Insight

Utah Regulatory Sandbox Proposal Is First of its Kind

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Update: HB 217 was signed into law by Governor Spencer Cox on March 22, 2021.

EXECUTIVE SUMMARY

- The Utah state legislature is considering legislation to expand the state's regulatory sandbox program, which allows businesses to apply for exemptions to regulation.
- If this bill is enacted, Utah would become the first state to make such a program available for businesses of all industries.
- This expanded sandbox program aims to spur innovation by lowering regulatory barriers, with the broader goals of driving economic growth and encouraging companies to relocate to Utah.
- Although opponents of the bill cite concerns over weakening consumer protections, there are a number of mechanisms in place to ensure that businesses participating in the regulatory sandbox are not risking consumer safety.

INTRODUCTION

Last month, the Utah House of Representatives passed House Bill (HB) 217, which would expand the scope of the state's regulatory sandbox program beyond the financial services, insurance, and legal services industries. If the legislation is passed by the Senate and signed by the governor, it would be the first sandbox program of its kind to be available to all businesses, regardless of industry.

Regulatory sandbox programs allow businesses to apply for exemptions to existing regulations. Such regulatory-waiver programs are designed to spur innovation and drive economic growth. A number of states already have sandbox programs, including Florida,

West Virginia, Arizona, Nevada, and Wyoming. These states, however, generally restrict eligibility to businesses in the financial technology sector.

HOUSE BILL 217 PROVISIONS

The bill, entitled "Regulatory Sandbox Program Amendments," establishes the Office of Regulatory Relief (ORR) and gives the office administrative jurisdiction over the expanded sandbox program. The ORR requires businesses to cite specific regulations that they wish to be waived. In order for an exemption to be granted, the business must demonstrate how doing so will benefit consumers and promote innovation. Applicants will also have to identify potential risks that may arise due to the exemption, and what measures they will take to limit possible harms.

Following the ORR's receipt of an application, each effected agency will be required to review the waiver request to assess the costs and benefits of the proposed relief. Following review, each agency will be required to formally recommend whether to waive the specified regulations. If approved by the ORR, following consultation with every relevant agency, the business will be exempted from the given regulations for a duration of one year and may reapply for a one-year extension.

LEGISLATIVE BASIS AND DESIRED OUTCOMES

Legislators hope to do two things with this bill: to reduce the regulatory burden on potentially innovative companies, and to assess whether existing regulations are efficient and effective. Proponents of the legislation expect this policy to benefit the economy and consumers.

First, Utah hopes to drive innovation by reducing regulatory barriers for companies with high growth potential. In turn, improving the environment for innovation will result in more widespread economic benefits, such as job growth and increased tax revenue. Policy experts corroborate these outcomes, pointing to the inhibiting effects of regulation on economic growth. Moreover, in a study of 73 financial technology sandboxes across 53 countries, the World Bank Group found that "the overall evidence from outcomes observed from fintech sandboxes suggests that they have several benefits for regulators as well as for the financial sector ecosystem as a whole."

Consumers also stand to benefit from regulatory sandbox programs if adequate protections are upheld and the market is not overly distorted. Assuming that regulatory waivers do not unduly place consumers at risk, those transacting with sandbox participants will likely see benefits in the form of lower prices or increased access to otherwise-restricted goods and services. With that said, the ORR should work to develop specific metrics to measure the

success of program, accounting for factors such as consumer benefit, level of market competitiveness, and effects on social welfare.

It is equally important, however, to ensure that the market for a particular good or service is not monopolized as a result of regulatory exemptions. According to Brian Knight of the Mercatus Center, "Sandboxes present something of a paradox in that for any firm to want to use them, there needs to be a benefit to that firm, but any benefit to one firm in a market may be a disadvantage to all of that firm's competitors." While HB 217 calls upon the ORR to "consider whether a competitor to the applicant is or has been a sandbox participant" and to "weigh that as a factor in favor [of the applicant]," it does not include provisions to protect companies that choose to not participate in the program. Implementing such safeguards are vital for guaranteeing market competitiveness.

Another benefit of sandbox programs is their efficacy as a tool for regulatory evaluation. Sandbox programs put regulatory agencies in a constant dialogue with covered industries, allowing them to consistently evaluate the costs and benefits of their own rules. When a business receiving exemptions achieves high growth—while not harming consumers or distorting the market—the business's success indicates to regulators that they can reduce or eliminate the associated regulatory burden. Furthermore, the application review process offers regulators the opportunity to develop a deeper understanding of a particular innovation, allowing for more comprehensive regulatory activity in the future. In a context in which regulators are almost always lagging behind innovation, this educational component of the program may prove invaluable.

CONSUMER PROTECTION

Although opponents of sandbox programs cite concerns regarding consumer protection, HB 217 includes a number of mechanisms that seek to mitigate potential harms. Oversight and inter-agency coordination will still be necessary, however, to ensure that waiving regulations does not unnecessarily heighten risks for consumers.

Supporters of HB 217 say that regulations related to public safety and the safety of the consumer would not be waived, and that businesses "can't do anything that would be unsafe to the consumer, or fraudulent." That determination would be made by the ORR, which would weigh whether "the risk of harm to consumers is outweighed by the potential benefits to consumers." Certainly, regulatory exemptions granted through sandbox programs are not risk-proof, but the multistep review process will help insulate consumers from many potential dangers.

The bill also requires businesses to fully disclose their participation in the program to their

customers. This provision was put in place so that consumers are fully aware of any additional risks they may be assuming. This disclosure must include explicit enumeration of the potential harms detailed in the application review process, which includes the commentary of the associated regulatory agencies. Furthermore, the business participating in the sandbox program must inform the customer that it is not immune from civil liability or criminal prosecution for violations that fall outside the scope of the regulatory waiver.

Although HB 217 does not include provisions that require a participating business to have insurance coverage for potential harms to consumers, it does allow for sandbox protections to be removed at any time. The bill permits the ORR to "end a sandbox participant's participation in the regulatory sandbox at any time and for any reason, including if the director determines that a sandbox participant is not operating in good faith to bring an innovative offering to market."

While this bill will likely face opposition on the basis of consumer protection, it is unlikely that agencies would waive significant protectionist regulations and or that regulators would permit clear misbehavior among sandbox participants to persist for any extended period of time.

CONCLUSION

Although the regulatory sandbox bill is currently tabled, and will not be considered by the Senate until funds for the new office are appropriated, it seems likely the bill will be passed and signed into law. If enacted, the new program will create a regulatory environment in Utah more friendly to innovation and may serve as an example to other states considering the expansion of regulatory sandbox programs.