ADMINISTRATIVE CONFERENCE OF THE UNITED STATES

Benefit-Cost Analysis at Independent Regulatory Agencies

Committee on Regulation - Draft Recommendation

(Apr. 23, 2013)

Benefit-cost analysis (sometimes referred to as cost-benefit analysis) is one of the primary tools used in regulatory analysis to anticipate and evaluate the likely consequences of rules.[1] Although some regulatory benefits and costs are difficult to quantify or monetize, those preparing such analyses generally attempt to estimate the overall benefits that a proposed or final rule would create as well as the aggregate costs that it would impose on society, and then determine whether the former justify the latter. Some observers have disputed its utility in rulemaking,[2] but benefit-cost analysis (and other forms of regulatory analysis) can help ensure that decisionmakers fully contemplate the risks and rewards of any proposed regulatory strategy.[3] Benefit-cost analysis can also improve transparency, helping to ensure that the public and Congress understand why regulatory decisions are made.

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[1] *See* Office of Management and Budget, Circular A-4, September 17, 2003, *available at* http://www.whitehouse.gov/omb/circulars_a004_a-4/ (hereinafter "OMB Circular A-4"). The literature on regulatory analysis, including prior recommendations of the Administrative Conference, has used the term "cost-benefit analysis" in lieu of or in addition to "benefit-cost analysis." Circular A-4 uses the term "benefit-cost analysis," and this recommendation will therefore utilize the same terminology.

[2] Critics of benefit-cost analysis contend that it ignores values that cannot be easily quantified, that benefits can often be difficult to monetize, that it tends to overestimate costs, and that it undervalues future benefits through the application of discounting methodologies. *See, e.g.*, Frank Ackerman & Lisa Heinzerling, *Pricing the Priceless: Cost-Benefit Analysis of Environmental Protection*, 150 U. PA. L. REV. 1553, 1557–60, 1580–81 (2001).

[3] *See* Administrative Conference of the United States, Recommendation 79-4, *Public Disclosure Concerning the Use of Cost-Benefit and Similar Analyses in Regulation*, 44 Fed. Reg. 38,826 (July 3, 1979) ("Wise decisionmaking presupposes that the potential benefits and costs of the actions under consideration will be identified, will be quantified if feasible, and will be appraised in relation to each other."); Cass R. Sunstein, *The Office of Information & Regulatory Affairs: Myths and Realities*, __ HARV. L. REV. __, __ (forthcoming 2013) ("Cost-benefit analysis can be exceedingly important, and in the Obama Administration, several steps were taken to strengthen it, contributing

For more than 30 years, Cabinet departments and independent agencies like the Environmental Protection Agency (but not independent regulatory agencies[4] like the Securities and Exchange Commission (SEC)) have been required by executive orders to conduct benefit-cost or other types of regulatory analyses for their "major" or "economically significant" rules (e.g., those likely to result in annual costs, benefits, or transfer payments[5] of $100 million or more). In 1981, President Ronald Reagan issued Executive Order (EO) 12,291,[6] which instructed those agencies to prepare regulatory impact analyses (including a description of benefits and costs of their draft proposed and final "major rules"), and to submit their draft rules to the Office of Information and Regulatory Affairs (OIRA) within the Office of Management and Budget (OMB) before publication in the Federal Register.[7] Subsequent administrations have reaffirmed the importance of benefit-cost analysis and OIRA review in the issuance of such rules.

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to a situation in which the net benefits of economically significant rules were extraordinarily high."); *cf.* RICHARD L. REVESZ & MICHAEL A. LIVERMORE, RETAKING RATIONALITY: HOW COST-BENEFIT ANALYSIS CAN BETTER PROTECT THE ENVIRONMENT AND OUR HEALTH 10 (Oxford Univ. Press 2008) ("Although cost-benefit analysis, as currently practiced, is . . . biased against regulation, those biases are not inherent to the methodology. If those biases were identified and eliminated, cost-benefit analysis would become a powerful tool for neutral policy analysis.").

[4] As a general matter, "independent regulatory agencies" are those whose heads possess "for cause" removal protection and that enjoy some degree of independence from the executive branch. DAVID E. LEWIS & JENNIFER L. SELIN, ACUS SOURCEBOOK OF UNITED STATES EXECUTIVE AGENCIES 49 (1st ed., 2d Printing Mar. 2013).

[4] *See, e.g.,* Exec. Order No. 12,866, *supra* note 7, § 3(b), which generally defines an "agency" to exclude independent regulatory agencies. However, independent regulatory agencies are covered by the planning requirements in section 4 of the executive order.

