Distributional Effects in Regulatory Impact Analysis

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In brief…

President Biden is right to demand more rigorous analysis of how regulatory benefits and costs are distributed. This commentary offers some principles for undertaking such analysis in a transparent way. GW Regulatory Studies Center scholars expect to offer further insights and ideas in the months ahead.

In his Modernizing Regulatory Review memorandum, President Biden reinforced longstanding requirements for regulatory impact analysis and placed renewed emphasis on understanding the distribution of regulatory benefits and costs. Specifically, he directed federal agencies to "propose procedures that take into account the distributional consequences of regulations, including as part of any quantitative or qualitative analysis of the costs and benefits of regulations, to ensure that regulatory initiatives appropriately benefit and do not inappropriately burden disadvantaged, vulnerable, or marginalized communities."

Understanding the distributional impacts of regulation is important, especially because well-organized and politically-connected groups have outsized influence in the regulatory process and can shape regulatory policy to benefit their interests at the expense of more diffuse interests. Further, unlike taxes, the costs of regulations are mostly regressive and their incidence is not transparent. Regulatory costs ultimately fall less on investors than on consumers and workers in the form of higher prices for goods and services, or lower wages and fewer opportunities. A few more dollars for groceries or utilities or a slightly smaller paycheck might not affect wealthier families, but they comprise a higher portion of low-income families' budgets, and reduce resources for other welfare enhancing activities, such as childcare, education, and healthcare.

The purpose of regulatory impact analysis is to inform policy makers of the benefits and costs of alternative regulatory approaches before a regulation is put into effect. It begins by identifying the problem to be solved, and justifying why a government solution is needed. Then, it considers viable alternative approaches that might address the problem, and evaluates the benefits and costs of those approaches, quantifying them and putting them in monetary terms when possible. Understanding the

incidence or allocation of those benefits & costs has long been an element of regulatory impact analysis, but distributional analysis hasn't been done in a rigorous way.

It's important to emphasize that regulatory analysis *informs* policy decisions, but it does not decide them. As such, assigning dollar values to every consequence of a regulatory alternative is not nearly as important as being *transparent* about what assumptions are made and how different scenarios might affect outcomes. Critics of regulatory impact analysis tend to characterize it as a technocratic tool in which decisions are made by subtracting monetary costs from monetary benefits. Not only is that an inaccurate characterization of the analysis itself, but it misrepresents how it is used. I have been involved in regulatory policy for decades and cannot identify a single time when quantitative benefit-cost analysis was the sole determinant of a regulatory decision.

One virtue of benefit-cost analysis is that it helps identify options that maximize net improvements in human welfare; these aren't always the right options to choose, but it is important for policymakers to know whether regulations are increasing or reducing welfare. For this reason, proposals to add "weights" to benefits or costs that accrue to different populations are not the right way to respond to President Biden's call. Rather than an objective and transparent presentation of information, weights effectively put a thumb on the scales, leaving policy makers and the public little reason to be confident that the thumb will be used to do good, rather than mischief. At the very least, weighting runs the risk of obfuscating empirical measurement in a manner that could favor political advocacy.

Instead, the distribution of regulatory impacts should be considered transparently and explicitly at every stage of the regulatory analysis. In identifying the compelling public need for a regulation, a good analysis should recognize the diversity among individuals, and ask what barriers prevent people with different preferences from making choices in their own interest. The analysis should explicitly and transparently examine which populations are likely to receive the benefits and which are likely to bear the costs. It should consider the effects of alternative regulatory (and non-regulatory) approaches on opportunities for employment, housing, education, etc. It should identify intergenerational effects. When valuing benefits and costs, serious thought must be given to whose "willingness to pay" should count, and whose discount rate should be applied.

Policy makers will have to take this information and make tough choices about how to compare policies that increase the size of the pie against those that divide a smaller pie more equally. But that's where those tough choices should be made—transparently and by politically accountable policy officials—not buried as factors in an analysis veiled from public debate and review.

None of this will be easy, but President Biden is right to demand more rigorous analysis of how regulatory benefits and costs are distributed. Over the next few months, GW Regulatory Studies Center scholars will be offering additional insights and ideas for ways to heed his call.