MERCATUS CENTER
George Mason University

May 2, 2011

Mr. Cass Sunstein
Administrator, Office of Information and Regulatory Affairs
Office of Management and Budget
725 17th Street, NW
Washington, DC 20503

Dear Mr. Sunstein:

The Regulatory Studies Program of the Mercatus Center at George Mason University is dedicated to advancing knowledge of the impact of regulation on society. As part of its mission, the Regulatory Studies Program conducts careful and independent analyses employing contemporary economic scholarship to assess rulemaking proposals and reports from the perspective of the public interest.

We appreciate the invitation to comment on the Draft 2011 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local and Tribal Entities,and hope that our comments will be useful to the Office of Management and Budget.

Sincerely,

Richard A. Williams, Ph.D.

Director for Policy Studies

The Regulatory Studies Program (RSP) of the Mercatus Center at George Mason University is dedicated to advancing knowledge of the impact of regulation on society. As part of its mission, RSP conducts careful and independent analyses employing contemporary economic scholarship to assess rulemaking proposals from the perspective of the public interest. Thus, this comment on the Draft 2011 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities (The Report) does not represent the views of any particular affected party or special interest group, but is designed to assist the Office of Information and Regulatory Affairs (OIRA) in the Office of Management and Budget (OMB) as it seeks advice on this draft report.

OIRA is to be congratulated on an excellent report, although we have some minor disagreements with the findings. We agree with all of OIRA's recommendations found on page 5 of the Report[1]. The following are some additional observations/recommendations:

I. Independent agencies

OMB should be commended for its section on the independent agencies. The Report cites the Government Accountability Office (GAO) report that notes that, of the 17 rules performed by independent agencies, not one assessed benefits and costs of their rules.[2] OMB states, "The absence of such information is a continued obstacle to transparency, and it might also have adverse effects on public policy."[3] We agree strongly with this conclusion. The lack of analysis will become particularly acute as more rules implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act, since independent agencies have substantial new rulemaking responsibilities under this act. This is particularly troublesome

[1] See this publication for a review of regulations impact on jobs. Williams, Richard A. "The Impact of Regulation on Investment and the U.S. Economy." http://mercatus.org/publication/impact-regulation-investment-and-us-economy
[2] Draft 2011 "Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local and Tribal Entities," p. 4.
[3] IBID, p. 30.

with respect to the new Consumer Financial Protection Bureau, which is able to write rules "autonomously" without oversight from, apparently, any executive branch agency or even the Federal Reserve, where it is housed.

II. Retrospective Review

OMB should also be commended on its section soliciting recommendations on retrospective analysis. The suggestion that agencies actually "undertake" retrospective analysis is a good one. That would be improvement on just asking the public which rules need to be taken off of the books. Most the interest in any existing rules will be by those who must directly comply with the rules and their incentives are usually to keep the rules. Many of the rules, or at least a portion of them, were put into place at the behest of the regulated industry in the first place,to raise the cost of rival firms.[4] Additionally, firms may worry that, if a rule is removed, it might be replaced by one that is more stringent. The group that will not comment on existing rules, but who might be viewed as the most severely impacted, are new entrants into industries in the future. These entities don't comment because they don't exist yet. In a sense, there is no *guardian ad litem* to represent their interests.

An analysis of existing rules could demonstrate the effects on both incumbent firms and consumers, as well as the potential to affect new entrants. However, just as there is very little incentive for incumbent firms to remove rules, the same might also be said with respect to the agencies that often labored for years to produce them. This probably means that there needs to be an independent organization performing such analysis. Agencies can do their part by explaining in their Regulatory Impact Analyses (RIAs) which agency strategic goals under the Government Performance and Results Act (GPRA) the regulation is intended to

[4] Salop, SC, Raising Rivals' Costs, The American Economic Review, 73(2) May, 1983.

advance. Agencies can also establish goals and measures for individual regulations and identify data that could be used to evaluate the regulation's effects in the future. [5]