[5] Transfer payments are monetary payments from one group to another that do not affect total resources available to society. *See* OMB Circular A-4, *supra* note 1. The most common form is the transfer of federal funds to the recipients of those funds (e.g., grants, food stamps, Medicare or Medicaid funds, and crop payments). In 2010, more than one-third of all major rules were transfer payments. *See* U.S. Cong. Research Service, *REINS Act: Number and Types of "Major Rules" in Recent Years*, R41651, Feb. 21, 2011, by Curtis W. Copeland and Maeve Carey.

[6] Exec. Order No. 12,291, 46 Fed. Reg. 13,193 (Feb. 17, 1981).

[7] *Id.* § 3; *see also* Sunstein, *supra* note 3, at __. Under EO 12,291, agencies were required to submit all draft proposed and final rules to OIRA for review but were only required to prepare regulatory impact analyses for major rules.

Currently, EO 12,866,[8] issued by President Bill Clinton in 1993, requires Cabinet departments and independent agencies to "assess both the costs and benefits of the intended regulation and, recognizing that some costs and benefits are difficult to quantify, propose or adopt a regulation only upon a reasoned determination that the benefits of the intended regulation justify its costs."[9] It also requires them to assess the costs and benefits of "significant" draft proposed and final rules submitted to OIRA for review, and to conduct more thorough analysis of economically significant draft rules.[10]

As noted previously, independent regulatory agencies have traditionally not been subject to the formal benefit-cost analysis requirements imposed by executive order,[11] although several recent Presidents have encouraged those agencies to voluntarily apply the principles contained in the relevant executive orders.[12] All independent regulatory agencies are subject to certain crosscutting statutes that may require some type of regulatory analysis, such as the Regulatory

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[8] Exec. Order No. 12,866, 58 Fed. Reg. 51,735 (Oct. 4, 1993) (President Clinton).

[9] *Id.* § 1(b)(6).

[10] *Id.* § 6(a)(3); *see also* Exec. Order No. 13,563, 76 Fed. Reg. 3821 (Jan. 21, 2011) (President Obama) (stating that the benefits of proposed and final rules must "justify" the costs); Administrative Conference of the United States, Recommendation 88-9, *Presidential Review of Agency Rulemaking*, 54 Fed. Reg. 5207 (Feb. 2, 1989) (suggesting guidelines for the enhanced openness of executive regulatory review and recommending the reconsideration of existing rules looking toward the repeal of unnecessary regulations).

[11] *See, e.g.,* Exec. Order No. 12,866, *supra* note 7, § 3(b), which generally defines an "agency" to exclude independent regulatory agencies. However, independent regulatory agencies are covered by the planning requirements in section 4 of the executive order.

[12] *See, e.g.*, Exec. Order No. 13,579, 76 Fed. Reg. 41,587 (July 14, 2011) (stating that independent regulatory agencies "should promote" the goal articulated in EO 13,563 of producing a "regulatory system that protects public health, welfare, safety, and our environment while promoting economic growth, innovation, competitiveness, and job creation" and that independent regulatory agencies "should comply" with the provisions in EO 13,563 regarding public participation, integration and innovation, flexible approaches, and science "[t]o the extent permitted by law").

Flexibility Act[13] and the Paperwork Reduction Act.[14] In addition, some agency organic acts or other statutes require certain independent regulatory agencies to conduct benefit-cost analyses or consider certain economic effects of their regulations, although the requirements vary significantly from agency to agency. For instance, some agencies (e.g., the Consumer Product Safety Commission) are required to prepare a formal regulatory analysis statement that describes expected costs and benefits prior to issuing certain rules.[15] Other agencies (e.g., the Commodity Futures Trading Commission (CFTC) and the SEC) are required to "consider" costs and benefits or other factors associated with some of their rules, but are nominally under no obligation to prepare a formal benefit-cost analysis.[16] Still other agencies (e.g., the Federal Communications Commission and the Nuclear Regulatory Commission) are not subject to any formal regulatory analysis requirements for most of their rules.

The Conference believes that it is in the interest of the independent regulatory agencies, the executive branch, Congress, and the courts that independent regulatory agencies' current practices relating to benefit-cost analysis be documented. In this light, the report supporting the recommendation examined efforts by independent regulatory agencies to analyze regulatory

[13] 5 U.S.C. §§ 601–12.

[14] 44 U.S.C. §§ 3501–21.

[15] 15 U.S.C. § 2058(f).

