what those dollars would have been used for; how would the public have been served by those expenditures. Those are the things that end up being given up. So it is harder, in principle, to estimate costs if you try to do this correctly.

It is a mystery to me why it has become such a controversy, especially since I cut my teeth in cost-benefit analysis 30 years ago with a rather famous book called "Damming the West." It was a book on exposing all of the flaws in cost-benefit analysis performed, as it happens, by the Bureau of Reclamation. They were inflating the benefits and they were low-balling the costs and they were cheating on the different methods; they were double-counting benefits. They were doing everything wrong and it was a terrific book; it caused me to become an economist. Now, I find it ironic that the book was a product of the Ralph Nader study group at the time.

So, to me, the methods are the same now as they were in 1973, and maybe the parties have changed as to who is putting their thumbs on the scale. But the methods are the methods, and they inform people; they help you make decisions, they don't tell you what you have to decide.

Mr. OSE. Mr. Tierney.

Mr. TIERNEY. I feel like I should offer somebody some rebuttal time, but I am not sure who.

Ms. Claybrook, go ahead.

Ms. CLAYBROOK. Well, the chairman didn't ask me about cost-benefit analysis.

Mr. OSE. Consider asked.

Mr. TIERNEY. My time just expired. I get to Dr. Belzer and I sit here.

Ms. CLAYBROOK. Well, our concern about cost-benefit analysis is that, different than in your daily lives, which Dr. Belzer mentions, the value and enjoyment of clean air, for example is priceless, and that is what Dr. Heinzerling's book discusses. There are many priceless elements to the benefits of regulation that are simply non-calculable, and so when you reduce it to cost and benefit analysis in monetary terms, those are eliminated, those are ignored; they don't get counted.

In addition, Dr. Belzer is right, the cost issue is very complicated, and the fact is that most of the time agencies, because they don't have the resources to collect the cost data, evaluate the cost data, they just rely on what the industry claims are; and often, as I have mentioned already, they are much less.

On the benefits side, it is very expensive to collect the benefits. I give you one example of the agency I used to regulate, that regulates the auto industry, and that is on the national accident sampling system, which is the collection of data about harm in auto crashes, and the fatal accident reporting system, when I was in office, the budget was $20 million, and that was 24 years ago. The budget is now $17 million. The agency is collecting one-fifth of the data that it used to collect because the budget has not kept up with it, even with inflation, much less where it was 24 years ago. So the benefit data are tremendously degraded.

How is the agency going to comply with your requirement, Mr. Chairman, that it do a cost-benefit analysis, even if you could change the value of a life into a dollar? It can't. For example, the finding of the problem with the Firestone tire was completely outside the agency's scope, because it just didn't have the data. The harm to children in auto crashes is completely uncalculated by this agency, and we all know that it is the largest killer of people between age 2 and 34 in the United States of America. But, they can't collect that data because it is too obscure, given the small amount of money they have to collect such data today.

So, when you argue that there should be these calculations, even aside from the prices element, there is no way. And, talk about EPA. EPA has a larger budget than the National Highway Traffic Safety Administration, but it administers a wide variety of programs. There is no way that they can collect the benefit data.

So, I just think that it is fraudulent. The reason I use that word, because the information isn't there. Even if Dr. Belzer and I agreed on the adequacy of the agency's efforts, there is no capacity to do this. And, I think that when you say that the agency should do this with current regulations, then you look at it 10 years hence, and you don't even go back and adjust the way this regulation has been implemented, what the costs really are to the industry at that time, what the benefits are that have come out, and you want a regulatory accounting without any update, I just think it is an impossibility.

Mr. TIERNEY. I am always mindful, when we talk about trying to measure these things. The oil refinery industry used to come in here all the time and bellyache that they just couldn't build a single new refinery, they couldn't get a single new permit for a 10-year period of time because of regulations and regulations. And, when we finally brought them in and we asked the administrator of the EPA how many oil refinery permits had been sought in that period of time, it was zero. We found out they hadn't asked for one because they found out it was cheaper for them to expand the existing ones, so they can come in and concoct more information. And, there was a tremendous amount of information on that, too, of the overestimate of the costs on that. And, when the requirements were actually implemented, sometimes they ended up to be less than a single-digit percentage of what the estimates had originally been.

Mr. Verchick, is there anything you would like to add before we close out here?

Mr. VERCHICK. Yes. I would like to say just one more thing about the cost-benefit analysis, because I think intuitively what people want is they want more information. They think, well, if cost-benefit analysis gives me some numbers, I would rather have the numbers, even if they are flawed, than not have the numbers.

