Statement of Sally Katzen

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before the

Subcommittee on Courts, Commercial and Administrative Law
of the
House Committee on the Judiciary

on

"Cost Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"

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Chairman Coble, Ranking Member Cohen, Members of the Subcommittee. Thank you for inviting me to testify today. I have been privileged to appear before this Committee on a number of occasions, both as a government official and as a private citizen. The Committee's oversight activities in the field of administrative law make an important contribution to the public's understanding of our nation's regulatory system and help frame the issues for both the legislative and the executive branches.

As you know, I served as the Administrator of the Office of Information and Regulatory Affairs (OIRA) at the Office of Management and Budget (OMB) for the first five years of the Clinton Administration, then as the Deputy Assistant to the President for Economic Policy and Deputy Director of the National Economic Council, and then as the Deputy Director for Management of OMB. After leaving government service in January 2001, I taught administrative law courses at the University of Michigan Law School, George Washington University Law School, George Mason University Law School, and the University of Pennsylvania Law School, and also taught American Government courses to undergraduates at Smith College, Johns Hopkins University, and the University of Michigan in Washington Program; this semester, I am teaching a seminar in advanced administrative law at NYU School of Law and am a Senior Advisor at the Podesta Group here in Washington. Before entering government service, I was the Chair of the ABA Section on Administrative Law and Regulatory Practice (1988-89), and during my government service, I was the Vice Chair (and Acting Chair) of the

Administrative Conference of the United States (ACUS). I have written articles for scholarly publications and have frequently been asked to speak on administrative law in general and rulemaking in particular.

The subject of today's hearing is "Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits." I understand the Committee wants to focus on several things: Cost/Benefit Analysis (CBA) in developing proposed and final regulations, Presidential (or centralized regulatory) Review of the economic analysis underlying those regulations, and Judicial Review. I support – strongly support – the use of economic analysis in developing regulations and the centralized review of those regulations, but I have reservations – serious reservations – about codifying the requirements for economic analysis and centralized review and providing for judicial review of that process.

When someone says "Cost/Benefit Analysis," people tend to look away or their eyes glaze over. The analysis itself – that is, the actual work product -- may be complicated, highly technical and often difficult to follow, but the concept is quite simple. It is a way to think about the consequences of a proposed action and then try to translate quite diverse consequences into the same metric -- typically money – so we can evaluate whether the proposal is, on the whole, good for us or not. We do this every day of our lives, whether it be for something trivial (walk or take a taxi) or significant (purchase a home or launch a new business), with the extent of the analysis roughly commensurate with the importance of the decision we are trying to make.

Requirements for economic analysis to inform, or in support of, important regulatory proposals adopted through rulemaking -- typically proceedings under Section 553 of the Administrative Procedure Act -- have been around at least since President Nixon established a "Quality of Life Review" program for certain high-profile regulations. Beginning in 1981 with President Reagan's Executive Order 12291, all Presidents (both Republicans and Democrats) have required regulatory agencies within

the Executive Branch to assess the costs and benefits of proposed actions, and, among other things, to the extent permitted by the laws that you enact, ensure that the benefits of the intended regulations justify the costs. The requirement to undertake this economic analysis and to submit it along with a draft proposed or final rule to OIRA was designed to make sure that the agency has thought through, in a disciplined and rigorous way, the obvious and the less obvious costs and benefits that are likely to occur if the proposal is adopted and has the force and effect of law. It is a significant undertaking. Consider the description of the overview of the analysis to be developed by regulatory agencies under Executive Order 12866:

> "An assessment . . . of benefits anticipated from the regulatory action (such as, but not limited to, the promotion of the efficient functioning of the economy and private markets, the enhancement of health and safety, the protection of the natural environment, and the elimination or reduction in discrimination or bias), together with, to the extent feasible, a quantification of those benefits;
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> "An assessment . . . of costs anticipated from the regulatory action (such as, but not limited to, the direct cost both to the government in administering the regulation and to businesses and others in complying with the regulation, and any adverse effects on the efficient functioning of the economy, private markets (including productivity, employment, and competitiveness), health, safety and the natural environment), together with, to the extent feasible, a quantification of those costs . . . [and]
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> "An assessment . . . of costs and benefits of potentially effective and reasonably feasible alternatives to the planned regulation . . . ."

