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A Future for Federal Regulatory Budgeting?

For decades, a strong case has been made for comprehensive reform of the U.S. federal government's regulatory processes (for early contributions, see Weidenbaum & DeFina, 1978; Lave, 1981; Breyer, 1982; Harrison & Portney, 1983; Litan & Nordhaus, 1983; Viscusi, 1992; Breyer, 1993; Sunstein, 1996; Graham, 1996, 1997). Establishment of centralized Office of Management and Budget (OMB) oversight through the Office of Information and Regulatory Affairs (OIRA) was an important achievement, but Congress has not yet passed comprehensive regulatory reform legislation.

Jim Tozzi has been a central player in the case for reform, based on his roles in the establishment of OMB's OIRA in the early 1980s and his subsequent leadership of the influential Center for Regulatory Effectiveness. Drawing from this wealth of experience, Tozzi has penned "Office of Information and Regulatory Affairs: Past, Present, and Future" (2019). I am honored to have been asked to comment on this thoughtful piece of scholarship.

Tozzi starts from the premise that a central problem with federal regulation is the uncontrolled growth of the cumulative costs of federal regulation. He emphasizes the need for a national regulatory budgeting system, one that is modeled after the standard budgetary processes for governmental appropriations. He envisions a regulatory budget that is determined each year by the Congress in collaboration with OMB and the agencies. Because an annual regulatory budget would cap regulatory costs (at each agency and in total), it is seen as a solution to the growth in cumulative regulatory costs.

Tozzi recognizes that the regulatory budgeting system imposed by the Trump administration via executive order does not enjoy broad bipartisan support. Most agencies have been assigned negative regulatory budgets, which – if implemented faithfully – requires a net reduction in regulatory costs at each agency each year. Many agencies are trying to deregulate, but the administration has a poor track record of defending deregulation in federal courts (Graham & Belton, 2019). Moreover, it is not obvious what happens if an agency fails to meet their negative cost cap, as apparently happened at some agencies in 2018. One also wonders why there is not any major agency that has made a persuasive case for a significant increase in

The author appreciates constructive comments on an earlier draft from Keith Belton, Art Fraas, and Kerry Krutilla, although they do not necessarily share the views expressed here.

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their regulatory budget. Trump's system is also supplemented and confused by the "two-for-one" gimmick, a separate requirement that two regulations be rescinded for each new one that is adopted. The number of regulations per se is widely regarded as an unimportant metric for serious regulatory reform. For a variety of reasons, it seems unlikely that the Trump approach to regulatory budgeting will survive the Trump presidency (Belton *et al.*, 2017; Graham & Belton, 2019).

Tozzi argues that a more promising approach to regulatory budgeting was proposed (although not enacted) in the Jimmy Carter era. Indeed, it was never really proposed by the Carter administration, although it had bipartisan interest in Congress during Carter's term of office. The Carter-era approach would involve Congress as well as OMB and the agencies, and the approach need not be saddled with the "two-for-one" gimmick (my word) that symbolizes Trump's commitment to deregulation (Belton *et al.*, 2017; Graham & Belton, 2019).

Why impose a cost cap on agencies? When an agency's incremental regulatory costs are capped, the theory is that agencies will give priority to new regulatory initiatives that are affordable within the cap and have the highest societal return per dollar of imposed cost. The budgetary limitation will also provide each agency an incentive to do the tedious work of scrutinizing existing regulations and finding some that can be made less burdensome or more cost-effective, because those savings create room under the agency's cap for promising initiatives (Belton *et al.*, 2017). As long as the executive branch's total appropriations are constrained by Congress but total regulatory costs are unconstrained by Congress, an agency will have an incentive to shift program development from budgeted activities to off-budget activities like regulation. As a result, Congress is currently imposing no coherent constraint on the overall size of the federal government's influence on the economy, a role that OMB could play if Congress would enact regulatory budgeting. I agree with Tozzi's central point that regulatory budgeting, in order to have maximum impact and longevity, must be embraced and implemented by the Congress.

Whether Congress has any near-term interest in adopting a regulatory budget is certainly doubtful. The current bout of partisan polarization in Congress has stifled most legislative activity. More generally, the members of Congress may have an electoral incentive to grant broad regulatory authority to agencies without accepting any political accountability for the specific rules that are issued or the cumulative costs of the regulatory state. In the future, a window of opportunity for regulatory budgeting could arise if the Congress decides to consider ways to resolve the fiscal challenges facing the country.