I am against that way of thinking, and the reason is that it is not that these numbers that you see on these tables are somehow mistaken in a small way; they are worse than having no information, because they suggest things that clearly aren't true. Some of these numbers are based on a discount rate into the future of deaths at 7 percent, some are based on 3 percent. Well, what is the difference of discounting a saved life 30 years from now, 3 percent or 7 percent? Well, the difference is, if you work it out, a 3 to 1 ratio. So some of these rules you are looking at are either three times the benefit of human lives saved or a third of the benefit of human lives saved. And, of course, there is no indication of when what number is being used uniformly.

And, that is just one example of having information that is really worse than not having information at all. And that is why I think that cost-benefit analysis is wonderful things that we have market prices for. But no other country that I am aware of is using cost-benefit analysis to such a degree in the environmental area, which leads me to think that it is something less than common sense.

Mr. OSE. Mr. Schrock.

Mr. SCHROCK. Thank you, Mr. Chairman. I am going to probably talk about one of Ms. Claybrook's favorite topics, and that is automobiles. By the way, in the spirit of full disclosure, my wife and I each have an SUV, and my son is about ready to buy one. I know, it is terrible.

Ms. CLAYBROOK. I hope it is a recent model.

Mr. SCHROCK. Brand new.

Ms. CLAYBROOK. Brand new? Oh, that is a little bit better.

Mr. SCHROCK. But, in full disclosure, I wanted to tell you that.

You know, you talked about 40,000 highway deaths, and Dr. Belzer was talking about something about the west, what was it?

Ms. CLAYBROOK. Reclamation, Bureau of Reclamation.

Mr. SCHROCK. No, no, no, some book title.

Mr. BELZER. Oh, it is called "Damming the West."

Mr. SCHROCK. Oh, "Damming the West." Speaking of damning the west and 40,000 highway deaths, I just came back from California, where I spent 10 days, most of it on the 405, and I can tell you where a lot of those 40,000 deaths are going to come from, just because of the way they drive. It is not the way the car is built, it is just the way people drive out there and other places.

But in her written statement to this committee in a previous year, Ms. Dudley said, "Studies reveal that a reallocation of current spending from lower risk to higher risk problems could greatly increase the lifesaving benefits of regulations designed to reduce health and safety risks and achieve other social goals." Question to Ms. Claybrook: "If these studies are correct in whole or in part, isn't regulatory accounting essential to better protect public health and safety? If we don't know the costs or benefits of a regulation, how do we know if we are truly protecting the public and saving lives?"

And that was a roundabout way to get there, but that was a question.

Ms. CLAYBROOK. Well, first of all, I would just like to comment that no matter how people drive, they also do crash, or someone crashes into you. And, so, there was a wonderful analytical piece of work that was done in 1966 by the first administrator of the National Highway Traffic Safety Administration, and he divided that one-twenty-fifth of a second crash into three parts: what caused the crash, what causes the injury, and the after treatment. And all of those are relevant to whether you live.

And, so, the problem with SUVs is that even if you don't roll over, but someone else crashes into you, there is a possibility that because the roof crushes in and the belts don't cinch up and then you roll over, that you are going to die anyway, even if you are the best driver in the world.

I just wanted to make that statement for the record.

Mr. SCHROCK. But it could be the same way with sedans as well?

Ms. CLAYBROOK. Yes, but they don't roll over as frequently. And, the problem with the SUV is it has this greenhouse roof, and so, it sticks up more than the roof, and so if you roll, when you roll in a car it rolls without smashing the roof as much; whereas, if you are in an SUV, the roof smashes in more, and you are tall, and your head is going to be smashed. So, I just would point that out.

Mr. SCHROCK. OK, but I am probably as bad a driver as anybody, and I have had no problem with my SUV.

Ms. CLAYBROOK. OK. Well, that was just a little comment on auto safety injury prevention.

Mr. SCHROCK. I understand.

Ms. CLAYBROOK. Would you repeat your question?

Mr. SCHROCK. OK. We talked about Ms. Dudley's statement when she was here in a previous year, and if those studies are correct in whole or in part, isn't regulatory accounting essential to better protect public safety and health? And, if we don't know the cost or benefits of a regulation, how do we know if we are truly protecting the public and saving lives?

Ms. CLAYBROOK. Well, at the National Highway Traffic Safety Administration, the agency I am most familiar with in that regard,

there are regulatory evaluations done all the time to look at whether or not the estimates that the agency made for lives saved are in fact being saved; and in some instances they say it is more, in some instances it is less, and in some instances it is about the same. So, there is an evaluation done of the actual lives saved based on the data that the agency has. As I have said, part of the problem is that most of these agencies aren't funded sufficiently to get the data, and so, if you want to really have that, I would urge this agency to go to the Appropriations Committee and ask them to please increase the capacity of these agencies to do this work.