And for those who thirst for a detailed description of how to do all of the above, I would refer you to OMB Circular A-4, which I require my students to read--with profuse apologies.

There are some items in the calculus, such as the costs of new equipment, the time it will take to install that equipment and train employees to use it, or savings from fewer

trips to the hospital or less employee time off to recuperate from workplace injuries that are relatively easy to quantify and monetize. There are other factors that are more difficult to quantify and monetize, such as being able to see across the Grand Canyon, increased protection from invasions of privacy, or peace of mind that food in the stores is free of e-coli. There are many economists working on ways to use samples or surrogates to provide relatively accurate data, such as willingness to pay, etc., and a literature that is full of commendations and critiques from their proponents and detractors. The theories and practices are evolving and are not without controversy, on the cost side as well as on the benefit side. But with benefits as with costs, thinking through the consequences and seeking to quantify and value them in a serious way is itself highly informative.

Indeed, gathering the data and structuring the analysis help the agency staff refine its thinking in drafting the proposal; the presentation of the analysis to the agency decision-makers can reinforce existing assumptions or cause rethinking of conventional wisdom; the review of the analysis by the staff of OIRA provides a dispassionate second opinion and quality control for the analysis; and the availability of the data and the analysis throughout the process enables the various stakeholders, their elected officials and the public generally to evaluate in a more objective way the merits of the regulatory action – what is at stake and for whom?

In a word, undertaking economic analysis in the course of developing regulations provides important information that often affects, for the better, the shape or scope of a proposed regulatory action. It is an input; it is useful; it is instructive. Indeed, I cannot imagine making regulatory choices (or legislative choices for that matter) without a systematic consideration of the intended (and unintended) consequences of a proposed action. But such economic analysis, carried out by the most eminent economists according to tried and true methodology, is not and cannot be dispositive; it is not precise on its own terms, and I believe it was Professor Einstein who supposedly had a sign over his desk at Princeton saying: "Not everything that can be counted counts and not everything that counts can be counted." CBA (and economic analysis generally) is

valuable, but hardly a silver bullet to resolve all issues – you can't just turn it on and declare the job is done.

There are other aspects of CBA that may become relevant if the Congress seeks to codify the Executive Order and/or provide for judicial review of that process that I will turn to in a moment. But first it is important to recognize that while regulatory agencies in the Executive Branch have been required to prepare Regulatory Impact Analyses (RIA), including analyses of costs and benefits, since at least 1981, there is no similar requirement for Independent Regulatory Commissions (IRCs) – those multi-headed commissions, such as the SEC, FCC, FTC, FEC, CFTC and the Federal Reserve, whose Members do not serve at the pleasure of the President and can be removed from office only for cause.

I raised this anomaly when I testified before this Committee on July 27, 2010, on "Federal Rulemaking and the Regulatory Process." Among other things, I noted that there was no legal barrier to the President's extending the requirement for economic analysis and centralized review to the IRCs, and that both President Reagan and President Clinton declined to do so for political reasons – namely, out of deference to the Congress -- rather than a lack of constitutional authority. The result, however, is that IRCs do not typically engage in the analysis that has come to be expected for Executive Branch agencies; in the 2010 OMB Report to Congress, it appears that roughly half of the rules developed by the IRCs over a ten-year period have no information on either costs or benefits, and those that do have very little monetization of benefits and costs. This is not a good sign because we are about to see a large increase in regulations from the IRCs; in Dodd-Frank alone, there are over 300 provisions saying that agencies shall or may issue rules, most of them directed at IRCs.

