Mercatus Reports

The **Mercatus Center** at George Mason University is an education, research, and outreach organization that works with scholars, policy experts, and government officials to bridge academic theory and real-world practice. The center's Regulatory Studies Program works within the university setting to improve the state of knowledge and debate about regulations and their impact on society. More information about the center can be found on the Web at www.mercatus.org or by contacting Jennifer Zombone at jzambone@mason.gmu.edu.

Ozone Air Quality Standards

STATUS: Comment period pending.

On May 14, 1999, the U.S. Court of Appeals, D.C. Circuit, remanded to the Environmental Protection Agency (EPA) its national ambient air quality standards for ozone. The court found that, in preparing the rule, EPA had illegally failed to consider such factors as the beneficial health effects of ozone in shielding the public from the "harmful effects of the sun's ultraviolet rays."

EPA has now proposed a response to the remand. The Office of Information and Regulatory Affairs (OIRA) concluded its review of the proposal with changes in October, and the response is to be published in the *Federal Register*.

Tanker Vessel Monitoring Devices

STATUS: Analyzing public comment.

In response to a December 2000 decision by the U.S. Court of Appeals, D.C. Circuit, the U.S. Coast Guard has proposed a rule requiring oil tankers to install tank-level or pressure monitoring devices to alert vessel operators of a leak. Attempting to comply with the court's decision and the mandate of Section 4110 of the Oil Pollution Act, the Coast Guard proposed eight different options for the rule, with total cost for implementation ranging from $64 million to $211 million, depending on the option.

In accordance with former president Bill Clinton's Executive Order 12866, OIRA conducted a benefit-cost analysis of the different options. OIRA found that all eight would fail to deliver benefits that offset the cost. For example, OIRA noted in its "post-review" letter to the Coast Guard that "the most effective option would generate a net cost to society (cost in excess of benefits) of $12 to $64 million annually."

The Coast Guard itself admits that the rule is not cost-effective and asked for public comments, which were due to the agency at the end of November. Because of the constraints of the court's decision, the only remedy for the situation may be legislative relief.

Non-Road Vehicle Emissions

STATUS: Analyzing public comment.

EPA has proposed a new rule regulating the emissions of several types of non-road vehicle engines, including spark-ignition engines with power over 19kW, recreational marine compression ignition engines, and engines used in off-road recreational vehicles. EPA argues that such regulation is necessary because exhaust from the engines contributes to an area's nonattainment of carbon monoxide, particulate matter, and ozone standards. The agency also claims that the rule is necessary to improve visibility in national and state parks.

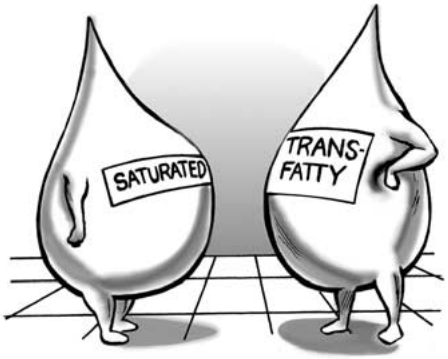
OIRA reviewed the proposed rule and concluded that EPA's analysis is insufficient to support the proposed regulation. In a post-review letter, OIRA stated that EPA failed to provide an adequate benefit-cost analysis of the rule, failed to evaluate alternatives, and failed to quantify the rule's environmental benefits. OIRA allowed the proposal to go out for public comment, but stated in the letter that it expects "improved analyses to be completed prior to submission of the final rule."

Trans-Fatty Acids Labeling

STATUS: OIRA prompt for action.

In November of 1999, the Food and Drug Administration (FDA) proposed requiring the inclusion of trans-fatty acid content on food labels. The FDA based that decision on a series of studies showing that the consumption of trans-fatty acids leads to an increased risk of coronary heart disease. Since that time, no final rule has been proposed.

On September 18 of this year, OIRA



ILLUSTRATIONS BY KEVIN TUMA

sent a prompt letter to the Department of Health and Human Services urging it and the FDA to "consider giving greater priority" to releasing a final rule. OIRA cited the "growing body of scientific evidence" showing the link with heart disease, as well as estimates of the costs and benefits of such a rule that the FDA included in its preliminary Regulatory Impact Analysis.