III. Improvements in Analysis and Claimed Net Benefits

The report claims that "OMB and the regulatory agencies have taken a number of steps to improve the rigor and transparency of analysis supporting public policy decisions."[6] We agree that this is an excellent use of OIRA resources and believe that they should continue to do so. However, OMB claims that they have achieved superior performance for their regulations as compared to the two previous administrations. In Figure 2-1: "Annual Net Benefits of Major Rules through the Second Fiscal Year of an Administration," the claim is made that the current administration has generated much higher net benefits in its second year than the previous two administrations. The current administration claims to have about $35.5 billion in net benefits as opposed to $2.3 in the Bush Administration and $10.6 in the Clinton Administration.[7] However, this claim should be viewed skeptically for several reasons. First, as the Mercatus Regulatory Report Card shows, the regulatory analyses that this report draws from are simply not good enough overall to make any claim about the relative net benefits of these rules. The chart below adds the scores from the Report Card for those regulatory analyses that have been evaluated[8]:

Agency	RIN	Title	Budget Effects	Regulatory Report Card Score

[5] See the testimony by Jerry Ellig to the House Judiciary, March 29, 2011 on this subject at http://mercatus.org/sites/default/files/publication/Ellig%20Written%20Testimony%20House%20Judiciary%20March%2029%202011.pdf . Very few agencies do this now.
[6] IBID. The Report, p. 65.
[7] IBID., The Report, p. 51.
[8] Not all rules have been scored (highlighted rules). If no score appears it is because the rule was proposed prior to 2008 and we only began scoring in 2008, the rule was a budget rule in 2010 and we only scored budget rules in 2008 and 2009 or the rule was an interim final rule, not a proposal. Two rules did not show up on reginfo.gov, Broadband Technology Opportunities Program (0660-ZA28) and Early Retiree Reinsurance Program (0991-AB64).

USDA	0560-AH90	Supplemental Revenue Assistance Payments Program (SURE)	0.1	
USDA	0560-AI07	Dairy Economic Loss Assistance Payment Program	0.2	
USDA	0578-AA43	Conservation Stewardship Program	2.7-3.2	
USDA	0584-AD30	SNAP: Eligibility and Certification Provisions of the Farm Security and Rural Investment Act of 2002	2.2	
DOC	0660-ZA28	Broadband Technology Opportunities Program	2.1	
DOD	0720-AB17	TRICARE: Relationship Between the TRICARE Program and Employer-Sponsored Group Health Coverage	>(0.1)	
DOD	0790-AI59	Retroactive Stop Loss Special Pay Compensation	0.4	
HHS	0938-AP40	Revisions to Payment Policies Under the Physician Fee Schedule for CY 2010 (CMS-1413-FC)	(11.0)	23/60
HHS	0938-AP41	Changes to the Hospital Outpatient Prospective Payment System and Ambulatory Sugical Center Payment System for CY 2010 (CMS-1414-F)	0.4	24/60
HHS	0938-AP55	Home Health Prospective Payment System and Rate Update for CY 2010 (CMS-1560-F)	(0.1)	25/60
HHS	0938-AP57	End Stage Renal Disease Bundled Payment System (CMS-1418-F)	(0.2)	32/60
HHS	0938-AP72	State Flexibility for Medicaid Benefit Packages (CMS-2232-F4)	(0.7)	
HHS	0938-AP77	Revisions to the Medicare Advantage and Medicare Prescription Drug Benefit Programs for Contract Year 2011 (CMS-4085-F)	(0.3)	18/60
HHS	0938-AP78	Electronic Health Record (EHR) Incentive Program (CMS-0033-F)	1.0-2.5	25/60

HHS	0938-AP80	Medicare Program; Changes to the Hospital Inpatient Prospective Payment Systems for Acute Care Hospitals and the Long Term Care Hospital Prospective Payment System and Fiscal Year 2011 Rates	(0.2)	
HHS	0991-AB64	Early Retiree Reinsurance Program	1.0	
HHS	0991-AB71	Pre-Existing Condition Insurance Plan Program	1.0	
STATE	1400-AC58	Schedule of Fees for Consular Services, Department of State and Overseas Embassies and Consulates	0.3-0.4	
DHS	1615-AB80	U.S. Citizenship and Immigration Services Fee Schedule	0.2	
DHS	1651-AA83	Electronic System for Travel Authorization (ESTA): Fee for Use of the System	0.1-0.2	
DHS	1660-AA44	Special Community Disaster Loans Programs	0-1.0	20/60
ED	1810-AB04	State Fiscal Stabilization Fund Program--Notice of Proposed Requirements, Definitions, and Approval Criteria	9.5	23/60
ED	1810-AB06	School Improvement Grants--Notice of Proposed Requirements Under the American Recovery and Reinvestment Act of 2009; Title I of the Elementary and Secondary Education Act of 1965	2.9	31/60
ED	1810-AB07	Race to the Top Fund--Notice of Proposed Priorities, Requirements, Definitions, and Selection Criteria	3.2	23/60
ED	1810-AB08	Teacher Incentive Fund--Priorities, Requirements, Definitions, and Selection Criteria	0.4	

