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AEI-BROOKINGS JOINT CENTER FOR REGULATORY STUDIES

Evaluating the New Executive Order on Regulation

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Executive Summary

In 2007, President Bush amended President Clinton's executive order on government regulation, making changes that could have far-reaching consequences for how the government weighs the costs and benefits of regulatory activity. Although the new Bush executive order would impose greater requirements on regulatory agencies than are currently imposed, we think the benefits are likely to exceed the costs. We argue that the new executive order should have included independent regulatory agencies, such as the Federal Communications Commission, in addition to executive regulatory agencies.

Evaluating the New Executive Order on Regulation

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I. Introduction

We are pleased to appear before this subcommittee to present our views on the recent executive order on regulation. We have studied and written about regulatory institutions for more than two decades. About a decade ago, we organized a cooperative effort between the American Enterprise Institute and the Brookings Institution to study regulation. The result was the AEI-Brookings Joint Center for Regulatory Studies.[1]

A primary objective of the center is to hold lawmakers and regulators more accountable by providing thoughtful, objective analysis of existing regulatory programs and new regulatory proposals. The Joint Center has been at the forefront of outlining principles for improving regulation, enhancing economic welfare, and promoting regulatory accountability.[2]

Our testimony analyzes the new executive order on regulation. In 2007, President Bush amended President Clinton's executive order on government regulation, making changes that could have far-reaching consequences for how the government weighs the costs and benefits of regulatory activity.[3] We argue that the changes in the order are modest and that the new order is generally an improvement. Specifically, we believe that expanding the executive order to consider guidance is a positive step; the changes regarding regulation are not likely to substantially increase an agency's analytical burden; and, the expansion of presidential influence over major regulatory policies will serve to enhance accountability.[4]

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[1] All publications of the AEI-Brookings Joint Center can be found at http://www.aei.brookings.org.

[2] *See* Arrow et al. (1996).

[3] *See* Exec. Order 13,422, 72 Fed. Reg. 2763 (2007) [hereinafter Exec. Order 13,422]. Previously, President Bush only made minor changes to Exec. Order 12,866, such as transferring the roles assigned to the Vice President to the OMB Director or Chief of Staff. *See* Exec. Order 12,866, 58 Fed. Reg. 51,735 (1993) [hereinafter Exec. Order 12,866]; Exec. Order 13,258, 67 Fed. Reg. 9385 (2002).

[4] For a more pessimistic view of Exec. Order 13,422, see Sally Katzen, *Amending Executive Order 12866: Good Governance or Regulatory Usurpation?*, Testimony 07-01: AEI-Brookings Joint Center for Regulatory Studies (2007) (focusing on the restrictions of agency discretion) and Peter L. Strauss, *Testimony of Peter L. Strauss Concerning President Bush's Recent Amendments to Executive Order 12866*, Testimony 07-02: AEI-Brookings Joint Center for Regulatory Studies (2007) (discussing possible separation of powers concerns). *See also* Robert Pear, *Bush Directive Increases Sway on Regulation*, N. Y.

II. Treating Guidance More Like Regulation

The new Bush order adds to the old Clinton order in three key ways. First, instead of focusing primarily on federal regulations that are likely to cost hundreds of billions annually, the Bush order also focuses on regulatory "guidance" when its impact is likely to be significant. Guidance is similar to regulation because it presents an agency's interpretation or policy on a particular regulatory or technical issue, but it is usually non-binding.[5] For example, the Environmental Protection Agency has issued guidance on the interpretation of waste management activities, and also on some reporting requirements under the Community Right-to-Know Act.[6]

No one actually knows the real impact of most guidance, but it could be substantial. We do know that regulatory agencies issue significant amounts of guidance. The U.S. Food and Drug Administration has a list of over 1,500 guidance documents that are currently in use.[7] Previously, agencies could issue guidance documents in lieu of regulations in order to circumvent the requirements of regulatory review required by executive orders used by President Reagan, the first President Bush, and President Clinton.[8]

TIMES, January 30, 2007; Cindy Skrzycki, *Bush Order Limits Agencies' 'Guidance'*, WASH. POST, January 30, 2007, at D01.

