

United States Senate Committee on the Budget and
Committee on Homeland Security and Governmental Affairs

Hearing on:

**Accounting for the True Cost of Regulation:
Exploring the Possibility of a Regulatory Budget**

Prepared Statement of Susan E. Dudley

Chairman Johnson, Chairman Enzi, Ranking Member Carper, Ranking Member Sanders, and distinguished members of the Committee, thank you for inviting me to testify at this joint hearing on “Accounting for the True Cost of Regulation: Exploring the Possibility of a Regulatory Budget.” I am Director of the George Washington University Regulatory Studies Center, and Distinguished Professor of Practice in the Trachtenberg School of Public Policy and Public Administration.¹ From April 2007 to January 2009, I oversaw executive branch regulations of the federal government as Administrator of the Office of Information and Regulatory Affairs (OIRA) in the Office of Management and Budget (OMB).

I appreciate the Committees’ interest in exploring the possibility of a regulatory budget. Taxes, and subsequent spending, are one way the federal government redirects resources from the private sector to accomplish public goals. Regulation of private entities—businesses, workers, and consumers—is another. Like the programs supported by taxes, regulations provide benefits to Americans. However, the costs associated with regulatory programs are not subject to the same checks and balances.

As an OECD paper observes, “while governments are required to account in detail for their fiscal spending, regulatory costs or ‘expenditures’ are still largely hidden and there is still no accountability for the total amount of regulatory expenditure which a government requires.”²

¹ The George Washington University Regulatory Studies Center raises awareness of regulations’ effects with the goal of improving regulatory policy through research, education, and outreach. This statement reflects my views, and does not represent an official position of the GW Regulatory Studies Center or the George Washington University.

² Nick Malyshev, *A Primer on Regulatory Budgets*, OECD JOURNAL ON BUDGETING, 2010/3.

Because regulatory costs are less visible (regulations have been called a “hidden tax”³) and they are assumed to be borne by businesses (even though individual consumers and workers ultimately bear them), regulatory tools may seem preferable to direct spending programs for accomplishing policy objectives. As a result, the scope and reach of regulation has been growing.⁴ (An attachment to this testimony presents some proxy measures to illustrate this.) In 2015, there are over 70 federal agencies, employing almost 300,000 people to write and implement regulation.⁵ Every year, they issue tens of thousands of new regulations,⁶ which now occupy over 175,000 pages of regulatory code.⁷

In the U.S., individual regulations are constrained by 1) their enabling legislation, 2) the Administrative Procedure Act, which requires agencies to provide public notice and seek comment before issuing new regulations, and 3) executive requirements for regulatory impact analysis. Presidents of both parties for over 40 years have supported ex ante impact analysis of regulations as a way to make agencies weigh the likely positive and negative consequences of regulations before they are issued.

Executive Order 12866,⁸ issued by President Clinton in 1993, continues to guide the development and review of regulations today (having been reinforced by both President Bush and President Obama). It expresses the philosophy that regulations should (1) address a “compelling public need, such as material failures of private markets”; (2) be based on an assessment of “all costs and benefits of available regulatory alternatives, including the alternative of not regulating”; and (3) “maximize net benefits” to society unless otherwise constrained by law.⁹

³ Wendy L. Gramm, *Regulatory Review Issues, October 1985–February 1988*, 63 ADMINISTRATIVE LAW REVIEW (2011).

⁴ The GW Regulatory Studies Center’s “Reg Stats” page provides various measures of regulatory activity. <http://regulatorystudies.columbian.gwu.edu/reg-stats>

⁵ Susan Dudley & Melinda Warren, REGULATORS' BUDGET INCREASES CONSISTENT WITH GROWTH IN FISCAL BUDGET: AN ANALYSIS OF THE U.S. BUDGET FOR FISCAL YEARS 2015 AND 2016. The George Washington University Regulatory Studies Center and the Weidenbaum Center on the Economy, Government, and Public Policy. (2015) available at <http://regulatorystudies.columbian.gwu.edu/2016-regulators-budget-increases-consistent-growth-fiscal-budget>. Note that “agencies that primarily perform taxation, entitlement, procurement, subsidy, and credit functions are excluded from this report,” so these figures exclude staff developing and administering regulations in the Internal Revenue Service, the Centers for Medicaid and Medicare Services, etc.