[16] CFTC is required to "consider the costs and benefits" of the agency's action before issuing certain rules and orders. 7 U.S.C. § 19(a). The SEC is required, when it is engaged in rulemaking under certain statutory provisions, to "consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation." 15 U.S.C. § 77b(b). Although some courts have applied this language in a manner that effectively imposes a requirement to quantitatively analyze regulatory costs and benefits, *see Bus. Roundtable v. Sec. & Exch. Comm'n*, 647 F.3d 1144, 1148–49 (D.C. Cir. 2011), the relevant statutory language does not provide that the agency must quantify the economic effects of its rules.

benefits and costs in recent major rules.[17] It also examined whether the agencies factor benefits and costs into their decisionmaking. The report indicated that, in many instances, independent regulatory agencies quantify at least some of the costs (and, to a lesser extent, the benefits) created by rules they adopt and, in other instances, such agencies usually provide at least qualitative descriptions of the associated benefits and costs. The report also discusses several factors that the agencies said affected their ability to quantify and monetize regulatory costs and benefits. For example, several agencies mentioned the Paperwork Reduction Act approval process as inhibiting their ability to gather the data needed to prepare regulatory analyses in a timely fashion.[18]

This recommendation encourages agencies to voluntarily adopt certain practices that some independent regulatory agencies (and other agencies) have developed in conducting regulatory analyses. The Administrative Conference recognizes that increasing the attention paid to the impacts of proposed and final rules necessarily requires independent regulatory agencies to make significant tradeoffs among competing priorities, and may result in the substantial use of agency resources, delay in the rulemaking process, and the need to acquire relevant expertise (e.g., hiring staff economists). Nevertheless, some independent regulatory agencies are already subject to benefit-cost and other types of regulatory analysis requirements, and others have

Comment [r1]: Independent Agency staff recommend rephrasing as follows: "The Administrative Conference recognizes that increasing the attention paid to the impacts of proposed and final rules necessarily requires substantial use of limited agency resources. This requires independent regulatory agencies to make significant tradeoffs among competing priorities and may delay the rulemaking process."

[17] *See* Curtis W. Copeland, Economic Analysis and Independent Regulatory Agencies 60–107 (Mar. 29, 2013), *available at* http://acus.gov/sites/default/files/documents/Copeland%20CBA%20Report%203-29-13.pdf.

[18] *See* Administrative Conference of the United States, Recommendation 2012-4, *Paperwork Reduction Act*, ¶ 3, 77 Fed. Reg. 47,800, 47,808 (Aug. 10, 2012) (recommending that agencies "use all available processes for OMB approval for information gathering," including "OMB's available generic clearances and fast track procedures").

voluntarily conducted such analyses, and the Conference therefore wishes to highlight innovative practices undertaken by these agencies.[19]

The recommendation, first, identifies various policies and practices used in several of the independent regulatory agencies and offers a series of proposals to encourage their use in other agencies. Second, the recommendation highlights a series of analytical practices that OMB Circular A-4 recommends to Cabinet departments and independent agencies, and encourages independent regulatory agencies to consider whether those practices may be useful in their own regulatory programs ~~for major rules~~. The recommendation does not seek to establish a one-size-fits-all approach to regulatory analysis, and recognizes that each agency must tailor the analyses it conducts to accord with relevant statutory requirements, its own regulatory priorities, and the potential impact of the analysis on regulatory decisionmaking to ensure proper use of limited agency resources. Finally, the recommendation proposes that, to the extent Congress decides to impose new regulatory analysis requirements, those requirements should be scaled to the significance of the rule and should provide resources sufficient to achieve that mandate. Focusing on those larger rules would minimize the resources required for analysis,[20] while maximizing the potential impact of those analyses on regulatory decisionmaking.

Comment [r2]: Some have proposed deleting recommendation 9 (*see* infra). If the committee ultimately decides to do so, these sentences should also be deleted.

[19] *See, e.g.*, Copeland, *supra* note 17, at 99 (describing the Federal Communications Commission's increased usage of benefit-cost analysis in light of EO 13,579).

[20] Between January 2007 and December 2012, federal agencies published 19,246 final rules, of which 485 were considered "major" rules. See Copeland, *supra* note 17, at Table 1. Expanding the rules on which regulatory analysis is required from "economically significant" or "major" rules to rules considered "significant" under EO 12,866 would likely quintuple the number of analyses required. See http://www.reginfo.gov/public/do/eoCountsSearch for data on this issue.