[5] There are certain kinds of guidance that may be considered binding. *See* Robert A. Anthony, *Interpretive Rules, Policy Statements, Guidances, Manuals, and the Like: Should Federal Agencies Use Them to Bind the Public?*, 41 DUKE L. J. 1311, 1311–84 (1992). OMB makes it clear that guidance cannot impose a legally binding requirement. *See* Office of Management and Budget, *Final Bulletin for Agency Good Guidance Practices*, Bulletin No. 07-02: Executive Office of the President (2007) [hereinafter OMB, *Guidance*]. See M. Elizabeth Magill, *Agency Choice of Policymaking Form*, 71 U. CHI. L. REV. 1383, 1383-1447 (2004) for a discussion of the kinds of regulatory tools statutes and case law make available to agencies, and why agencies select certain tools such as adopting a rule, bringing a case to court, or issuing guidance.

[6] *See* Environmental Protection Agency, *Interpretations of Waste Management Activities: Recycling, Combustion for Energy Recovery*, Treatment for Destruction, Waste Stabilization and Release, Office of Pollution Prevention and Toxics (1999); Environmental Protection Agency, *Emergency Planning and Community Right-to-Know Act–Section 313: Guidance for Reporting Releases and Other Waste Management Quantities of Toxic Chemicals: Lead and Lead Compounds.* EPA 260-B-01-027: Office of Environmental Information (2001). More Environmental guidance documents can be found at http://www.epa.gov/epahome/search.html.

[7] For the list of all Food and Drug Administration guidance documents currently in use, see Notice, *Annual Comprehensive List of Guidance Documents at the Food and Drug Administration*, 70(3) Fed. Reg. 824-913 (2005), available at http://www.fda.gov/OHRMS/DOCKETS/98fr/05-155.htm.

[8] *See* OMB, *Guidance*, *supra* note 5 at 3.

The new Bush order will change the way guidance is handled by requiring that each agency evaluate the need for and consequences of the guidance, helping to ensure that it is reasonable. The specific requirements are modest, such as making sure that the guidance is consistent with applicable law, compatible with other regulations and guidance documents, and simple and easy to understand. Before issuing a significant guidance document, which could have an annual effect on the economy of $100 million or more, the agency must notify OMB's regulatory office and submit the draft with an explanation of why guidance is needed, but it is not required to do a full benefit-cost analysis. OMB can then select guidance that could benefit from regulatory review.

Critics suggest that applying some of the same standards to federal guidance as now apply to regulation will allow big business to exert more control over the process, either by delaying the issuance of guidance or changing the guidance to meet its needs. The critics might be right in some instances. In general, however, forcing guidance to be consistent, compatible, and understandable is appropriate.[9]

Interestingly, applying the new standards to guidance could serve to slow efforts by an administration interested in reducing burdens on business. If, for example a regulatory agency were captured by business interests, but guidance had to be approved by OMB, there would at least be some chance that OMB might pinpoint guidance that did not help the general public, or at least slow the rate at which such guidance is issued.[10]

Some critics also contend that the new executive order could impose undue analytical burdens on regulatory agencies. For example, some argue that oversight is not needed because much guidance is non-binding.[11]

The critics raise an important point, the solution to which is to make sure OMB's regulatory office implements its new oversight responsibilities wisely. If guidance is truly

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[9] The American Bar Association, for example, has issued statements calling for public comment on significant "nonlegislative rule(s)" and for availability of these documents on agencies' websites. *See* American Bar Association, *Rulemaking Procedures for Non-Legislative Rules*, A. B. A. (1993); American Bar Association, *Recommendation on Federal Agency Web Pages*, A. B. A. (2001). The American Bar Association confirms this in a draft letter regarding the amendments to Exec. Order 12,866, *available at* http://www.abanet.org/adminlaw/midyear/2007/Tab4Cletter12866.pdf [hereinafter A. B. A., *Draft*].

[10] Those who believe that the OMB review process is captured by business are unlikely to be persuaded by this argument. We believe OMB regulatory review tends to focus more on economic welfare of producers and consumers. That is, in part, because the executive orders focus on economic efficiency, which counts benefits and costs to workers, consumers, and owners of capital.

[11] Non-binding means that firms and other affected parties are not required to do anything specific. See OMB, *Guidance*, *supra* note 5 at 9 for this concern, raised by several commenters on the proposed Bulletin.

non-binding in an economic sense—say, because it does not affect firm behavior—then there is little reason to spend time analyzing it. However, there are cases when guidance may be non-binding in a legal sense, but could affect behavior.[12] Consider a situation where an agency says that it is acceptable to use blue paint to comply with a regulation, but is silent on whether using yellow paint is acceptable. This guidance could have the effect of encouraging firms to use blue paint more than they otherwise would, even though there is not a formal requirement to use it.