⁶ Office of the Federal Register. FEDERAL REGISTER PAGES PUBLISHED 1936 – 2013 (2014) available at: <https://www.federalregister.gov/learn/tutorials>

⁷ Office of the Federal Register. CODE OF FEDERAL REGULATIONS, PAGE BREAKDOWN - 1975 THROUGH 2014. (2015) available at: <https://www.federalregister.gov/learn/tutorials>

⁸ William J. Clinton. E.O. 12866. *Regulatory Planning and Review*, FEDERAL REGISTER, Vo. 58, No. 190. (1993) Available at: http://www.whitehouse.gov/sites/default/files/omb/inforeg/EO12866/EO12866_10041993.pdf

⁹ E.O. 12866, Sec. 1(a)

Applying Fiscal Budget Concepts to Regulation

Despite these requirements for public input and regulatory impact analysis, however, the growth in new regulations continues, and with it concerns that we have reached a point of diminishing returns. The application of fiscal budgeting concepts to regulation holds the potential to bring more accountability and transparency to the regulatory process.

The regulatory budget is premised on the view that the transfer of private resources by regulation is no less a cost imposed by government than the collection and expenditure of private resources through the tax and spending powers. But while government expenditures are constrained by the ability to tax and borrow, regulatory costs are subject to no built-in limitations. By creating a systematic limitation on regulatory costs, a regulatory budget would counteract the tendency by agencies to treat private resources as a “free good.”¹⁰

The idea of a “regulatory budget” is not new.¹¹ In 1980, President Carter’s *Economic Report of the President* discussed proposals “to develop a ‘regulatory budget,’ similar to the expenditure budget, as a framework for looking at the total financial burden imposed by regulations, for setting some limits to this burden, and for making tradeoffs within those limits.” The Report noted analytical problems with developing a regulatory budget, but concluded that “tools like the regulatory budget may have to be developed” if governments are to “recognize that regulation to meet social goals competes for scarce resources with other national objectives,” and set priorities to achieve the “greatest social benefits.”¹²

According to Christopher DeMuth, writing in 1980:

The regulatory budget would operate by close analogy to the conventional fiscal process. Each year (or at some longer interval), the federal government would establish an upper limit on the costs of its regulatory activities to the economy and would apportion this sum among the individual regulatory agencies. This would presumably involve a budget proposal developed by OMB in negotiation with the regulatory agencies, approved by the President, and submitted to Congress for review, revision, and passage. Once the President had signed the final budget appropriations into law, each agency would be obliged to live within its

¹⁰ Jeffrey A. Rosen and Brian Callanan, “*The Regulatory Budget Revisited*,” *ADMINISTRATIVE LAW REVIEW*, Vol. 66, No. 4, 839. (2014)

¹¹ Rosen & Callanan, 2014, provide a concise review of previous research and efforts. 848-853.

¹² Chairman of the Council of Econ. Advisers, 1980 *ECONOMIC REPORT OF THE PRESIDENT*, 125. (1980), *available at* http://fraser.stlouisfed.org/publications/ERP/page/4569/download/46077/4569_ERP.pdf.

regulatory budget for the time period in question. The budget would cover the total costs of all regulations past and present, not just new ones.¹³

Advantages of a regulatory budget

By making more transparent the private sector resources needed to achieve regulatory objectives, a regulatory budget would encourage policy officials in the legislative and executive branches, as well as the public, to consider regulatory priorities and tradeoffs. This transparency would also strengthen political accountability and discipline. Expected benefits would be considered up front (when issuing legislation or new regulations), and elected officials would have to consider how much achieving particular goals are worth.

A pure regulatory budget would require an explicit consideration of the aggregate economic costs of regulation. This transparency would “afford policymakers and the public a more complete picture of the economic footprint of regulation.”¹⁴

Resources would likely be better allocated because policy makers would have incentives to find the most cost-effective ways of achieving policy goals, not only among alternative forms of regulation, but among different vehicles for addressing a problem. It might reduce “the increasing tendency of government to pursue its objectives through regulation rather than taxing and spending—even when regulation is otherwise less desirable—*because* regulation is less constrained.”¹⁵