I don't say that data are not important. I think data are important. They are important. And, it is important for the public to be able to evaluate them and to look at them and to consider them. But when you talk about regulatory accounting, which takes costs-benefits and it monetized benefits that are non-monetizable, and then you take it to the next step, now, that is fine when you are making a decision as a regulator, to look at the numbers and then to make an evaluation and to make a decision. And, people can argue with you about it and, as you know, the standard for the courts is whether or not it is an abuse of discretion or whether it is substantial evidence on which you based your decision; and, that is, in our society, the way we evaluate what a regulator does in the courts. And, we delegate that authority to the agencies to do that, and we can argue with them, and we have public comment and all the rest.

To take it to the next step and say it can only be in monetized numbers, and then we are going to do a regulatory accounting and evaluate what is most important or not important then, loses the value of the human judgment; and I don't think you would want to do that for yourself, and I certainly don't want to do that for myself or for the public, because the value that we are able to express in terms of do we try and prevent death or injury or environmental health is as important in many ways as the costs and benefits as it is monetized. So you don't want to take the human decision-maker out. If we did that, we could just do it on a calculator and just have a calculator make all these decisions.

Mr. SCHROCK. Mr. Chairman, I know my time is up, but since I quoted Ms. Dudley, I would like to ask her if she would like to comment. If not, that is fine.

Ms. DUDLEY. Yes, just briefly. I agree that, when we do big cost-benefit analyses of rules that affect everyone in the Nation, we are losing some of the value of human judgment. But, what I am concerned about is that we are losing the value of the judgment of the people who are going to be affected by the rule. So, for example, with seatbelts, I am forced now to put my child in the back seat because there is an air bag in the front seat. I would rather buckle my child than have that air bag.

So, while we agree on some of the problems with cost-benefit analysis, I think the real problem is that we are not allowing enough human judgment, enough choice by individuals in the country. And that doesn't question the value of regulatory accounting, but it expands this notion of cost-benefit analysis and human judgment.

Ms. CLAYBROOK. But when your husband is in the front seat, you would want the air bag for him, I take it.

Ms. DUDLEY. No, because he buckles a seatbelt. We buckle our seatbelts.

Ms. CLAYBROOK. I know, but that is not enough, because you are going to have head injuries.

Ms. DUDLEY. No, but, see, that is it; I should make that decision rather than you. That is my point, that is a decision I think that individuals can make. And, that is a lot of what regulation does, it restricts individuals.

Mr. TIERNEY. So you do or you do not like your husband?

Ms. DUDLEY. I love my husband.

Mr. OSE. Keep in mind you are sworn.

Ms. DUDLEY. And, he is not even here.

Mr. OSE. Well, I want to thank our witnesses for joining us today. As with the first panel, we will leave the record open for 10 days to undoubtedly followup with some of you with written questions. And, to the extent that you could have timely response, that would certainly be appreciated.

Dr. Belzer, good luck.

Mr. BELZER. Thank you.

Mr. OSE. You have big days ahead of you.

We are adjourned.

[Whereupon, at 12:12 p.m., the subcommittee was adjourned, to reconvene at the call of the Chair.]

[Additional information submitted for the hearing record follows:]

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March 4, 2004

BY FACSIMILE

The Honorable John Graham
Administrator
Office of Information and Regulatory Affairs
Office of Management and Budget
Washington, DC 20503

Dear Dr. Graham:

This letter follows up on the February 25, 2004 hearing of the Government Reform Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs, entitled "How to Improve Regulatory Accounting: Costs, Benefits, and Impacts of Federal Regulation – Part II." Please respond to the enclosed followup questions for the record.

Please hand-deliver the agency's response to the Subcommittee majority staff in B-377 and the minority staff in B-350A Rayburn House Office Building not later than March 19, 2004. If you have any questions about this request, please call Subcommittee Staff Director Barbara Kahlow on 226-3058.

Thank you for your attention to this request.

Sincerely,

Doug Ose
Chairman
Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs

Enclosure

cc The Honorable Tom Davis
The Honorable John Tierney

Q1. Integration in the Fiscal Budget. Current law (codified as 31 U.S.C. 1105 Note for "Budget contents and submission to Congress," USCA pp. 219-237) requires that the Office of Management and Budget (OMB) submit its annual regulatory accounting statement and associated report on impacts "with" the President's Budget. This year, OMB missed this statutory deadline by submitting its draft (vs. final) report 11 days after the deadline; thereby, preventing Congressional Subcommittees from submitting fully informed recommendations for this year's Budget Resolution. Also, a public Notice of its Availability was not published in the Federal Register until 18 days after the statutory deadline.