Still, we are concerned that the process could slow or stop the issuance of some guidance that serves a useful social purpose. One possible example is guidance from the Food and Drug Administration, which already has good guidance standards and posts guidance on its web site.[13] It appears that a significant amount of guidance issued by this agency can reduce the overall regulatory burden by more clearly articulating government policy toward getting approval of drugs or medical devices. Such guidance would likely pass a benefit-cost test if its primary effect is to reduce regulatory uncertainty without sacrificing the social goal, which in this case could be assuring that a new drug is reasonably safe and effective. Determining the appropriate level of review for the guidance review process will entail tradeoffs between limiting guidance that improves economic welfare and discouraging guidance that reduces economic welfare.

As OMB learns more about the likely effect of different types of guidance, it should tailor its analytical reporting requirements accordingly. In addition, it should take great care in implementing a formal rulemaking for particular guidance because this process is time consuming and relatively costly.[14] Because OMB's regulatory office has a

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[12] *See* OMB, *Guidance*, *supra* note 5 at 9-10 (describing how guidance documents could have "coercive effects" or lead to a change in behavior).

[13] *See* Notice, *The Food and Drug Administration's Development, Issuance, and Use of Guidance Documents*, 62 Fed. Reg. 8961 (1997). The good guidance practices have some of the same features as OMB, *Guidance*, *supra* note 5, including absence of mandatory language, advance notice and opportunity for public comment on some guidance, and posting of guidance on the internet. Guidance from the Food and Drug Administration is available at http://www.fda.gov/opacom/morechoices/industry/guidedc.htm. The Biologics Consulting Group also maintains a database of the Food and Drug Administration's guidance documents, available at http://www.biologicsconsulting.com/guidancedocuments_all.htm.

[14] The American Bar Association expressed concern about the new provision to Exec. Order 13,422, *supra* note 3, reminding agencies to consider using formal rulemaking for complex determinations. *See* A. B. A., *Draft*, *supra* note 9. We, however, agree with the view expressed by Paul R. Noe, *Changes to OMB Regulatory Review by Executive Order 13422*, Testimony 07-04: AEI-Brookings Joint Center for Regulatory Studies (2007). Noe, *supra*, believes that because agencies always had the option to consider formal rulemaking, this provision is not likely to change anything.

very small staff for reviewing regulation and guidance, it has some incentive not to impose burdensome reporting requirements on agencies because then it would be expected to review these reports.

III. New Requirements for Regulation

The new order also adds some requirements for regulation. One feature, highlighted in the press, is that the Bush order requires an agency to provide a written rationale explaining why it is regulating. The only real difference between the Bush order and the Clinton order is that the Bush order specifically requires that the rationale be in writing. A careful reading of the Bush order suggests that a rationale for significant guidance should also be provided as a brief explanation for OMB.

This requirement is important, and should be included for all regulation and guidance. Most economists would agree that the government should not consider regulating unless there is a clear market failure being addressed, such as pollution, monopoly, or lack of good information. The Bush order stops short of requiring that the agency specify a market failure, per se. The agency simply needs to provide a reason for regulating. Regulatory agencies owe the citizenry at least that much before they decide to regulate.[15]

Another feature of the regulatory proposal that has been criticized in the press is the requirement that agencies provide aggregate annual costs and benefits of all regulatory activity on the agency's plan. This requirement should not add substantially to

[15] Professor Sally Katzen, *supra* note 4, former head of regulatory review at OMB, argues, "By giving special emphasis to market failures as the source of a problem warranting a new regulation, the Administration is saying that not all problems are equally deserving of attention; those caused by market failures are in a favored class and possibly the only class warranting new regulations." *See* Katzen, *supra* note 4. We think it is good for government generally to focus on market failures because too often government policies result in serious economic inefficiencies. *See* CLIFFORD WINSTON, GOVERNMENT FAILURE VERSUS MARKET FAILURE: MICROECONOMICS POLICY RESEARCH AND GOVERNMENT PERFORMANCE (AEI-Brookings Joint Center for Regulatory Studies 2006). Katzen brings up the example of civil rights. We think some civil rights legislation could have been justified on the basis of market failure arguments. Nonetheless, the Bush EO clearly allows for the agency to provide a rationale other than market failure. "Each agency shall identify in writing the specific market failure (such as externalities, market power, lack of information) *or other specific problem that it intends to address* (including, where applicable, the failures of public institutions) that warrant new agency action, as well as assess the significance of that problem, to enable assessment of whether any new regulation is warranted" [emphasis added]. *See* Exec. Order 13,422, *supra* note 3.