ED	1840-AC96	Student Assistance General Provisions; TEACH Grant, Federal Pell Grant, and Academic Competitiveness Grant, and National Science and Mathematics Access To Retain Talent Grant Programs	0.2	
ED	1840-AC99	General and Non-Loan Programmatic Issues	0.2	17/60
ED	1840-AD01	Federal TRIO Programs, Gaining Early Awareness and Readiness for Undergraduate Program, and High School Equivalency and College Assistance Migrant Programs	1.0	
ED	1855-AA06	Investing in Innovation--Priorities, Requirements, Definitions, and Selection Criteria	0.5	19/60
DOE	1901-AB27	Loan Guarantees for Projects That Employ Innovative Technologies	3.5-4.0	5/60
DOE	1904-AB97	Weatherization Assistance Program for Low-Income Persons - Multi-Unit Buildings	4.0	10/60
VA	2900-AN54	Diseases Associated With Exposure to Certain Herbicide Agents (Hairy Cell Leukemia and Other Chronic B Cell Leukemias, Parkinson's Disease, and Ischemic Heart Disease)	4.1-5.4	

For those that actually did analysis that were scored, the average score was 21 out of 60, which certainly would not be a passing grade in anyone's class and hardly sufficient to draw accurate comparisons with regulations from previous administrations.

OIRA could, to make their table more descriptive, show which rules were initiated in an earlier administration.

An additional problem is that there is at least one major benefit claimed that may not, in fact, be a true net benefit. The rule that claims the highest estimated benefits is the Passenger Car and Light Truck Corporate Average Fuel Economy Standards MYs 2012 to 2016.[9] But the benefits in this rule were largely the result of the federal government substituting its preferences for discounting for the actual preferences of consumers. The claim is that consumers will save "more than $3,000 due to fuel savings" while only paying out approximately $1100. In the NHTSA analysis, at a 3% discount rate the present value of the fuel savings is $158 billion and the present value of the CO_2 reduction is $16.4 billion. The fuel savings appears to represent over 90% of the benefits. But consumers choose cars for many different reasons, and fuel economy is only one reason. Any regulation that begins with the assumption that consumer purchases are irrational (and that the agency is in a better position to determine what is rational) should be suspect. In particular, if 90% of the benefits are from correcting this "irrationality," it may very well be that there are net costs from reduced consumer surplus, not net benefits.[10] At a minimum, EPA should note that any benefits accruing from cars that consumers have not chosen based on their demonstrated preferences do not result from a market failure. EPA's choice of a discount rate of 3% is apparently much lower than consumers choose when investing in an automobile.

IV. Happiness Research

While the push towards using behavioral economics to fashion more effective and less onerous regulations are to be applauded, OMB should approach research on "happiness" with a great deal of caution, particularly with respect to federal regulation. For example, there may be considerable variance between owner/operators of small businesses and

[9] http://www.nhtsa.gov/staticfiles/rulemaking/pdf/cafe/CAFE_2012-2016_FRIA_04012010.pdf

[10] In its Regulatory Impact Analysis of the proposed regulation, EPA notes this "conundrum," and the Mercatus Regulatory Report Card gave this regulation a high score on identifying the systemic problem in part because the agencies were forthright about this puzzle.

owners/managers of large businesses as to how "happy" they are with regulations. Some results that should be considered include:

1) Republicans are "happier" than Democrats. PEW research shows that 88% of Republicans are "pretty happy" or "very happy" as opposed to only 77% of Democrats.[11] Only 9% of Republicans are "not too happy" whereas 20% of Democrats are not too happy. The difference appears to persist over time.
2) People that do not have children appear to be "happier."[12]
3) Since 1972, women's happiness has dropped, despite labor force participation rates rising to record levels.[13]
4) Religious people appear to be "happier."[14]
5) Divorced people are less "happy."[15]

It would be interesting to see precisely what federal policy prescriptions would follow from the above results. In fact, "Freedom" appears to account for the most happiness around the world, as reported in "Development, Freedom and Rising Happiness,"[16] although this seems to have escaped OMB's literature review.