Although there is considerable support for regulation that increases consumer information about trans-fatty acid content, there is debate over how that information should be displayed on the food label. The original FDA-proposed rule would require the trans-fat content be included as a component of the saturated fat total, indicating to the consumer that trans-fats are a variety of saturated fat. But that is incorrect; trans-fats are not saturated fats chemically, and FDA does not conclude that they are the same as saturated fats in their biological effects. According to some critics of the FDA's proposed rule, giving consumers the impression that trans-fats are exactly like saturated fats is misleading and could endanger some consumers' health.

Automated External Defibrillators

STATUS: OIRA prompt for action.

Last May, the Department of Health and Human Services and the General Services Administration developed guidelines for public access to Automated External Defibrillators (AEDs) in public buildings, pursuant to a May 2000 Clinton memorandum. Additionally, the Department of Transportation issued a final rule in April that instructed air carriers to put AEDs on all flights that require at least one flight attendant.

Following those actions, OIRA sent a prompt letter to the Department of Labor, urging the Occupation Safety and Health Administration (OSHA) to formulate a rule mandating the introduction of AEDs into all workplaces, public and private. The OIRA letter cited several articles claiming that AEDs are effective in increasing the survival rate of heart attack victims. Furthermore, OIRA argued that preliminary evidence shows the presence of AEDs in the workplace would be a cost-effective measure.

OIRA has given OSHA 60 days to respond to the letter.

Mercatus Reports: IN DEPTH

Bush's Rejuvenated OIRA

By Susan E. Dudley
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Beginning with the Nixon administration, every U.S. president has maintained, in one form or another, a centralized mechanism for executive branch oversight of regulations issued by federal agencies. Under Ronald Reagan, the Office of Information and Regulatory Affairs (OIRA) — a division of the Office of Management and Budget — held the lead role in carrying out that oversight. In accordance with Reagan's Executive Order 12291, OIRA asked agencies to identify a market failure before considering regulatory action. After the failure was identified, OIRA emphasized the philosophy that regulations should be adopted only after the completion of a benefit-cost analysis of available alternatives, and directed agencies to select the regulatory approach that maximizes net benefits to society unless constrained by law.

In 1993, Bill Clinton revoked E.O. 12291 and replaced it with E.O. 12866. The new order expressed the same philosophy as its Reagan predecessor, but the execution changed significantly. Under Clinton, the role of OIRA shifted from a substantive reviewer of regulations to a coordinator with little authority to hold agencies accountable to the principles espoused in E.O. 12866.

Reasserting its role OIRA now appears to be making a comeback under the new administration. Despite some criticism from Capitol Hill and special interest groups, President George W. Bush appointed John Graham, the former head of Harvard University's Center for Risk Analysis, as administrator of OIRA. Graham subsequently issued a memorandum to the President's Management Council, comprising deputies from more than 20 federal departments and agencies, that reasserted OIRA's role in overseeing the adoption of new regulation.

The September 20 memo noted that the "President's Chief of Staff, Andrew H. Card, Jr., has directed [OIRA] to work with the agencies to implement vigorously the principles and procedures in E.O. 12866 until a modified or new Executive order is issued." What is more, Graham's memorandum included an attachment, "OMB Regulatory Review: Principles and Procedures," that describes how OIRA will carry out its review and what it expects of regulatory agencies.

Emphasis on analysis The memorandum highlights and reinforces key aspects of Clinton's E.O. 12866, reflecting Graham's interest and expertise in benefit-cost analysis and risk assessment. It emphasizes the importance of Regulatory Impact Analyses (RIAs) and the principle that "in choosing among alternative regulatory approaches, agencies should select those approaches that maximize net benefits." It explicitly encourages agencies to have draft RIAs "reviewed by agency econo-

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mists, engineers, and scientists, as well as by agency attorneys, prior to submission to OIRA." Reminding agencies of their statutory responsibilities under the Congressional Review Act as well as E.O. 12866, the memorandum advises agencies that RIAs are required "regardless of the extent to which an agency is permitted by law to consider risks, costs, or benefits in issuing a regulation."