Support for requiring IRCs to engage in economic analysis in developing their rules has come from a number of commentators across the political spectrum. Several months ago (February 28, 2011), this Committee held a hearing on "The Administrative Procedure Act at 65," and all three witnesses (from both sides of the aisle) concurred in

the suggestion. Last month (April 7, 2011), Resources for the Future (a centrist think tank) held an all-day conference here in Washington, where various scholars and former government officials from five different IRCs (again, from both sides of the aisle) explored the status of IRC analysis in rulemaking and the agencies' potential to do more. The materials compiled for that conference would provide a solid foundation for your further consideration of this issue.

To be sure, the quality of the work done by Executive Branch agencies -- how solid or sophisticated is the economic analysis -- is mixed but has improved over the years. Some scholars have studied selected agencies and given them mediocre (or even failing) grades, but others have been generally complimentary while suggesting areas for improvement. This should not be surprising because agencies are very different from one to the next, with different cultures and different resources. The latter is important because economic analysis (at least thoughtful, careful, comprehensive analysis) takes time and resources, and the more significant the proposed regulatory action, the more time and resources it should consume. Yet some of the very people who call for more analysis are the first to suggest straight-lining or reducing the agencies' budgets.

An important incentive for Executive Branch agencies to provide high quality analysis is that their work is reviewed and critiqued by OIRA (and other agencies during the inter-agency process) under Executive Order 12866, and ultimately made available to the public. Nothing focuses the mind like knowing that someone will be reading (or listening) to your paper (or presentation). With Executive Branch agencies, OIRA staff regularly review the RIAs that accompany important draft proposed and final rules before they are officially signed by the issuing agency and published in the Federal Register. The OIRA staff communicates its views concerning the RIAs, formally or informally, to the agency staff, who generally pay attention to, and usually heed, the critiques/suggestions from OIRA; if there is disagreement, there is an informal process for "elevating the issue" to the more senior staff or even to the political appointees, where ultimately there is a meeting of the minds.

While the way Executive Branch agencies and IRCs conduct rulemaking is for all practical purposes the same, the differences between the two types of agencies in terms of their structure and their relationship to the President suggests that the review process or the "enforcement" of any requirement for economic analysis should not – possibly, cannot -- be the same without compromising the independence of the IRCs when they do not acquiesce in OIRA's assessment. Congress confronted this very question in the Paperwork Reduction Act, where it provided for OIRA review of information collection requests (i.e., government forms) from all agencies, Executive Branch and IRCs. OIRA was authorized to approve or disapprove paperwork from Executive Branch agencies directly, but when it disapproved paperwork from an IRC, the IRC is able to void any disapproval by majority vote, explaining the reasons for its decision to do so. A variation on that approach for review of the analysis underlying IRC rulemakings could be that OIRA would provide its views in writing to the IRC, and that document would be presented to the Commission (presumably in a public meeting), where the critiques/suggestions could be discussed and disposed of (accepted or dismissed) per the will of the Commission before final approval of the regulatory action.

As noted above, past presidents have been reluctant to extend OIRA's role to the IRCS out of deference to Congress. A Sense of the Congress that such a course would be desirable would go a long way to ameliorate any concerns in that regard. Or Congress could designate an entity outside the Executive Branch as the reviewer of the economic analysis undertaken by the IRCs. Two obvious candidates are the Government Accountability Office (GAO) and the Congressional Budget Office (CBO). The former was given a limited (check the box) role in reviewing and commenting (to Congress) on the regulations issued by IRCs under the Congressional Review Act, and the latter already has analytical capacity that could be directed to this effort. Neither of these entities has the expertise or experience that OIRA has with reviewing economic analyses, but both have the "virtue" of being identified with Congress rather than the President, which may be important to those who read "independent regulatory commission" as independent of only one and not the other political player.