To prevent this problem, on June 11, 2003, I introduced the "Paperwork and Regulatory Improvements Act" (H.R. 2432). Section 6 of this bi-partisan bill addresses improvements to regulatory accounting, including a change so that the annual regulatory accounting statement and associated report will be submitted "as part of" (vs. "with") the President's Budget. This provision provides OMB with considerable flexibility regarding in which of the various Budget documents it will present this information.

To increase its utility to Congress, would you support a requirement to integrate regulatory information in the President's Budget documents? If not, why not?

Q2. Regulatory Budget. OMB currently uses an Information Collection Budget (ICB) for OMB and the agencies to manage paperwork burdens on the public. Section 6 of H.R. 2432 addresses improvements to regulatory accounting, including a requirement for OMB to conduct a multi-agency study of regulatory budgeting.

Do you support such a study to see if this tool would help OMB and the agencies rank risks and prioritize, then make choices between new or revised regulatory programs and among alternative approaches, to maximize benefits and minimize costs to the regulated public?

Q3. Input from the Agencies. The law requires OMB to include, in its annual accounting statement, data separately for each agency and for each agency regulatory program. OMB's February 13, 2004 Draft Report is missing data on many agencies and most agency regulatory programs. In fact, one agency regulatory program was removed due to OMB's policy of limiting its data to only major rules issued in a "rolling" 10-year period.

I have asked OMB to issue an annual OMB Bulletin to the agencies for aggregate and new regulatory burden, as it does in annual OMB Bulletins to the agencies for aggregate and new paperwork burden. To date, OMB has not done so. Section 6 of H.R. 2432 addresses improvements to regulatory accounting, including requiring agencies to submit information, **where available**, for OMB's annual regulatory accounting statements.

Without agency input, how does the Administration expect to include complete aggregate agency-by-agency and agency program detail in OMB's subsequent annual regulatory accounting reports, as required by law?

Q4. Inconsistent Agency Estimates & OMB Returns. In the just-released draft report, OMB states that estimates presented "are based on agency information or transparent modifications of agency information performed by OMB" (p. 2) and "[a]gencies continue to take different approaches to monetizing benefits for rules that affect small risks of premature death. As a general matter, we continue to defer to the individual agencies' judgment" (p. 34). OMB also states, "Any aggregation involves the assemblage of benefit and cost estimates that are not strictly comparable. In part to address this issue," on September 17, 2003, OMB issued Circular A-4, "Regulatory Analysis" (p. 3).

OMB's written testimony states, "The final guidelines are designed to help analysts in the regulatory agencies by encouraging good regulatory impact analysis and **standardizing** the way that benefits and costs of Federal regulations are measured and reported" (emphasis added, p. 3).

The Chief Counsel for Advocacy of Small Business Administration's written testimony states, "We encourage OMB to use its return letter authority to enforce agency compliance with Circular A-4" (p. 6) and "Advocacy strongly recommends that OMB issue return letters on a rule-by-rule basis to enforce agency compliance with the Executive Order 12866 and OMB Circular A-4" (p. 9).

a. In May 2001, former OMB Director Mitch Daniels pledged to this Subcommittee to return agency regulatory submissions that were non-compliant with the Unfunded Mandates Reform Act. In that vein, **will OMB return for revision** all agency cost-benefit analyses that are non-compliant with its new Circular? If not, why not?

b. Will OMB adjust agency cost-benefit estimates in OMB's future annual regulatory accounting reports to ensure more consistent and reliable aggregate information? If not, why not?

Q5. Impact on Small Businesses. The law requires OMB to submit not only a regulatory accounting statement but also an associated report on the impacts of Federal rules and paperwork on selective groups, such as small business. Last year, OMB failed to submit this required element in both its February draft and September final reports. On October 24, 2003, Small Business Subcommittee Chairman Ed Schrock wrote OMB about last year's final report. He stated, "By law, every regulation that is certified to have a significant impact on a substantial number of small entities is required to develop a Regulatory Flexibility Analysis. Within each of the initial and final versions of this

agency analysis is a statement of the potential impact of the rule on small business." Also, Mr. Sullivan's written testimony states, "the Draft OMB Report would also benefit from *small business* impact analyses that should be prepared for rules reviewed by OIRA" (p. 4).

OMB's just-issued draft report includes a less than 3-page discussion of impacts on small business (pp. 25-27).

a. Did the Administration review each of the agencies' Regulatory Flexibility Analyses for its rolling 10-year period? If not, why not?

b. Has OMB asked the agencies for any data they may have on such impacts? If not, why not?

c. Wouldn't such data help in analyzing opportunities for sunset reviews of individual agency rules or of an entire agency regulatory program?