By constraining the private sector resources that can be committed to achieving regulatory mandates, a regulatory budget could impose internal discipline on regulatory agencies, perhaps lessening the need for case-by-case oversight. By focusing on the costs of regulations and allowing agencies to set priorities and make tradeoffs among regulatory programs, it might remove some of the contentiousness surrounding benefit-cost analysis and presidential oversight.¹⁶ “Faced with a budget constraint, the agencies would measure the costs and benefits of individual regulatory proposals in order to further their own organizational interests rather than to satisfy the minimum requirements of an executive order or judicial review.”¹⁷

A regulatory budget constraint would also encourage evaluation of existing rules’ costs and effects. Despite broad support, initiatives to require ex post evaluation of regulations have met

¹³ Christopher C. DeMuth, *The Regulatory Budget*, REGULATION MAGAZINE, Mar.–Apr. 1980, 31.

¹⁴ Rosen & Callanan, 842.

¹⁵ Demuth, 38.

¹⁶ Susan Dudley, *Improving Regulatory Accountability: Lessons from the Past and Prospects for the Future*, CASE WESTERN RESERVE LAW REVIEW, Vol. 65, Issue 4, 1050. (2015)

¹⁷ DeMuth, 36.

with limited success¹⁸ largely because they did not change underlying incentives. If the issuance of new regulations was contingent on finding a regulatory offset, agencies would have incentives to evaluate both the costs and effectiveness of existing programs.¹⁹

Analytical issues with a regulatory budget

While a regulatory budget holds considerable appeal for making regulatory policy more transparent, accountable, and cost-effective, the analytical problems associated with it are non-trivial. The task of gathering and analyzing information on the costs of all existing regulations in order to establish a baseline budget would be enormous, and the resulting numbers not very reliable. Even defining what should be considered “costs” will be challenging. Estimating the opportunity costs of regulations is not as straightforward as estimating fiscal budget outlays, where past outlays are known and future outlays can generally be predicted with some accuracy. Since the late 1990s, OMB has been compiling agency estimates of the costs (and benefits) of major regulations with mixed results.²⁰

An incremental approach, such as a “regulatory PAYGO,”²¹ would avoid some of these difficulties while retaining many of the benefits of a regulatory budget. Under a regulatory PAYGO or “one-in-one-out” approach, regulatory agencies would be required to eliminate an outdated or duplicative regulation before issuing a new regulation of the same approximate economic impact. Unlike a regulatory budget, agencies would only have to estimate costs for regulations being introduced (which they should already do) and offsetting regulations they propose to remove. Nevertheless, deciding what “costs” to include in estimating budgets or offsets will necessarily be a matter of judgment. Understanding the full social costs of regulation is difficult, if not impossible.

Some regulatory impacts will be harder to estimate than others. What are the costs associated with homeland security measures that reduce airline travelers’ privacy? What are the costs of regulations that prevent a promising, but yet unknown, product from reaching consumers? Even regulations whose costs appear to be straightforward, such as corporate average fuel economy standards that restrict the fleet of vehicles produced, depend on assumptions about consumer preferences and behaviors that may not reflect American diversity. The Environmental

¹⁸ Susan E. Dudley prepared statement before the Senate Homeland Security and Government Affairs Committee, July 2011, available at: http://www.tsppa.gwu.edu/docs/20110720_testimony_dudley.pdf

¹⁹ Senator Mark Warner, prepared statement at *Federal Regulation: A Review of Legislative Proposals, Part I*. June 23, 2011, available at <http://www.hsgac.senate.gov/download/2011-06-23-warner-testimony>

²⁰ Susan E. Dudley, *Perpetuating Puffery: An Analysis of the Composition of OMB’s Reported Benefits of Regulation*, 47 J. BUSINESS ECONOMICS. (2012)

²¹ See statements of Senator Mark Warner and Senator Rob Portman at a Homeland Security and Government Affairs Committee hearing on June 23, 2011, available at <http://www.hsgac.senate.gov/hearings/federal-regulation-a-review-of-legislative-proposals-part-i>.

Protection Agency and Department of Transportation estimate that these rules will have large negative costs (even if benefits were zero), because, according to their calculations, the fuel savings consumers will derive from driving more fuel-efficient vehicles will outweigh the increased purchase price.²² Are such estimates are credible,²³ and how should negative costs be treated under a regulatory budget?