the analytical burden of regulatory agencies because they already must present anticipated costs and benefits of individual regulations on the plan.[16] There is value in having an estimate of the annual regulatory cost, much in the same way that government provides an annual budget estimate. We would also add that, where possible, the annual regulatory cost should be compared with the annual regulatory benefit.

III. Expanding Presidential Influence

The third change in the Bush executive order is to require affected regulatory agencies to designate a presidential appointee as the regulatory policy officer. The regulatory policy office would then need to approve a specific regulation before it could be included in the agency's annual regulatory plan of the important regulations it expects to issue.

This change could be very important. Critics believe that it would politicize the process by taking away some discretion from civil servants. We agree with the critics, but think this is ultimately a good thing. The benefits are similar to the benefits of regulatory oversight in general. First, as Justice Breyer has noted, civil servants in some regulatory agencies may tend to have tunnel vision, and fail to consider the broader impacts of their regulatory proposals.[17] Second, requiring that a presidential appointee in a policy office approve regulations increases the chances that the regulations will consider costs and benefits because such balancing is more likely to be consistent with the president's agenda than an agency's agenda. Third, this change will hold the president more accountable for regulatory policies that his administration selects.[18] Of course, the particular person the president appoints could skew the process away or towards the

[16] Exec. Order 12,866, *supra* note 3, already required that the agency report the most significant rules on a "Regulatory Plan," along with each rule's anticipated benefits and costs. Exec. Order 13,422, *supra* note 3, only asks that agencies sum the estimated benefits and costs of the regulations, which is a way of enhancing transparency. *See* Steven D. Aitken, *Statement of Steven D. Aitken, Acting Administrator, Office of Information and Regulatory Affairs, Office of Management and Budget before the Subcommittee on Commercial and Administrative Law of the Committee on the Judiciary, United States House of Representatives* (2007). Katzen, *supra* note 4, believes that this estimate will be meaningless and should not be included.

[17] *See* STEPHEN BREYER, BREAKING THE VICIOUS CIRCLE: TOWARD EFFECTIVE RISK REGULATION (Harvard University Press 1993).

[18] See Strauss, *supra* note 4, for objections to this view on the grounds of the need for separation of powers.

balancing of costs and benefits, but we think the president should have that choice because voters can hold him accountable for his policies.

IV. New Executive Order Should Have Been More Ambitious

If we have any complaint about the President's executive order, it is that it does not go far enough. In particular, it excludes a whole group of regulatory agencies from review—the "independent" regulatory agencies like the Federal Trade Commission, the Federal Communications Commission, and the Federal Energy Regulatory Commission—that play a critical role in a number of areas ranging from telecommunications to energy.

We would suggest bringing these independent agencies under the executive order's umbrella.[19] This change would hold a wider range of regulators more accountable for the costs and benefits of their policies and hopefully lead to more efficient policies across the board. It is still an open question as to whether the president has the legal authority to make this change; if the president does not, then Congress should give this general authority to the president directly.[20]

In addition, we would suggest subjecting significant guidance documents to the same requirements as significant regulations—namely benefit-cost analysis and a broadly based benefit-cost test. This would give regulators and the public a better understanding of the likely economic impacts of guidance, and it could also improve actual guidance.

Although the new Bush executive order would impose greater requirements on regulatory agencies than are currently imposed, we think the benefits are likely to exceed its costs, but a lot will depend on how it is implemented. The new executive order is also consistent with a global trend toward featuring a more prominent role for economic analysis in informing regulatory decisions.

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[19] *See* Robert W. Hahn & Cass R. Sunstein, *A New Executive Order for Improving Federal Regulation? Deeper and Wider Cost-Benefit Analysis*, 150 U. OF PENN. L. REV. 1489 (2002).

[20] See Strauss, *supra* note 4, for an opposing view.