Q6. Impact on State/Locals. The law requires OMB to submit "an analysis of impacts of Federal regulation on State, local, and tribal government." OMB's draft report includes a 3-page discussion solely about seven Environmental Protection Agency major rules issued in the past eight years (pp. 23-25).

a. Does OMB have any estimates of the impact of Federal rules and paperwork imposed on State and local governments by other agencies, such as the Department of Health and Human Services' Centers for Medicare and Medicaid Services? If not, why not? And, has OMB asked the State and Local Interest Groups – such as the National Governors Association – for any data they have on such impacts? If not why, not?

b. Wouldn't such data help in analyzing opportunities for sunset reviews of individual agency rules or of an entire agency regulatory program?

Q7. Missing Data on Older Rules. OMB's February 13, 2004 Draft Report again limits its data presentation to major rules issued during a "rolling" 10-year period: October 1993 to September 2003. This 10-year limitation is not statutorily-based. In fact, many major rules were issued before October 1993 and are still burdensome on the public. OMB's draft states, "Based on information contained in this and previous reports, the total costs and benefits of all Federal rules now in effect (major and non-major, including those adopted more than 10 years ago) could easily be a **factor of ten or more larger** than the sum of the costs and benefits reported" herein (emphasis added, p. 6).

What steps, if any, has OMB taken to include available data for the still active major rules issued from 1981 (under President Reagan's E.O.) to 1993 (February 17, 1981 to September 30, 1993), and estimates for the still active major rules issued before 1981?

SEC'd 3/26/04

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

ADMINISTRATOR
OFFICE OF
INFORMATION AND
REGULATORY AFFAIRS

March 26, 2004

The Honorable Doug Ose
Chairman, Subcommittee on Energy Policy,
Natural Resources and Regulatory Affairs
Committee on Government Reform
U.S. House of Representatives
B-377 Rayburn
Washington, D.C. 20515-6143

Dear Mr. Chairman:

Thank you for your letter of March 4, 2004, enclosing additional questions as a follow-up to your February 25, 2004, hearing on Improving Regulatory Accounting. I appreciated the opportunity to testify before the Subcommittee.

Enclosed are the Office of Management and Budget's responses to your follow-up questions. If you would like any additional information, please contact me at your convenience.

Sincerely,

John D. Graham, Ph.D.
Administrator

Enclosure

cc: The Honorable Tom Davis
The Honorable John Tierney

Q1. *Integration in the Fiscal Budget. Current law (codified as 31 U.S.C. 1105 Note for "Budget contents and submission to Congress," USCA pp. 219-237) requires that the Office of Management and Budget (OMB) submit its annual regulatory accounting statement and associated report on impacts "with" the President's Budget. This year, OMB missed this statutory deadline by submitting its draft (vs. final) report 11 days after the deadline; thereby, preventing Congressional Subcommittees from submitting fully informed recommendations for this year's Budget Resolution. Also, a public Notice of its Availability was not published in the Federal Register until 18 days after the statutory deadline.*

To prevent this problem, on June 11, 2003, I introduced the "Paperwork and Regulatory Improvements Act" (H.R. 2432). Section 6 of this bi-partisan bill addresses improvements to regulatory accounting, including a change so that the annual regulatory accounting statement and associated report will be submitted "as part of" (vs. "with") the President's Budget. This provision provides OMB with considerable flexibility regarding in which of the various Budget documents it will present this information.

To increase its utility to Congress, would you support a requirement to integrate regulatory information in the President's Budget documents? If not, why not?

Answer: Since last summer, at the Subcommittee staff's request, OMB and Subcommittee staff have been informally discussing H.R. 2432. Our sense is that these discussions have been constructive, and we have appreciated the opportunity to engage in this dialogue.

One of the concerns that OMB has raised during these discussions relates to the provision in HR 2432 that would amend existing law, under which OMB has been required to submit the annual cost-benefit report to Congress "with" the President's Budget. Under the proposal in HR 2432, Congress would amend existing law to require that the annual cost-benefit report be submitted "as part of" the President's Budget. We are concerned about this proposed change to current law for several reasons. First, this would impose a mandate on the President with respect to what information the President must include in his Budget submission to Congress. We believe that the President should have the discretion to determine what information he wants to submit as part of his Budget.

Second, under existing law, the draft cost-benefit report that OMB issues in February, with the Budget, is subject to public comment, interagency review, and peer review. Then, in response to comment and reviews OMB receives, OMB revises the report and issues the final version of the report later in the year. If the cost-benefit report were made "a part of" the President's Budget, we have concerns about how the public comment and review procedures would work and how they could be incorporated into the development of the President's Budget.