In any event, I am a staunch supporter of requiring regulatory agencies to do economic analysis and of having their work reviewed by OIRA. These are two of the most important foundational principles in Executive Order 12866 (carried over with significant modifications from Executive Order 12291) and recently reaffirmed by President Obama in Executive Order 13653. As noted earlier, Presidents of both political parties have endorsed these principles by incorporating them in their own executive orders and/or implementing them under their predecessor's executive orders. Nonetheless, and with respect, I do not believe that the Congress should seek to codify these principles in legislation.

One of the first provisions in Executive Order 12866 is that "agencies should promulgate only such regulations as are required by law, are necessary to interpret the law, or are made necessary by compelling need . . . ." The agency should then "identify the problem it intends to address (including, where applicable, the failures of . . . public institutions that warrant new . . . action) as well as assess the significance of that problem"; it should "examine whether existing regulations (or other law) have created, or contributed to, the problem . . . and whether those regulations (or other law) should be modified to achieve the intended goal . . ."; and it should "identify and assess available alternatives to direct regulation . . . ." These are the standards that should be met when an agency intends to act. I would suggest that these same standards should be met before Congress takes action.

Given the recent reaffirmation of the salient principles in Executive Order 13653, and the now almost 30-year implementation of these provisions, what is the compelling need to be addressed by legislation? The Executive Branch agencies undertake economic analysis as part of the process of developing rules, and if further analysis is needed, OIRA works with the agency to accomplish that. Moreover, all indications are that the rules being developed by Executive Branch agencies generally meet the "benefits justify costs" standard of the Executive Order. For example, in OMB's 2010 Report to Congress, OMB included data on the cost ($43-$55 billion) and the benefits ($128-$616 billon) of major rules issued by Executive Branch agencies over the most recent ten-year

period (FY 1999-2009). Even if one uses the highest estimate of costs and the lowest estimate of benefits, the regulations issued over the past ten years have produced net benefits of $73 billion to our society. [This cannot be dismissed as a partisan report by the current administration, because OMB issued reports with similar results (benefits greatly exceeding costs) throughout the George W. Bush Administration (e.g., for FY 1998-2008, major regulations cost between $51 and $60 billion, with benefits estimated to be $126 to $663 billion dollars).]

Even if the Executive Branch agencies are not undertaking economic analyses when they should, or are not conducting them with sufficient rigor or proficiency, or are not adequately reflecting those analyses in the framing of regulations as required under the Executive Order – and, again, that case has not been made – would legislating pieces or all of the Executive Oder likely bring about significant change? And are there not alternatives to legislation that would likely have the same or similar salutary effect? Congress has imposed a series of analytical requirements on the agencies over the last 30 years, from the Paperwork Reduction Act, to the Regulatory Flexibility Act, to the National Environmental Policy Act, to the Unfunded Mandates Reform Act, to name just a few, without substantially increasing agency funding to carry out the tasks assigned in those statutes. Before adding another requirement, Congress might rationalize the current set of analytical requirements and/or provide more resources to the agencies to do the analyses and more resources to OIRA to review them. If there is an implementation problem, Congress should address the source of that directly and not just add another requirement that also cannot be implemented. Surely, Congress has a host of alternatives to legislation, including hearings such as this one, by which to monitor agency activity, evaluate current practices, spotlight any deficiencies, and bring public pressure to improve agency performance if that is what is called for.

Second, one of the last provisions in Executive Order 12866 is the statement: "This Executive order is intended only to improve the internal management of the Federal Government . . . ." This statement appears in virtually all executive orders from all administrations. It is not a throw-away clause but rather reflects the nature of

executive orders – that is, orders by the Executive (the President) to those who report to him and for whom he is constitutionally responsible. Executive orders are traditionally the prerogative of the President; they are not subject to notice-and-comment or any other form of public participation in their formulation or to any judicial interpretation or enforcement in their implementation. The history of this particular line of executive orders, from EO 12291 to EO 12866 to EO 13422 to EO 13653, shows that while many of the concepts are the same from one administration to the next, different presidents choose to emphasize different things – e.g., costs and the effects on the economy, openness and transparency, market failure as a basis for regulating, public participation, etc. The differences may be subtle but are nonetheless important indicators of administration policies and preferences, which would likely be lost if the President's prerogatives were preempted by legislation (which is much more difficult to modify than an executive order).