According to DeMuth:

Clearly, a workable budgeting system would have to rest on a practical compromise – some measure of “expenditures by firms, consumers, and third parties” that was narrow enough to facilitate general agreement in particular cases but not so narrow as to stimulate massive cost substitution strategies by the agencies.²⁴

How a budget or an offset requirement would affect agencies’ incentives for estimating costs is uncertain. In developing a baseline estimate of the costs of existing regulations, they may have incentives to overstate costs, particularly for regulations they may want to trade in exchange for new initiatives. In considering regulatory offsets, should ex ante estimates of costs be used, or ex post?

Congress would probably need to establish regulatory burden baselines in new authorizing legislation. Providing an entity outside of the executive branch (such as CBO or GAO) the resources and mandate to (1) estimate the regulatory costs associated with executing new legislation, and (2) evaluate and critique agency estimates of regulatory costs could be critical to the success of a regulatory budget or PAYGO.²⁵

Conclusion

Despite the analytical difficulties, a form of a regulatory budget has the potential to impose some needed discipline on regulatory agencies, generate a constructive debate on the real impacts of regulations, and ultimately lead to more cost-effective achievement of public priorities. Other countries, such as the United Kingdom,²⁶ Canada,²⁷ the Netherlands,²⁸ Australia²⁹ and

²² According to EPA & DOT, under the recently proposed standards for heavy-duty trucks, “the buyer of a new long-haul truck in 2027 would recoup the investment in fuel-efficient technology in less than two years through fuel savings.” Press Release: EPA, DOT PROPOSE GREENHOUSE GAS AND FUEL EFFICIENCY STANDARDS FOR HEAVY-DUTY TRUCKS. June 19, 2015.

²³ For a discussion of this question, see Brian F. Mannix and Susan E. Dudley, *The Limits of Irrationality as a Rationale for Regulation and Please Don't Regulate my Internalities*, J. POLICY ANALYSIS & MANAGEMENT, 34:3. Summer 2015.

²⁴ DeMuth, 39.

²⁵ Dudley HSGAC 2011 testimony.

²⁶ <https://www.gov.uk/government/collections/one-in-two-out-statement-of-new-regulation>

Portugal,³⁰ have addressed these issues and initiated programs that require new regulatory costs to be offset by removal of existing regulatory burdens.

While it will never be possible to estimate the real social costs of regulations with any precision, a regulatory budget or a more modest regulatory PAYGO should provide incentives for agencies, affected parties, academics, Congressional entities and non-governmental organizations to improve upon the rigor of regulatory impact estimates.

As President Carter's Economic Report of the President concluded in 1980:

The Nation must recognize that regulation to meet social goals competes for scarce resources with other national objectives. Priorities must be set to make certain that the first problems addressed are those in which regulations are likely to bring the greatest social benefits. Admittedly, this is an ideal that can never be perfectly realized, but tools like the regulatory budget may have to be developed if it is to be approached.³¹

²⁷ <https://www.tbs-sct.gc.ca/rtrap-parfa/0129bg-fi-eng.asp>

²⁸ <http://www.government.nl/issues/reducing-the-regulatory-burden/regulatory-burden-on-businesses>

²⁹ https://cuttingredtape.gov.au/sites/default/files/documents/australian_government_guide_regulation.pdf

