Administrative Conference Recommendation 2013-2

Benefit-Cost Analysis at Independent Regulatory Agencies

Adopted June 13, 2013

Benefit-cost analysis (also known 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.

[1] *See* Office of Management and Budget, Circular A-4 (Sept. 17, 2003), *available at* http://www.whitehouse.gov/omb/circulars_a004_a-4/ [hereinafter "OMB Circular A-4"]. Much of the literature on regulatory analysis, including prior recommendations of the Administrative Conference, uses 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*, 126 HARV. L. REV. 1838, 1846 (2013) ("Cost-benefit analysis can be

For more than 30 years, Cabinet departments and other executive agencies like the Environmental Protection Agency (but not independent regulatory agencies[4] such as the Federal Trade Commission (FTC)) have been required by executive orders to conduct benefit-cost or other types of regulatory analyses for their "major" or "economically significant" rules.[5] In 1981, President Ronald Reagan issued Executive Order (EO) 12,291,[6] which instructed covered executive agencies to prepare regulatory impact analyses of their draft proposed and final major rules (including a description of benefits and costs), and to submit all of 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. Subsequent administrations have reaffirmed the importance of benefit-cost analysis and OIRA review. Currently, EO 12,866, issued by President William Jefferson Clinton in 1993, requires Cabinet departments and other covered executive 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

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exceedingly important, and in the Obama Administration, several steps were taken to strengthen it, contributing 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 (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). Under Executive Order 12,866, 58 Fed. Reg. 51,735 (Oct. 4, 1993), the term "agency" excludes independent regulatory agencies. *Id.* § 3(b). However, independent regulatory agencies are covered by the planning requirements in section 4 of the executive order.

[5] "Major" and "economically significant" rules include (but are not limited to) rules likely to result in annual costs, benefits, or transfer payments of $100 million or more. *See* Congressional Review Act, 5 U.S.C. § 804(2); Exec. Order No. 12,866, *supra* note 4, § 3(f)(1). 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 so categorized because of the amount of 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) (revoked by § 11 of EO 12,866).

regulation only upon a reasoned determination that the benefits of the intended regulation justify its costs."[7] 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 proposed and final rules.[8]

As noted previously, independent regulatory agencies traditionally have not been subject to the formal benefit-cost analysis requirements imposed by executive order, although several recent Presidents have encouraged those agencies to voluntarily apply the principles contained in the relevant executive orders.[9] Virtually all independent regulatory agencies are subject to certain crosscutting statutes that may require some type of regulatory analysis, such as the Regulatory Flexibility Act[10] and the Paperwork Reduction Act.[11] In addition, some independent regulatory agencies' organic acts or other statutes require them to conduct benefit-cost analyses or to 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 by statute to prepare a formal regulatory analysis statement that describes expected costs and benefits prior to issuing certain rules.[12] Other agencies (e.g., the Commodity Futures Trading Commission (CFTC) and the Securities and

[7] Exec. Order No. 12,866, *supra* note 4, § 1(b)(6).

[8] *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).

[9] *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 "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").

[10] 5 U.S.C. §§ 601–12.

[11] 44 U.S.C. §§ 3501–21.

[12] 15 U.S.C. § 2058(f).

Exchange Commission (SEC)) are required by statute to "consider" costs and benefits or other factors associated with some of their rules.[13] 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 Administrative Conference believes that it is in the interest of the independent regulatory agencies, the executive branch, Congress, the courts, and the public 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 benefits and costs in recent major rules.[14] 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 the major 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.[15]

This recommendation encourages agencies to voluntarily adopt certain practices that some independent regulatory agencies (and other agencies) have developed when conducting

[13] 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). Interpretation of these provisions has been a matter of debate.

[14] *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.

[15] *Cf.* 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").

regulatory analyses for major rules. The Conference recognizes that increasing the attention paid to the economic impact of proposed and final rules might well require substantial use of limited agency resources. This might require independent agencies to make significant tradeoffs among competing priorities and may delay the rulemaking process. Nevertheless, some independent regulatory agencies are already subject to benefit-cost and other types of regulatory analysis requirements, and others have voluntarily conducted such analyses, and the Conference therefore wishes to highlight innovative practices undertaken by these agencies.[16]

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. For example, it recommends that each independent regulatory agency develop written guidance on the preparation of benefit-cost and other types of regulatory analyses. Such guidance 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. Second, the recommendation highlights a series of analytical practices that OMB Circular A-4 recommends to Cabinet departments and other executive agencies for their major rules, and the recommendation encourages independent regulatory agencies to consider whether those practices may be useful in the development of their major rules. For example, it recommends that agencies' analyses be as transparent and reproducible as practicable, subject to the limitations of law and applicable policies (including preventing the disclosure of proprietary information or trade secrets, or other confidential information). 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 or endorse new regulatory analysis requirements on

[16] *See, e.g.*, Copeland, *supra* note 14, at 99 (describing the Federal Communications Commission's increased usage of benefit-cost analysis in light of EO 13,579).

independent regulatory agencies, Congress should consider giving those agencies the discretion to scale the analyses to the significance of the rules, and should consider the agency resources needed to satisfy such requirements.[17]

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. To accomplish this goal, independent regulatory agencies may choose whether or not to adopt or adapt the regulatory analysis practices described in OMB Circular A-4 or any successor government-wide guidance.

2. If 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 made to the substance of the rule.

3. If an independent regulatory agency determines that additional analytical expertise or experience may be helpful to prepare a regulatory analysis (e.g., determining how certain costs or benefits could be quantified or monetized), it should, to the extent appropriate, consult with other governmental entities with expertise in this area.

[17] Between January 2007 and December 2012, federal agencies published 19,246 final rules, of which 485 were considered "major" rules. See Copeland, *supra* note 14, 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.

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 information necessary to develop the agencies' regulatory analyses.

Recommended Practices for Major Rules

5. Independent regulatory agencies should consider the appropriateness of the analytical guidance provided in OMB Circular A-4 when developing regulatory analyses for major rules. They should consider structuring their analyses of those rules 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 the proposed rule and the primary 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. Agencies should consider showing the effects of both types of actions in order to improve regulatory transparency.

7. Subject to the limitations of law and applicable policies, independent regulatory agencies' regulatory analyses should be as transparent and reproducible as practicable. 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 preambles of the notice of proposed rulemaking and the final rule.

8. Independent regulatory agencies should consider including in the preambles of the notice of proposed rulemaking and the 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 the primary alternatives, including any benefits or costs that could not be quantified or monetized.

Recommendations to Congress

9. If Congress decides to establish or endorse new requirements that independent regulatory agencies prepare benefit-cost analyses of their proposed or final rules, it should recognize that agencies need (a) the flexibility to scale the analyses to the significance of the rules and (b) the resources to satisfy such requirements.