Third, if Congress were to codify the analytical requirements of the Executive Order, it would be amending a host of previously enacted statutes (dating back over half a century or more). At this point, it is unclear how many and which statutes would be amended and what the implications of such an amendment would be, for both the regulated entities and the intended beneficiaries of these statutes. I am referring to the fact that under the Executive Order, agencies are required to conduct economic analysis, but in developing regulations the agencies are, in the first instance, bound by their authorizing legislation. Some legislation is silent on the question of the role of costs in the formulation of regulations; others do not permit consideration of such factors. For example, Section 109(b)(1) of the Clean Air Act provides that the Administrator should set standards for certain pollutants at a level "requisite to protect the public health" with "an adequate margin of safety." The Supreme Court (in a unanimous decision written by Justice Scalia) was emphatic that the Administrator cannot lawfully take account of costs in setting the standards. Whitman v American Trucking Associations, 531 US 457 (2001). For that reason, the Executive Order repeatedly prescribes certain practices "to the extent permitted by law."

However, if provisions of the Executive Order were codified, they would become decisional criteria. As a result, a proposed regulation -- even a regulation under a statute that does not permit the consideration of costs – could not become effective unless, among other things, the "benefits of the intended regulation justify its costs." And, notwithstanding the terms of the underlying statute, the agency would be required "in choosing among alternative regulatory approaches, [to choose] those approaches that maximize net benefits." Such a super mandate would effectively abrogate previously enacted Congressional decisions; one example that comes to mind is the requirement after 9/11 that airlines reinforce the steel in their cockpit doors. And such a super mandate might well delay such time-sensitive rules as those implementing the Migratory Bird Treaty, which must be issued on an annual basis and for which cost data has never been collected or analyzed. Congress can, of course, rewrite the Clean Air Act or the Occupational Health and Safety Act, or the National Traffic and Motor Safety Act, or any other existing authorizing legislation. But it should do so directly, not indirectly by creating a super mandate in the guise of promoting cost/benefit analysis and the consideration of that analysis in developing regulations.

It is important to emphasize that implementation of the Executive Order entails a great deal of judgment, even in those circumstances when costs and benefits are appropriate factors for consideration. As noted above, not all costs and benefits can be quantified and monetized. Yet those that cannot be are, according to the Executive Order (and common sense), "essential to consider." And there are not infrequently questions of disparate effects that should be taken into account, as well as other considerations that should properly come into play. With codification, the easily applied tests will inevitably take precedence over the judgment calls, which are more difficult to explain and document (especially in terms of the weight they are given). This becomes especially problematic if any such codification carries with it judicial review.

The issue of judicial review is difficult for me because I am a lawyer (who greatly respects our judicial system) and I am appearing before the Judiciary Committee. But I

must question whether the federal courts are the proper place to sort through cost/benefit analysis and its role in developing regulations. We are, as you know, a very litigious nation, and there is little disincentive for those who are disappointed at the agency level to take the matter to court. Judicial review of economic analysis will become yet another issue on appeal. Along with the lawyers debating whether the new decisional criteria trump the authorizing legislation, we can expect armies of competing economists with various theories about how to quantify or monetize the diverse direct and indirect effects of a proposed regulation. With Chevron and the hard look doctrine framing the inquiry, one would expect substantial deference to the agency's determinations, but there will nonetheless be substantial time and money (and the ensuing uncertainty) devoted to litigating whether benefits justify the costs and whether the alternative selected is the one that maximizes net benefits, among other concepts that will be placed before the court.

Thank you again for giving me an opportunity to speak to these issues. I look forward to any comments or questions you may have.