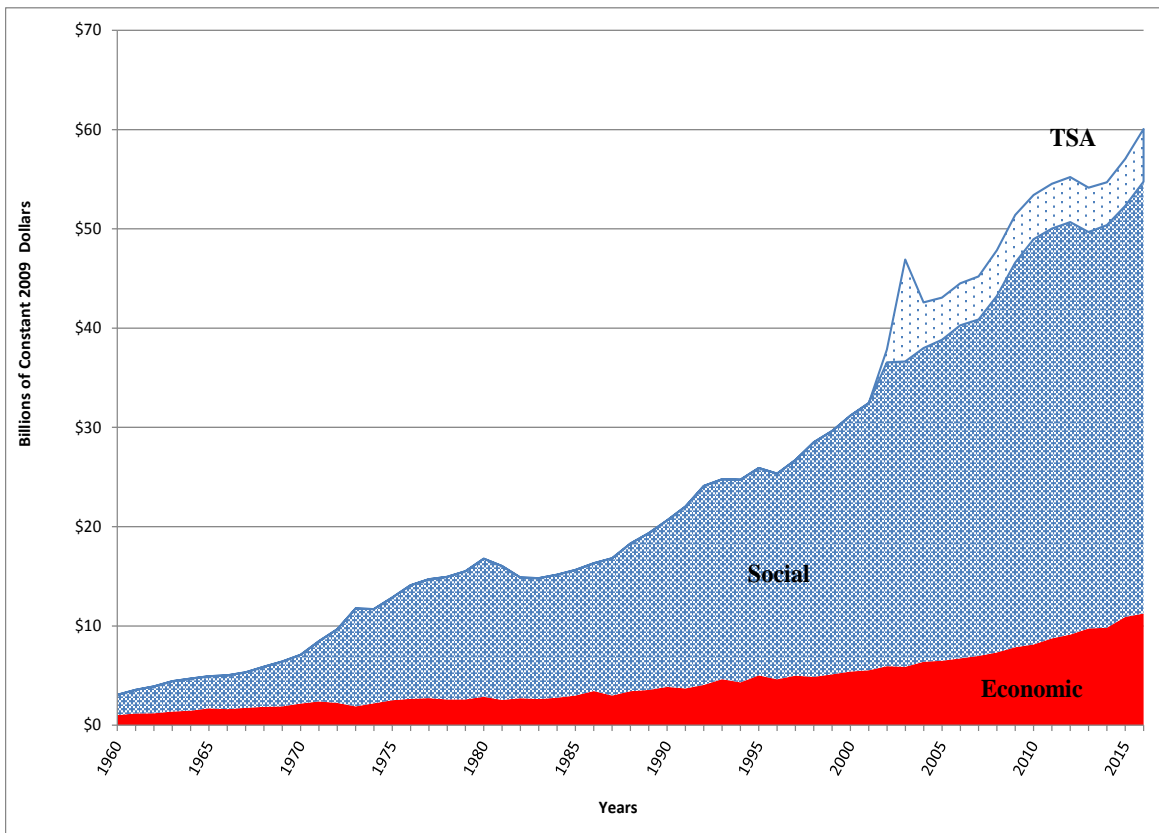
³⁰ European Commission, Group of High Level National Regulatory Experts (HLG-BR), Meeting of 6 May 2014. http://ec.europa.eu/smart-regulation/impact/docs/final_minutes_hlgbr_6_may_2014.pdf.

³¹ 1980 Economic Report of the President, 126.

Attachment: Measures of Regulatory Activity

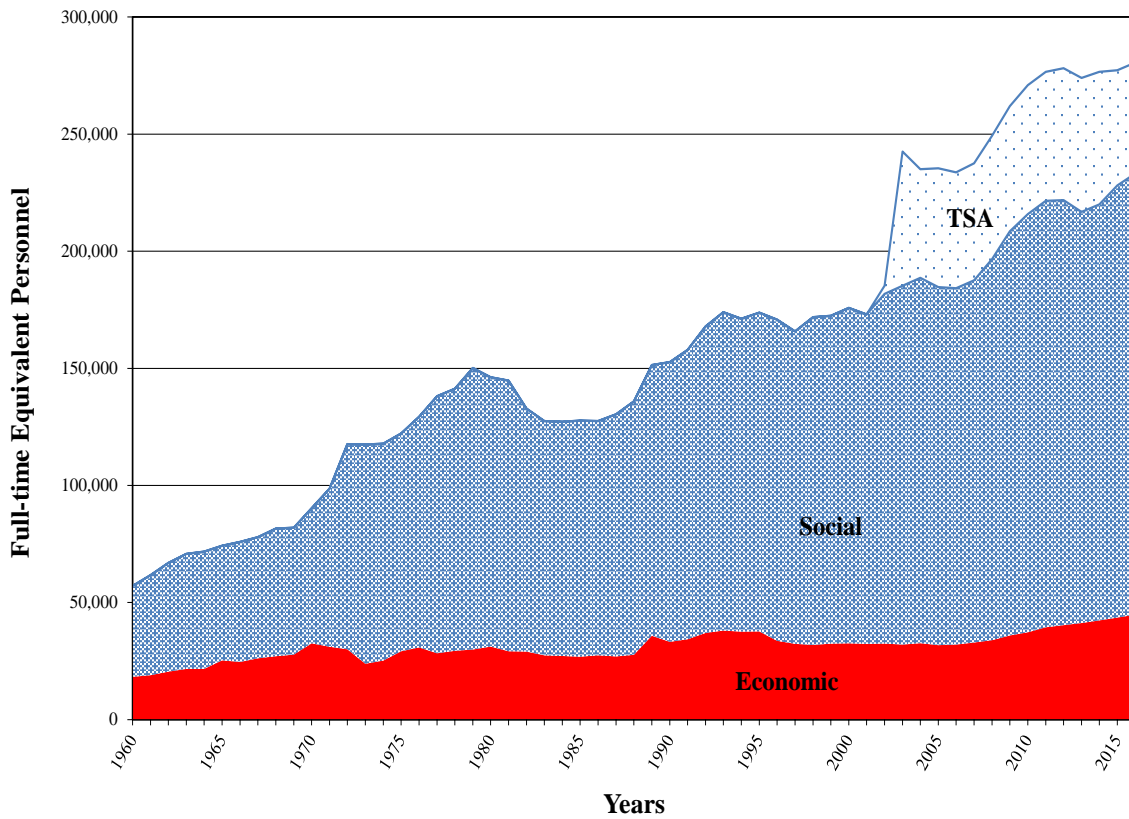
Unlike the fiscal budget, which tracks direct spending supported by taxes, there is no mechanism for keeping track of the off-budget spending generated through regulation. Thus, efforts to track regulatory activity over time often depend on proxies, such as the size of the budgets and staffing of regulatory agencies (Figures 1 and 2), the number of new regulations issued (Figure 3), the number of pages printed in the *Federal Register* (Figure 4), or the pages of federal regulatory code (Figure 5).