The memorandum also stresses the importance of basing regulatory action on "objective, realistic, and scientifically balanced" assessments of risk or environmental hazard. It cites language from the 1996 amendments to the Safe Drinking Water Act, and "recommends that each agency consider adopting or adapting these basic Congressional standards for judging the quality of scientific information about risk it uses and disseminates." The memorandum also "recommends that agencies subject RIAs and supporting technical documents to independent, external peer review by qualified specialists," and provides guidance on identifying appropriate peer reviewers and ensuring their independence.

JOHN GRAHAM

A benefit-cost analysis expert, Graham has instructed regulatory agencies to "select those approaches that maximize net benefits."

Procedural expectations The Graham memorandum describes the process by which OIRA will conduct its reviews, emphasizing that agencies may issue a significant regulatory action only after receiving notification from OIRA that it has concluded its examination. Graham encourages agencies, upon publishing a proposed rule, to provide at least 60 days for public comment.

While "in the case of a rule subject to statutory or judicial deadlines, OMB will not unilaterally delay publication beyond the deadline," the memorandum does not absolve agencies of their responsibilities in such cases. Instead, "the agency must submit the rule to OIRA in a timely fashion, so as to provide a meaningful opportunity for Executive Office review," or "where time frames are particularly tight due to a statutory or judicial deadline, agencies should consider submitting the draft rule to OIRA for preliminary review at the same time that it is being reviewed by senior agency policymakers."

The memorandum describes procedures by which OIRA officials will meet with outside parties regarding a rule under review. The procedures are consistent with those described in a 1986 memo by former OIRA administrator Wendy L. Gramm to ensure openness and transparency in the review process, and to those followed at OIRA during the 1990s under E.O. 12866.

Reconsideration Significantly, the memorandum highlights a procedure that was not often used during the last eight years: the authority of OIRA to return a rule to an agency for reconsideration. Graham writes, "Such a return may occur if the quality of the agency's analyses is inadequate, if the regulatory standards adopted are not justified by the analyses, if the rule is not consistent with the regulatory principles stated in the Order or with the President's policies and priorities, or if the rule is not compatible with other Executive orders or statutes."

Indeed, by October 3, OIRA had used E.O. 12866 to return 16 rules to agencies for reconsideration, compared to the nine rules returned by OIRA during the first eight years of the executive order. Graham also has sent two "post-review" letters to agencies upon concluding OIRA review of a regulation. Unlike a return letter, the post-review letters allow the agency to proceed to issue the proposed regulation, but they do critique the options proposed and/or the regulatory analysis supporting the draft proposal.

Prompt letters Graham's memorandum also introduces a new mechanism — the "prompt letter" — that informs an agency of "an issue that OMB believes is worthy of agency priority." Prompt letters could recommend "that an agency explore a promising regulatory issue for agency action, accelerate its efforts on an ongoing regulatory matter, or consider rescinding or modifying an existing rule." The memorandum requests that agencies respond to "prompt" letters, normally within 30 days. On September 18, OIRA issued two such prompt letters. One encouraged the Food and Drug Administration to issue a final rule requiring a change in the food labeling requirements for trans-fatty acids, and another requested that the Occupational Safety and Health Administration make the requirement that automated external defibrillators be placed in the workplace a priority, based on preliminary cost-effectiveness analysis done by OIRA staff.

There is no indication yet of when we might see a new executive order on regulations, and it is too early to pass judgment on the new administration's regulatory record. However, policy documents suggest that we are likely to see more rigorous executive oversight and a greater emphasis on ensuring regulations provide benefits greater than costs. Furthermore, Bush's new oversight mechanisms ensure that the process will be transparent and the record of decisions will be available to compare to the economic principles that Bush, like his predecessors, has endorsed. R

PHOTO COURTESY OF THE WHITE HOUSE

Measuring Hidden Taxes

By Joseph M. Johnson
The Mercatus Center

The U.S. Small Business Administration recently released a study estimating that federal regulations cost Americans $843 billion a year. The study, authored by George Mason University economist Mark Crain and Rochester Institute of Technology business school dean Thomas Hopkins, further breaks down the total cost of regulation to reflect the cost borne by each American household — a total of about $8,614 per year. That is a hefty sum, even when compared to the $19,613 average household share of federal tax revenues.