ADMINISTRATIVE CONFERENCE OF THE UNITED STATES

RECOMMENDATION

Encouraging the Diffusion of Certain Policies and Practices

1. Each independent regulatory agency should develop and keep up to date written guidance regarding the preparation of benefit-cost and other types of regulatory analyses. That guidance should be tailored to the agency's particular statutory and regulatory environment, and should be designed to help ensure that any regulatory analysis the agency undertakes is soundly developed, transparent, consistently conducted, and contributes to agency compliance with applicable statutes and other rulemaking requirements. To accomplish this goal, independent regulatory agencies may choose to adopt or adapt the regulatory analysis practices described in OMB Circular A-4 or any successor government-wide guidance.

2. When an independent regulatory agency prepares a regulatory analysis for a proposed or final rule, the analysis should be developed as early in the rulemaking process as reasonably practical. Once prepared, the analysis may need to be updated as the agency becomes aware of new information that may affect the rulemaking, or if changes are otherwise made to the substance of the rule.

3. When an independent regulatory agency determines that additional analytical expertise or experience may be helpful to prepare a regulatory analysis, it should, to the extent appropriate, consult with other agencies (e.g., through the Council of Independent Regulatory Agencies) and/or with OIRA. This consultation could address such issues as how certain costs and benefits could be quantified or monetized.

Comment [r3]: Independent Agency staff comment: Why must this be mentioned? This isn't a recommendation, and we are aware of A-4's existence. There seems to be a subtle attempt to push OMB A-4 on all of us. See first page, first sentence, which starts out with it. This contradicts ACUS's statement earlier that no "one-size-fits-all".

Comment [r4]: Independent Agency staff comment: Same comment, even though A-4 is not mentioned, OIRA is. This seems to go beyond being a recommendation.

4. Consistent with applicable laws and the procedures and flexibilities permitted in the Paperwork Reduction Act, independent regulatory agencies and OIRA should facilitate the timely collection of high quality information that may be used to support the agencies' regulatory analyses.

Highlighting OMB-Recommended Analytical Practices ~~for Major Rules~~

5. Independent regulatory agencies should consider the appropriateness of the analytical guidance provided in OMB Circular A-4 when evaluating regulations and structuring their regulatory analyses in terms of three general principles: (a) identify the need for the regulation; (b) examine plausible alternative regulatory approaches; and (c) estimate, to the extent possible, the benefits and costs of those alternatives.

6. Consistent with applicable laws and agency resources, independent regulatory agencies should consider including in their regulatory analyses assessments of the impact of not only those actions that are within the agency's statutory discretion but also of those actions that are statutorily mandated. Showing the effects of both types of actions (separately, when practicable) can improve regulatory transparency and allow the public to understand whether the agency or Congress is responsible for regulatory burden.

Comment [r5]: Independent Agency staff comment: We continue to have problems with this recommendation being included at all.
This sentence is not even a recommendation – it seems to belong in the preamble.

7. Subject to the limitations of law and good practice (including preventing the disclosure of information obtained or developed in the course of regulation or supervision of financial institutions, proprietary information or trade secrets, privileged information, or other similar confidential information that would be protected by a Freedom of Information Act exemption or other law), independent regulatory agencies' regulatory analyses should be as transparent and reproducible as possible. In particular, agencies should consider disclosing how

the analyses were conducted, posting the analyses on their websites and other appropriate online fora, and summarizing the methods and results in the notice of proposed rulemaking or preamble to a final rule.

8. Independent regulatory agencies should consider including in the notice of proposed rulemaking and in the preamble to each proposed or final rule a summary statement or table concisely showing the agencies' overall estimates of the expected total benefits, costs, and transfer payments of regulatory actions and reasonable alternatives, including any benefits or costs that could not be quantified or monetized.

Comment [r6]: The committee should consider whether the proposed addition would impose an excess burden on agencies by requiring them to describe costs and benefits of rejected alternatives.

Funding for Additional Benefit-Cost Analysis Requirements

9. If Congress decides to establish new requirements that independent regulatory agencies prepare benefit-cost analyses of their proposed or final rules: (a) the new analysis requirements should be scaled to the significance of the rule (e.g., the distinction between significant and economically significant as set out in EO 12,866), and (b) additional funding for those new analyses should be provided to the agencies, either through direct appropriations (in agencies that rely on appropriated funds) or through an authorization to collect additional fees (in agencies authorized to collect fees sufficient to offset their appropriation each year).

Comment [r7]: Some recommend adding a comma after rules, followed by "Congress should consider whether." Some have also proposed deleting this recommendation entirely.