Figure 1
Budgetary Costs of Federal Regulation, Adjusted for Inflation



Source: Weidenbaum Center, Washington University and the George Washington University Regulatory Studies Center. Derived from the *Budget of the United States Government* and related documents, various fiscal years.

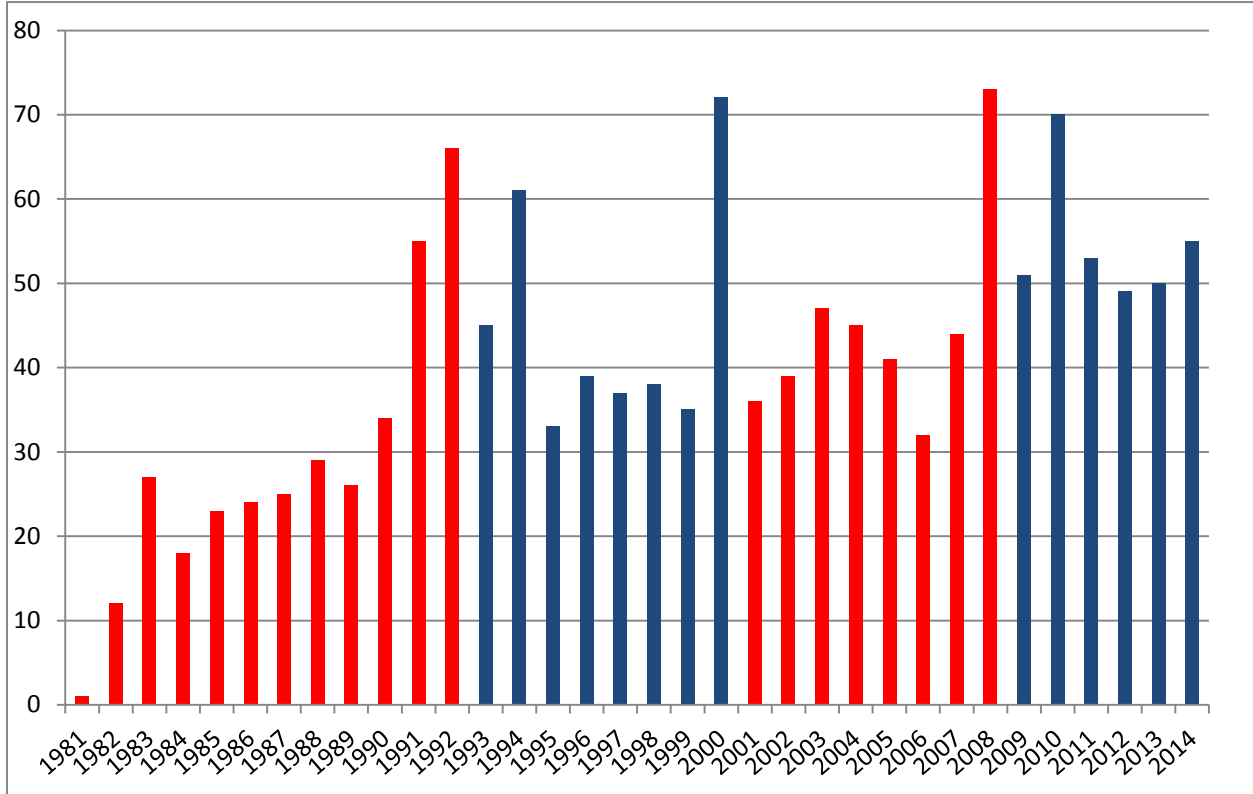
Figure 2
Staffing of Federal Regulatory Agencies