Two articles were cited by the OMB report on the implications for regulatory policy and uses of cost-benefit analysis (footnote 81, missing from draft report by supplied by OIRA).[17] The one that seems closest to suggestions for incorporation of happiness metrics was "Happiness

[11]http://pewresearch.org/pubs/1005/republicans-happier
[12] Simon, Robin, "The Joys of Parenthood, Reconsidered" Contexts, 7(2) April 2008, pp. 40-46.
[13] Stevenson, Betsey and Justin Wolfers," The Paradox of Declining Female Happiness," American Economic Journal: Economic Policy 1(2), 2009.
[14] See, for example, Robbins, Mandy and Leslie J. Francis, "Are religious people happier? A study among undergraduates in Research in religious education by Francis, Leslie, et. al. Smyth Y Helwys Publishing, Georgeia, U.S. 1996.
[15] Lucas, Richard e. al., "Time Does not Heal All Wounds: A Longitudinal Study of Reaction and Adaptation to Divorce 16 Psychol., Science, 945, 947 (2005).
[16] Inglehart, Ronald, et. al. "Development, Freedom, and Rising Happinesss: A Global Perspective (1981-2007)
[17] The missing citations were: Vitarelli (2010); and Adler and Posner (2008).

Metrics in Federal Rulemaking" by Anthony Vitarelli.[18] Vitarelli suggests that agency's supplement traditional benefit-cost analysis with a "happiness inquiry." He produces some interesting conclusions such as, "Consumers… are resilient and adapt quickly to (the) negative income effect."[19] If so, he concludes that agencies could give on-going costs less weight. However, when examining the implications for discount rates, he states that happiness research should "counsel in favor of a far higher discount rate" because of "individuals' propensity to adapt to changed circumstances. However, unlike the unquestioning acceptance of de-weighting the effects of costs on consumers, here he suggests that to use the results on discount rates would be "unsettling-and even offensive" if these results were accepted.[20]

Despite these issues, he suggests that agencies may soon find their regulations will be "arbitrary and capricious" if they are found missing the additional information supplied by happiness research. To the best of our knowledge, there is not a single statute that governs any of the federal agencies that mandates that they ensure that consumers are made any "happier" because of their regulations.

Finally, there is a literature that casts doubt on the entire idea that some measure of "happiness" is an appropriate goal for policy.[21] None of this literature appears to be mentioned in the OMB report.

As Professor Tyler Cowen of George Mason University has pointed out, because of the massive ambiguity of happiness as an endpoint, growth and employment are much better

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[18] Vitarelli, Anthony, "Happiness Metrics in Federal Rulemaking," Yale Journal on Regulation, 27(1), 2010.
[19] IBID, p. 137
[20] IBID, P. 141.
[21] A summation of this literature can be found in Wilkinson, Will, "In Pursuit of Happiness Research: Is it Reliable? What Does it Imply for Policy?" Policy Analysis, 590, April 11, 2007

indicators of human well being; and growth is a particularly better metric for comparing policies.[22] In fact, benefit-cost analysis corrects GDP to include things that people find valuable but do not show up as being counted in GDP, particularly when these items can be measured using market-based willingness-to-pay results.

Summary

OMB has produced a thorough and useful report based on the instructions in the Regulatory-Right-to Know-Act. Requiring agencies to produce both more (particularly in the case of independent agencies) and better quality analysis is the right direction for OIRA. However, OIRA should be cautious about over claiming success, particularly based on our analysis of the quality of regulatory impact analyses to date. Of course, OIRA must rely on the agencies for this analysis. The focus on retrospective review, in particular, how best to accomplish retrospective review, is a welcome one. Finally, we urge caution when embracing behavioral economics in analyzing the benefits of market interventions. In particular, we note that the happiness research may not ever develop into useful metrics and, given its current state, is not ready for prime time use in RIA's.

Richard A. Williams, PhD.

Director for Policy Studies

[22] Cowen, Tyler, "How to Think About Policy," in The Growth Imperative: A New Approach to the Theory of Economic Policy.