There are, however, some weaknesses in the case for the regulatory budgeting. Those weaknesses need to be addressed in the academic literature and discussed in bipartisan forums. I am pleased that Tozzi acknowledges some of the weaknesses and calls for bipartisan deliberation. Here are some of the weaknesses that I believe need to be considered.

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First, it is not obvious that a regulatory budgeting system will place much effective constraint on the cumulative cost of federal regulation. If Congress wishes to allow a large amount of growth in federal regulation, the budgetary limitations imposed on agencies can be set at very high, permissive levels, thereby facilitating continued growth in the cumulative costs of federal regulation. Congress can also exempt huge swaths of regulation from the budget, thereby reducing the effective discipline. In the appropriations process, Congress has demonstrated for decades a willingness to ignore fiscal discipline and allow federal spending and the overall size of the federal debt to balloon (Lee *et al.*, 2013). Proponents of regulatory budgeting need to explain why Congress would be any more disciplined with regulatory budgeting than they are with federal appropriations.

Second, the international experience with regulatory budgeting is not similar to the comprehensive regulatory budgeting discussed during the Carter era and favored by Tozzi. European systems of regulatory budgeting tend to focus exclusively on the "administrative" costs of regulation (e.g., paperwork burdens and "red tape"), which are typically a small share of the total costs of regulation. The largest share of regulatory costs, the compliance costs shouldered by industry, are typically ignored in European budgetary systems. Administrative costs are already addressed in the U.S. system, however imperfectly, by OMB-approval procedures under the Paperwork Reduction Act (PRA) of 1980. If administrative costs are the central concern (although I doubt this is the case in the United States), it may make more sense to modernize the PRA than to enact regulatory budgeting. The key point is that there is virtually no international experience with the comprehensive type of regulatory budgeting that Tozzi is favoring.

Third, the premise that the cumulative costs of the federal regulatory system are a problem – either for the performance of the U.S. economy or as a threat to human liberty – is not shared on a bipartisan basis as Tozzi presumes it is. Concerns about the cumulative cost of federal regulation are expressed primarily by fiscally conservative think tanks, some business groups and libertarians (e.g., see Weidenbaum & DeFina, 1978; Coffey *et al.*, 2016; Crain & Crain, 2014; Crews, 2017).

There is a strong, multi-decade literature, authored by scholars linked to both political parties, demonstrating regulatory inefficiency, where inefficiency is characterized by a somewhat chaotic mix of under-regulation and over-regulation (for early contributions, see Viscusi, 1992; Breyer, 1993; Graham, 1996, 1997; Sunstein, 2002*a*, *b*). Regulatory inefficiency seems to call for a stronger focus on benefit-cost analysis or cost-effectiveness analysis rather than regulatory budgeting per se. Proponents of regulatory budgeting need to make the case that the phenomenon of under-regulation will be solved – or at least not exacerbated – by budgeting, in order for budgeting to attract more bipartisan support. Alternatively, regulatory budgeting needs to be married with other reforms aimed at curing under-regulation.

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Reactions to the Trump administration's deregulation agenda illustrate the dilemma. Strong concerns have been raised that the administration is so focused on deregulation that agency officials are ignoring the benefits of regulation and refusing to consider new regulations, even when they have a solid benefit-cost justification (Linn and Krupnick, 2017; Graham & Belton, 2019). Indeed, since the Trump administration has such little interest in new regulations (excepting campaign priorities such as restraints on immigration and trade), the administration's two-for-one and budgeting reforms have not created much incentive for agencies to repeal or streamline existing regulations that are ineffective or wasteful. A regulatory budgeting system would have much more impact on retrospective review of regulations at agencies in an administration that has substantial ambitions for new regulations but also recognizes the compelling need to modernize the existing stock of regulations (Belton *et al.*, 2017). Given how costly, sensitive, and time consuming it is to perform meaningful retrospective reviews, agencies will not engage in the activity unless they have a powerful incentive to do so.

Fourth, regulatory budgets are a weak instrument to control the capital costs of existing regulations, since capital costs are typically incurred soon after a regulation takes effect. For capital costs, there is no substitute for effective ex ante evaluation of regulatory proposals. Finally, there is a widespread misperception that regulatory budgeting focuses only on costs, and the benefits of regulation have no role in budgetary processes. The misperception is unfortunately espoused by a wide range of academic economists who have historically been reliable proponents of efforts to modernize federal regulation. Well-respected economists affiliated with Resources for the Future have espoused this view (e.g., see Krupnick, 2017).