An important difference between the average household's federal tax bill and its regulatory tax bill bears scrutiny. Taxes are relatively transparent; they are reflected on the pay stubs of most workers and in the annual federal budget of the United States. But the regulatory tab is paid through reduced wages and salaries, lower returns on investment, and higher prices for goods and services. Regulations are, therefore, a hidden tax on American businesses, employees, and families.

One fact that makes the $843 billion regulatory tax bill even more disturbing is that it likely is an underestimate of the true regulatory burden. Again, unlike standard federal taxes, regulatory taxes are not collected by the Internal Revenue Service and placed in the government coffers in Washington, D.C. to be scrutinized and counted by federal accountants. Instead, regulatory taxes are estimated by those interested in understanding how much federal rules really cost, chiefly by looking at their effects or by guessing how much affected parties will have to spend to comply *ex ante*. Generally, that is determined by undertaking the grueling task of building estimates of the thousands of federal regulations, one by one. Thus, it is not surprising that we still do not know the total cost of all federal regulations.

Improving research Fortunately, progress is being made toward the goal of developing an itemized account of all federal regulations — a "regulatory budget" — by continually increasing the number of regulations for which costs have been estimated. In a recent Mercatus Center paper, I examined available information on federal rules regulating the workplace. I specifically was interested in the rules resulting from 25 statutes and executive orders relating to safety and health, employee benefits, wage standards, and civil rights, among other areas. Based on that research, I conservatively estimated the cost of workplace regulations at $91 billion annually. Crain and Hopkins used that research in their total estimate of regulatory costs, making their study the first to reflect workplace regulations as a separate category of regulatory costs.

My research brought to light the importance of continuing research into the costs and benefits of federal regulation. At present, any endeavor to understand regulatory costs is hindered by the scarcity of data available on many important regulations; that is why I say that my estimate of $91 billion per year is a conservative one. For instance, the costs of occupational safety and health regulations make up about half of that total ($48 billion) and are reasonably well researched. But the costs resulting from regulations based on civil rights legislation, such as the Americans with Disabilities Act, are less understood and likely are underrepresented in my total. (I estimated civil rights regulations to cost $6.5 billion annually when the cost of litigation is included.)

Bearing the burden While smaller in absolute magnitude than the costs associated with environmental, economic, and tax compliance regulations, workplace regulations nevertheless represent a significant burden on all Americans. Comprising roughly 11 percent of the $843 billion annual regulatory budget, workplace regulations place the most serious burdens on American workers.

Yet, to the casual observer, the assumption is that rich corporations pay the costs imposed by workplace regulations. To be certain, corporate shareholders feel the sting of higher costs and lower productivity due to regulation. Consumers, most often members of the workforce themselves, also tend to pay higher prices for goods when regulatory costs increase. Ultimately, however, it is the worker who pays, in the form of lower compensation — or even unemployment in some cases — when workplace regulations directly increase the cost of labor. Of course, regulations also convey benefits to some workers, but more often than not the cost of benefits mandated by workplace regulations is greater than most would be willing to pay without the regulatory impetus.

Considered more broadly, regulations affect everyone, and we all bear some of the costs. The annual regulatory budget of the U.S. government is becoming more clear as researchers continue to examine regulatory costs and as estimates become more refined. Currently, the benchmark stands at $843 billion per year, but that figure surely will grow as new regulations are promulgated and old regulations previously unexamined are added to the total.

The cost estimates are not merely figures that affect the balance sheets and income statements of corporate America. They increasingly are being recognized as hidden taxes that affect the paycheck of every American, even if they do not appear among the lines of federal withholding on every American's pay stub. R

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