Source: Weidenbaum Center, Washington University and the George Washington University Regulatory Studies Center. Derived from the *Budget of the United States Government* and related documents, various fiscal years.

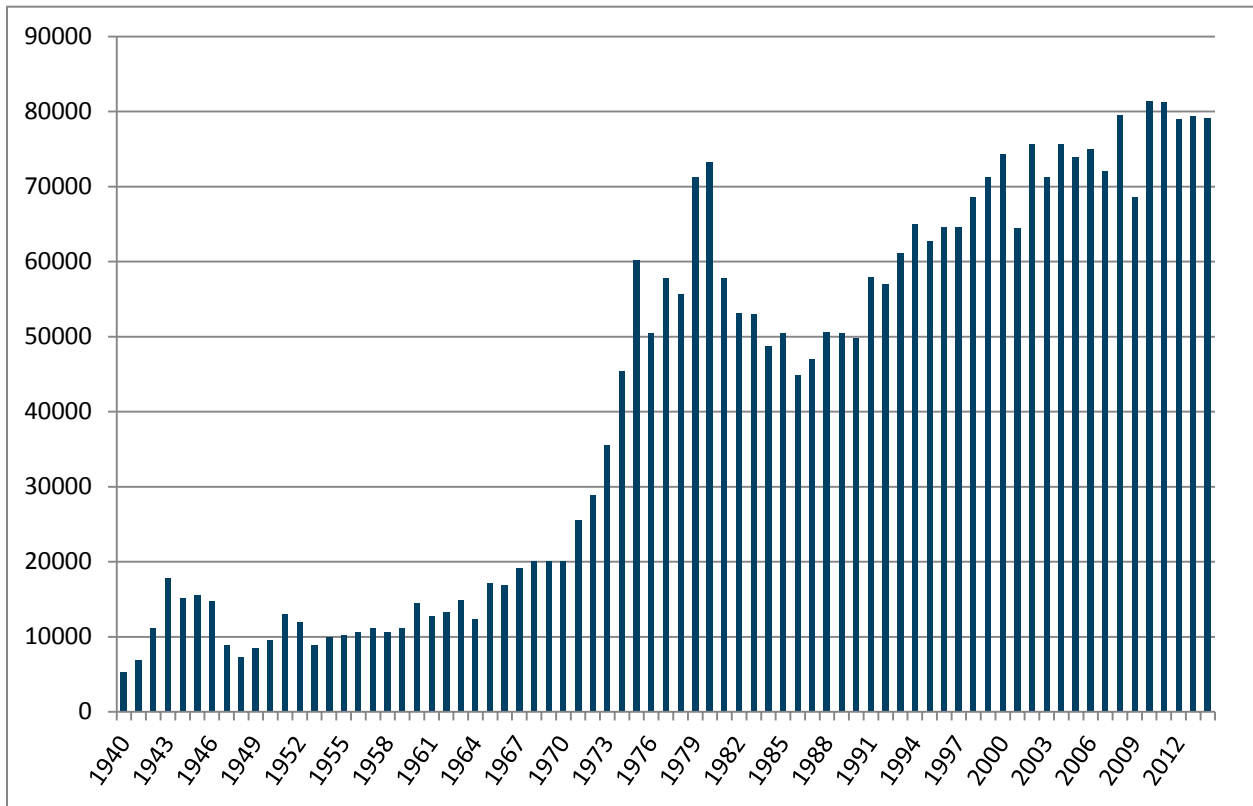
Figure 3

Number of Final Economically Significant Rules
Published by “Presidential Year”