In addition, during our informal discussions with the Subcommittee staff, OMB staff have raised the question of the benefit that would result from having the cost-benefit

report be submitted "as part of" the Budget rather than "with" the Budget. Under existing law, OMB issues a cost-benefit report each and every year, and each year's report presents regulatory cost and benefit information that cover a series of years. Thus, with respect to the regulatory accounting section of the report, each year's report provides only one additional year's information on the costs and benefits of Federal regulations -- namely, information concerning those regulations that agencies issued within the past year. Information concerning the benefits and costs of those recently-issued regulations that are economically significant is available in the Regulatory Impact Analyses that the agencies prepared for those rules, and this information is presented in a consolidated form when OMB releases the draft cost-benefit report for public comment in February. In addition, if Committees and Members of Congress want to review the activities of the rulemaking agencies over a longer timeframe, they can review OMB's most recent final cost-benefit report. For example, OMB's final cost-benefit report for 2003 was issued in September of last year, and it provided a presentation of the costs and benefits of Federal regulations for a ten-year period running from October 1, 1992 to September 30, 2002. Thus, to the extent that Committees and Members, and their staffs, have wanted to learn more about the costs and benefits of Federal regulations over the past decade, they have been able to review OMB's final report for 2003, which is on OMB's website, and they can now review OMB's draft report for 2004, which is also on OMB's website. Accordingly, we recommend that existing law not be amended to require the President to submit the annual cost-benefit report "as part of" the President's Budget rather than "with" the Budget.

Q2. *Regulatory Budget. OMB currently uses an Information Collection Budget (ICB) for OMB and the agencies to manage paperwork burdens on the public. Section 6 of H.R. 2432 addresses improvements to regulatory accounting, including a requirement for OMB to conduct a multi-agency study of regulatory budgeting.*

Do you support such a study to see if this tool would help OMB and the agencies rank risks and prioritize, then make choices between new or revised regulatory programs and among alternative approaches, to maximize benefits and minimize costs to the regulated public?

Answer: Since last summer, at the Subcommittee staff's request, OMB and Subcommittee staff have been informally discussing H.R. 2432. Our sense is that these discussions have been constructive, and we have appreciated the opportunity to engage in this dialogue.

As Dr. Graham stated in his oral testimony during this hearing, we are enthusiastic about the idea of trying to move forward with a pilot project to study a regulatory budget. During these discussions, however, OMB staff has raised some concerns. Our first concern is about the workload implications of the study, given the limited resources available to OMB and the agencies. OMB staff and the Subcommittee staff have discussed options for addressing these workload concerns. In addition, by requiring this study to be conducted, H.R. 2432 would not amend any of the underlying laws that

govern the Federal Government's regulatory programs. If the Executive Branch wanted to carry out the kind of study envisioned by H.R. 2432, we could do so under existing authorities. Rather than simply adding another mandatory study, the Subcommittee might consider whether any existing OMB studies are no longer necessary.

Q3. *Input from the Agencies. The law requires OMB to include, in its annual accounting statement, data separately for each agency and for each agency regulatory program. OMB's February 13, 2004 Draft Report is missing data on many agencies and most agency regulatory programs. In fact, one agency regulatory program was removed due to OMB's policy of limiting its data to only major rules issued in a "rolling" 10-year period.*

I have asked OMB to issue an annual OMB Bulletin to the agencies for aggregate and new regulatory burden, as it does in annual OMB Bulletins to the agencies for aggregate and new paperwork burden. To date, OMB has not done so. Section 6 of H.R. 2432 addresses improvements to regulatory accounting, including requiring agencies to submit information, **where available**, *for OMB's annual regulatory accounting statements.*

Without agency input, how does the Administration expect to include complete aggregate agency-by-agency and agency program detail in OMB's subsequent annual regulatory accounting reports, as required by law?

Answer: Since last summer, at the Subcommittee staff's request, OMB and Subcommittee staff have been informally discussing H.R. 2432. Our sense is that these discussions have been constructive, and we have appreciated the opportunity to engage in this dialogue.

During these discussions, OMB staff have explained the data limitations that exist. Specifically, whereas agencies develop regulatory impact analyses for those rules that are economically significant, they typically do not do so for other rules. In addition, even in the case of the economically significant rules, the analyses consist of estimates of anticipated costs and benefits. Agencies typically do not conduct a "look back" that attempts to determine what have been the actual costs and benefits resulting from Federal regulations.