I describe this as a misperception because (*a*) regulatory budgeting is modeled after appropriations processes and (*b*) benefits of federal programs, although they are not always framed in economic terms, play an important role in appropriations processes. In fact, when agencies make their case to OMB for including new spending in the President's annual budgetary request, OMB evaluates the strength of the evidence-base case for additional spending. This is a key responsibility of an OMB budget examiner, one of the most important posts in the federal career civil service! Those benefits may be framed as program effectiveness against statutory goals, progress against accepted performance metrics or other budgetary constructs, but appropriations processes are designed do consider what good a budgetary increase would accomplish. The OMB-agency budgeting process is surely not perfect, but no serious student of the appropriations process would claim that program benefits are ignored in the process.

My hypothesis is that professional economists are inclined to harbor this misperception about regulatory budgeting because they are generally mistrustful of the Trump administration (not an unreasonable sentiment) and/or because they have little knowledge of budgetary processes. The latter point requires a bit of elaboration.

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Most academic economists who teach students in economics have little or no formal training in budgetary processes and little hands-on experience in governmental budgeting or public administration. For readers who are surprised about this observation, I encourage them to examine the common textbooks in public finance used in U.S. economics departments. Those textbooks are typically strong on topics such as public goods and externalities, welfare economics, social insurance and income maintenance, and tax analysis and revenue systems. They are typically sparse with regard to the practical aspects of how the budget of a government agency is determined and how a case is made for a budgetary increase (see, for example, the superb text authored by Rosen & Gayer, 2010). I am referring to public-administration processes that occur at the state and local levels of government, in the federal government and in governments around the world. There are superb textbooks in "public budgeting," but doctoral students in economics are not typically required to take coursework in budgeting (Lee *et al.*, 2013).

Even in the White House, I was struck – during my service as OIRA administrator to President George W Bush (2001-2006) – by how unevenly connected the White House Council of Economic Advisors (CEA) was to OMB's annual process of preparing the President's budgetary request of Congress. Indeed, I often felt that CEA played a greater advisory role in the OIRA-led regulatory side of OMB than on the budget side, and I deeply appreciated the assistance from CEA's members and staff in OIRA activities (Graham, 2007, 2008).

I am not arguing that standard budgetary processes incorporate cost-benefit analysis as defined by the field of welfare economics. I am arguing that evidence-based cases are used in budgetary processes, and the key evidence to support a budgetary increase is often related to what tangible societal gains the budgetary increase would facilitate for a program's effectiveness or performance (e.g., more poor children receiving dental care or more vulnerable senior citizens served by meals on wheels). This is the crucial consideration of "benefits" that OMB budget examiners look for, and public administration professionals are trained to look for this evidence and take it seriously, rather than simply assume that all government spending is beneficial or worthless. A regulatory budget would operate similarly except that agencies would typically frame benefits as the field of welfare economics recommends that they be framed unless cost-benefit analysis is not feasible.

Academic economists do have a point that a strong system of cost-benefit review of new and existing regulations reduces the need for a regulatory budgeting system. However, there are well-recognized weaknesses in the cost-benefit system currently monitored by OIRA at OMB, so it would be a mistake to think there is no need to consider complementary reforms that might provide more fiscal, analytic, and evidence-based discipline to federal rulemaking (for some nonbudgetary reforms worthy of consideration, see Breyer, 1993; Graham, 1997, 2008; Fischbeck & Farrow, 2001;

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Harrington *et al.*, 2009; Sunstein, 2013, 2014; Graham & Broughel, 2014; Graham & Liu, 2014; Coglianese, 2017; Noe & Graham, 2019). Nonetheless, I believe that regulatory budgeting is one of a portfolio of reforms that has some promise, if it is embraced by Congress with bipartisan support. Unfortunately, the lack of widespread support for regulatory budgeting among academic economists is an important obstacle for proponents of regulatory budgeting.

In summary, Jim Tozzi has for decades been a determined promoter of a more analytical and transparent federal rulemaking process. I was pleased to see that he remains intellectually active in making the case for reform, as he has a wealth of valuable experience to bring to the table. I share his view that more work needs to be done to build bipartisan support for a legislative approach to regulatory budgeting.

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