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Hearing Title: A Regulatory Budget and the U.S. Economy

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My name is John D. Graham. I am Dean of the Indiana University School of Public and Environmental Affairs (SPEA) in Bloomington and Indianapolis. SPEA is ranked #2 out of 266 Master's of Public Affairs programs in the United States and is best known for its outstanding programs in environmental science and policy, public budgeting and finance, public management, and policy analysis. During the George W. Bush administration (2001-2006), I served as Senate-confirmed administrator of the Office of Information and Regulatory Affairs (OIRA) in the White House Office of Management and Budget (OMB). Prior to my OMB service, I was a tenured Harvard Professor and founding Director of the Harvard Center for Risk Analysis. I earned my BA in politics and economics at Wake Forest University (1978), my MA in public affairs at Duke University (1980), and my Ph.D. in urban and public affairs at Carnegie-Mellon University (1983).

ORIGINS OF THE REGULATORY BUDGET

Our topic today is a promising reform of the federal regulatory system called the "regulatory budget." In the late 1970s, when the regulatory reform movement began to gather steam, reformers noticed an oddity about how the federal government operates. If the costs of a federal program are incurred within the federal budget, then those costs are subject to scrutiny in the normal appropriations process. But, if instead, federal agencies impose costs on the private sector and/or state/local governments, those costs are "off budget" and thus not considered a part of the federal budgetary process. Why, reformers asked, should \$1 billion in compliance costs on industry (investors, workers and consumers) be treated differently than \$1 billion in federal budgetary outlays that are typically financed by taxes?

Congress imposes strict annual limits on the magnitude of an agency's appropriations but there are no limits imposed on the unfunded mandates that federal agencies may impose on the private sector and state/local governments. In order to remove this odd discrepancy between budgetary and off-budget costs, the concept of a regulatory budget was developed.

Although there are several variants of the regulatory budget, the basic notion is that Congress should place annual limits on off-budget regulatory expenditures through a process similar to what is currently used to define appropriations for agencies. Step 1: agencies request a regulatory budget from OMB for the forthcoming fiscal year; Step 2: OMB, representing the president and the agencies, makes a regulatory budget request to Congress for the federal

government as a whole and for specific departments and programs. Step 3: Congress makes final decisions regarding the regulatory budget, first in committee actions and then in floor actions. The regulatory budget is defined in monetary units that represent the costs of regulation. Once a regulatory budget is enacted by Congress, the regulator is not permitted to impose regulatory burdens in excess of the authorized budget.

ADVANTAGES OF THE REGULATORY BUDGET

Advocates of the regulatory budget foresee several advantages compared to the current system.

First, the process of setting an annual regulatory budget would force the U.S. Congress to accept political accountability for regulatory costs, both the costs of individual agencies and programs and the overall magnitude of regulatory burdens on the economy. Under current procedures, Congress delegates significant regulatory authority to federal agencies, without having to accept any accountability for the regulatory burdens that result. Indeed, members of Congress may criticize the burdens associated with individual rules, knowing that they do not have to vote for any limitation on the level of regulatory burden for that particular year. Thus, from a standpoint of democratic accountability and transparency, the regulatory budget compels the US Congress and the President (through his or her budget request) to decide how much regulatory burden they are willing to authorize.

Second, the regulatory budget would induce a healthy competition between new regulatory proposals, since the budget may not be large enough to support all of the new proposals suggested by regulators. By setting priorities among worthy proposals, the regulators will work to advance the best proposals and drop the weaker ones. As a result, new regulations under a regulatory budget are expected to be more effective and more cost-effective than they would be without a regulatory budget.

Finally, budget limitation creates an incentive for agencies to streamline or eliminate wasteful regulations, since those savings can be used, under the regulatory budget, to pay for the cost of promising new regulations. Thus, if an agency is already at its cap on regulatory burden, the agency can move forward with a promising new regulation if the savings from the rescission or modernization of an existing rule are adequate to pay for the new rule.

Over the last twenty years, the regulatory budget has been -- and continues to be -- considered in the US, Canada, Australia, the UK, the Netherlands and Portugal. The UK has accumulated the most significant practical implementation experience.

MYTHS ABOUT A REGULATORY BUDGET.

1. *A regulatory budget is not technically feasible because the costs of regulations are unknown.*

The overall costs of the thousands of existing federal regulations have never been estimated and thus it would indeed be very difficult to establish a baseline for the current regulatory budget. However, a regulatory budget can be defined in terms of new ("incremental") regulatory burdens for the next year, without any need to estimate the overall size of current regulatory

burdens. The costs of economically significant new rules are already being estimated in the OMB regulatory review process mandated by presidential executive order. Those estimates -- and the agency procedures that produce them -- provide clear evidence that it is technically feasible to estimate the costs of new regulations.

2. A regulatory budget is unnecessary because the president, through OMB review, already subjects economically significant rulemakings to a cost-benefit test.

While the president does accept some political accountability under current executive order procedures, the cost-benefit reviews performed by OIRA/OMB are not shared with Congress, the Congress does not have any expertise in cost-benefit analysis, and the Congress does not establish any budget for regulatory costs on a regular basis. Moreover, the tenacity of OMB's review process varies from administration to administration (and even from rule to rule), depending on how committed a president is to the rigors of cost-benefit analysis. In some cases, agencies and OMB do not consider costs and benefits because of statutory preclusions or because of public opinion or interest-group pressures. A regulatory budget would constrain burdens in situations where the executive branch is disinclined to constrain burdens.

3. A regulatory budget looks only at the burdens of regulation, and thus ignores benefits.

The fact that the regulatory budget is defined as a cap on regulatory costs does not mean that regulatory benefits play no role in the process. As is the case with the normal budgetary process, agencies advance whatever case they wish for benefits (whether it be quantitative or non-quantitative, monetary or non-monetary, economic or environmental, or whatever) when making the case for their desired regulatory expenditure cap. If the case for benefits is strong, OMB (or Congress) might be inclined to set a higher regulatory budget; if the case for benefits is weak, OMB (or Congress) might lower the proposed regulatory budget.

Conclusion

In my opinion, the concept of a regulatory budget is appealing. The key question is how to move the idea from theory to reality. My suggestion is a congressionally-designed pilot project where three regulatory agencies (e.g., EPA, DOT and SEC) work under a regulatory budget for a 3-year to 5-year period. If the pilot is successful, the pilot could be extended to the entire federal government.

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