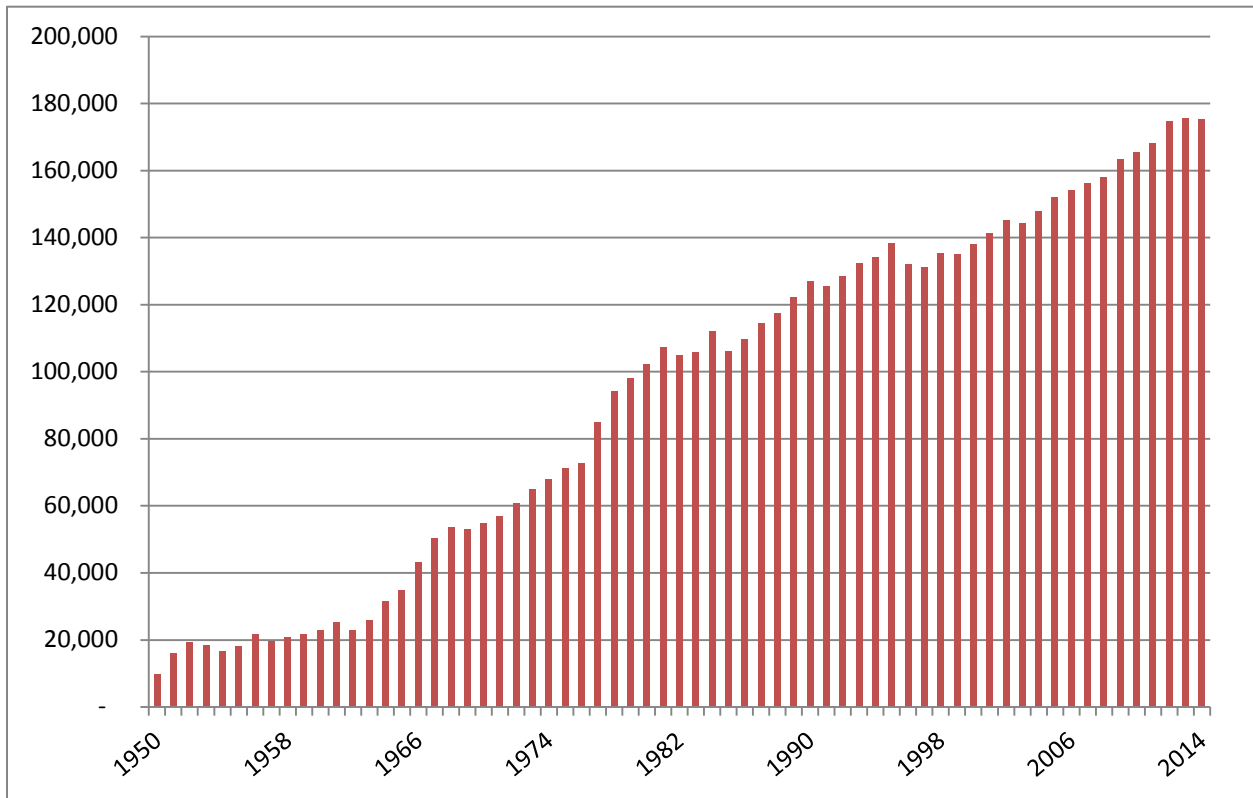
Source: RegInfo.gov: Number of economically significant regulations published between February 1 and January 30.

Figure 4
Federal Register Pages



Source: <https://www.federalregister.gov/uploads/2015/05/OFR-STATISTICS-CHARTS-ALL1-1-1-2014.xls>

Figure 5
Code of Federal Regulation Pages



Source: <https://www.federalregister.gov/uploads/2015/05/OFR-STATISTICS-CHARTS-ALL1-1-1-2014.xls>³²

³² RegData.org, a product of the Mercatus Center at George Mason University, provides more detailed information on regulatory requirements in the Code of Federal Regulations, including the number of “restrictions” by section.