Finally, OMB staff have indicated that OMB has concerns about amending the language that is found in the existing law, which requires OMB to submit regulatory cost and benefit information to Congress "to the extent feasible." If Congress were to enact a parallel provision, such as that in H.R. 2432, that would require agencies to submit to OMB the information that OMB would then use in preparing its report to Congress, we believe that such a parallel provision should similarly provide that the information to be submitted shall be "to the extent feasible." We do not see a reason why the agencies, in their submissions to OMB, should operate under a different standard than applies to OMB in its submissions to Congress. Both the agencies and OMB should be submitting information "to the extent feasible."

4. *Inconsistent Agency Estimates & OMB Returns. In the just-released draft report, OMB states that estimates presented "are based on agency information or transparent modifications of agency information performed by OMB" (p. 2) and "[a]gencies continue to take different approaches to monetizing benefits for rules that affect small risks of premature death. As a general matter, we continue to defer to the individual agencies' judgment" (p. 34). OMB also states, "Any aggregation involves the assemblage of benefit and cost estimates that are not strictly comparable. In part to address this issue," on September 17, 2003, OMB issued Circular A-4, "Regulatory Analysis" (p. 3).*

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a. *In May 2001, former OMB Director Mitch Daniels pledged to this Subcommittee to return agency regulatory submissions that were non-compliant with the Unfunded Mandates Reform Act. In that vein,* ***will OMB return for revision*** *all agency cost-benefit analyses that are non-compliant with its new Circular? If not, why not?*

Answer: It is the Administration's policy that all regulatory impact analyses for economically significant proposed rules must comply with Circular A-4 after January 1, 2004, and that all regulatory impact analyses for economically significant final rules mus comply with Circular A-4 after January 1, 2005. A regulatory impact analysis that is not compliant with Circular A-4 will be a basis for returning rules to agencies; however, a return letter is just one of many tools that OIRA will use to help agencies comply with th new Circular.

b. *Will OMB adjust agency cost-benefit estimates in OMB's future annual regulatory accounting reports to ensure more consistent and reliable aggregate information? If not, why not?*

Answer: The new Circular A-4, on page 17, states that agencies should clearly set out th basic assumptions, methods, and data underlying the analysis and discuss the uncertainties associated with the estimates. A qualified third party reading the analysis should be able to understand the basic elements of the analysis and the way in which the agency developed its estimates. OMB expects that these new disclosure requirements an the new guidelines in general will lead to estimates that are more comparable across

agencies. We are aware of this issue, however, and will continue to monitor the comparability of estimates across agencies and the effect of the new Circular on comparability. As the Subcommittee points out, a goal of our Circular is to encourage the standardization of the way that benefits and costs of rules are measured and reported.

Q5. *Impact on Small Businesses. The law requires OMB to submit not only a regulatory accounting statement but also an associated report on the impacts of Federal rules and paperwork on selective groups, such as small business. Last year, OMB failed to submit this required element in both its February draft and September final reports. On October 24, 2003, Small Business Subcommittee Chairman Ed Schrock wrote OMB about last year's final report. He stated, "By law, every regulation that is certified to have a significant impact on a substantial number of small entities is required to develop a Regulatory Flexibility Analysis. Within each of the initial and final versions of this agency analysis is a statement of the potential impact of the rule on small business." Also, Mr. Sullivan's written testimony states, "the Draft OMB Report would also benefit from* small business *impact analyses that should be prepared for rules reviewed by OIRA" (p. 4).*

OMB's just-issued draft report includes a less than 3-page discussion of impacts on small business (pp. 25-27).

a. *Did the Administration review each of the agencies' Regulatory Flexibility Analyses for its rolling 10-year period? If not, why not?*

Answer: OMB did review these small business impact analyses during the original review of the final rules included in our cost-benefit report, but has not aggregated information on these rules in the 2004 draft report. OMB is open to discussing this type of review with the SBA Office of Advocacy. As the subcommittee has noted, OMB continues to expand the breadth of our reports to the extent feasible, and is open to discussion on further directions these reports may take. One concern that we have, however, is that Advocacy already produces a very comprehensive report on Agency compliance with the Regulatory Flexibility Act. We would not want to duplicate and introduce possible inconsistencies into the process of reviewing agency activity under the Regulatory Flexibility Act, which is why we will work with Advocacy under our Memorandum of Understanding to discuss this issue.

b. *Has OMB asked the agencies for any data they may have on such impacts? If not, why not?*

Answer: OMB has not asked the agencies to provide comprehensive data. OMB is open to discussing this type of data submission with the SBA Office of Advocacy. As the subcommittee has noted, OMB continues to expand the breadth of our reports to the extent feasible, and is open to discussion on further directions these reports may take. As we mentioned before, if Congress were to enact a provision that would require agencies to submit to OMB any information that OMB would then use in preparing its report to

Congress, we believe that such a provision should provide that the information to be submitted shall be "to the extent feasible." We do not see a reason why the agencies, in their submissions to OMB, should operate under a different standard than applies to OMB in its submissions to Congress. Both the agencies and OMB should be submitting information "to the extent feasible."

c. *Wouldn't such data help in analyzing opportunities for sunset reviews of individual agency rules or of an entire agency regulatory program?*

Answer: This data may be useful for retrospective reviews of regulations; however, a more useful avenue for regulatory reform would likely involve a direct retrospective analysis of regulatory impact, including whether or not the regulation in question performed as expected. Agencies typically do not conduct a "look back" that attempts to determine what have been the actual costs and benefits resulting from Federal regulations; however, academic studies of retrospective regulatory impact have found that both costs and benefits can be over or underestimated. Some of the strongest candidates for regulatory reform are likely those rules that had unintended consequences, which only retrospective studies could identify.

Q6. *Impact on State/Locals. The law requires OMB to submit "an analysis of impacts of Federal regulation on State, local, and tribal government." OMB's draft report includes a 3-page discussion solely about seven Environmental Protection Agency major rules issued in the past eight years (pp. 23-25).*

a. *Does OMB have any estimates of the impact of Federal rules and paperwork imposed on State and local governments by other agencies, such as the Department of Health and Human Services' Centers for Medicare and Medicaid Services? If not, why not? And, has OMB asked the State and Local Interest Groups – such as the National Governors Association – for any data they have on such impacts? If not why, not?*

Answer: The report on State, local, and tribal government focused on the 7 EPA rules because these 7 rules were the only rules in the past 8 years that were designated as a major rule under the Unfunded Mandates Reform Act because they had impacts on State, local, or tribal government of over $100 million (adjusted for inflation) in any one year. Other agencies certainly do impose burdens on State, local, and tribal governments; however, just as we focus on economically significant rules that are responsible for the majority of the costs and benefits of regulation, we focus on major rules that we believe are responsible for the majority of unfunded mandates on State, local, and tribal governments.

OMB has solicited input from State and local governments and interest groups in a variety of ways. For example, in our 2002 draft report, we directly solicited input from States and localities on the adequacy of the consultation opportunities they were provided by Federal agencies during their rulemaking processes. Although we did not receive any

responses from State and local entities in response to that inquiry, State and local governments were among the entities that have provided us with valuable recommendations of regulations needing reform as part of our draft cost-benefit reports in 2001 and 2002.

b. Wouldn't such data help in analyzing opportunities for sunset reviews of individual agency rules or of an entire agency regulatory program?

Answer: This data may be useful for retrospective reviews of regulations; however, a more useful avenue for regulatory reform would likely involve a direct retrospective analysis of regulatory impact, including whether or not the regulation in question performed as expected. Agencies typically do not conduct a "look back" that attempts to determine what have been the actual costs and benefits resulting from Federal regulations; however, academic studies of retrospective regulatory impact have found that both costs and benefits can be over or underestimated. Some of the strongest candidates for regulatory reform are likely those rules that had unintended consequences, which only retrospective studies could identify.

Q7. Missing Data on Older Rules. OMB's February 13, 2004 Draft Report again limits its data presentation to major rules issued during a "rolling" 10-year period: October 1993 to September 2003. This 10-year limitation is not statutorily-based. In fact, many major rules were issued before October 1993 and are still burdensome on the public. OMB's draft states, "Based on information contained in this and previous reports, the total costs and benefits of all Federal rules now in effect (major and non-major, including those adopted more than 10 years ago) could easily be ***a factor of ten or more larger*** *than the sum of the costs and benefits reported" herein (emphasis added, p. 6).*

What steps, if any, has OMB taken to include available data for the still active major rules issued from 1981 (under President Reagan's E.O.) to 1993 (February 17, 1981 to September 30, 1993), and estimates for the still active major rules issued before 1981?

Answer: OMB has made considerable progress. The 2004 draft report contains information on all regulations finalized in the previous 11 years. The totals for the 10-year look-back are reported in Chapter 1, and Appendix B presents an itemized list of the rules that are included in the totals from the 2003 report but are not included in the 2004 report totals since they were finalized between October 1, 1992 and September 30, 1993. In addition, in Chapter 2 of the draft report, OIRA has assembled a time series of new Federal regulatory costs for the past 17 years, from 1987-2003. These costs include rules that did not quantify or monetize benefits, thus this list is even more inclusive than our standard accounting statement in Chapter 1. We do not yet have comparable measures of new regulatory benefits for 1987-2003, although we are in the process of preparing such information for the 2005 Report to Congress. This is the most comprehensive analysis of historic regulatory costs we are aware of.