Insight

What Will "Modernizing" Regulatory Review Look Like?

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EXECUTIVE SUMMARY

- The Biden Administration is currently undertaking what will likely be the most significant changes to regulatory development since the early 1990s.
- Likely changes will make regulations appear more net beneficial than they would have previously and also centralize regulatory agenda setting within the Office of Information and Regulatory Affairs (OIRA).
- Modifications will likely include major changes to OIRA's regulatory impact analysis guidance to lower discount rates, include the social cost of carbon, and more explicitly account for distributional effects.
- The changes will be designed to help the administration use regulation to enact its policy agenda.

INTRODUCTION

For more than four decades, presidential administrations have conducted reviews of proposed and final regulations, including their effects, to ensure rules are consistent with the law and presidential priorities. The current form of regulatory review places this duty on the Office of Information and Regulatory Affairs (OIRA) – an office within the Office of Management and Budget (OMB) – and has been in place for almost 30 years.

A day-one directive from President Biden promises to "modernize" the existing process by shifting OIRA's posture from one of a neutral reviewer to more of a pro-regulation advocate. The effort promises to be the most significant modification to regulatory review since the Clinton Administration. While the outcome of this modernization remains to be seen, it is expected to consist of reforms that will appreciably change how benefits and costs are considered by federal agencies. This analysis considers the likely changes and their implications for rulemaking.

EXISTING REGULATORY REVIEW

The existing regulatory-review process was established by Executive Order (EO) 12,866, signed by President Clinton in 1993. The EO established a set of regulatory principles to drive federal rulemaking activity and entrusted OIRA to review regulations to "provide meaningful guidance and oversight so that each agency's regulatory actions are consistent with applicable law, the President's priorities, and the principles set forth in this Executive order and do not conflict with the policies or actions of another agency."

OIRA only reviews significant regulatory actions, which are those that meet one or more criteria defined in the EO. According to the EO, those criteria cover actions that:

> 1) Have an annual effect on the economy of $100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities;
>
> (2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;
>
> (3) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or
>
> (4) Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in this Executive order.

In its current role, OIRA does not proactively drive agency decisions to pursue certain regulatory initiatives. Instead, it provides balanced analyses of agency rules to help ensure they meet the principles of EO 12,866, including a fair presentation of a rule's expected benefits and costs.

At the heart of OIRA's reviews of benefits and costs is a guidance document called Circular A-4, which sets expectations for how agencies should conduct regulatory analyses (and by extension how OIRA will review them). This guidance also specifies discount rates of 3 and 7 percent for forecasting costs and benefits into the future. This circular was written in 2003 and has not been updated.

LIKELY CHANGES TO REGULATORY REVIEW

The day-one memorandum calling for OIRA review to be modernized suggested that the current process was unfit to address today's "serious challenges" – specifically the COVID-19 pandemic and subsequent economic downturn, systemic racial inequality, and climate change. It also called for the OMB Director to work with agencies to develop recommendations that should achieve four goals: revise Circular A-4 to bolster the benefits side of benefit-cost analysis, develop procedures to account for distributional effects of regulation to ensure that disadvantaged groups are not inappropriately burdened, allow for OIRA to be more proactive in regulatory initiatives, and reform how OIRA reviews significant guidance documents.

Based on the justification for the memorandum and the recommendations it aims to implement, it is evident that OIRA's role is to shift from a neutral analyzer of regulations to more of a champion of those actions. There are four main ways this shift will likely happen.

Revision of Circular A-4

Per the memorandum, Circular A-4 should be revised in a way to fully account for regulatory benefits that are difficult or impossible to quantify and to ensure that the circular does not have any harmful anti-regulatory or deregulatory effects. The memorandum does not, however, mention costs. This omission signals that the Biden Administration views the current circular as being an anti-regulatory document. This sentiment is curious, because it seems based on the premise that justifying regulatory action by identifying market failures and ensuring the benefits of regulation outweigh costs is an impediment rather than sound public policy.

The implications of this provision are profound. If the memorandum is read in the broadest terms, one could argue that any constraint on regulatory action beyond those found in statute is anti-regulatory. While it is

unlikely the Biden Administration will go that far since the memorandum reaffirms the principles of EO 12,866, it does give the administration wide latitude to revise Circular A-4 in a way that justifies extensive regulation, particularly on the serious challenges mentioned.

A likely change will be to the discount rates agencies use to estimate benefits and costs into the future. Progressive advocates argue that these current rates, 3 and 7 percent, are too high because of how far interest rates have fallen in the 18 years since Circular A-4 was written. Accordingly, one should expect to see a revised Circular A-4 reduce these values and go further by using declining discount rates on estimates far into the future on things such as environmental benefits. Lowering the discount rate and using declining discount rates will have the effect of increasing the net benefit calculation of regulations. As a result, it will be more likely that the benefits of proposed regulatory actions from the Biden Administration will appear to vastly outweigh the costs.

Incorporate the Social Cost of Carbon into Circular A-4

The Biden Administration has already taken one major step toward increasing the calculated benefits of its rules. In February, it raised the social cost of carbon (SCC), the estimate of the costs of greenhouse gas impacts, from about $7 per ton to roughly $50. The increase is primarily due to reversing a Trump-era change by incorporating the global costs of greenhouse gases as opposed to just the United States' costs. This increase also reflects a return of the SCC to levels established during the Obama Administration. The effect is that each ton of greenhouse gas emissions prevented will now generate approximately seven times more expected benefits than under recent calculations. This move alone will boost the benefits side of a regulatory benefit-cost analysis tremendously.

It is likely that the Biden Administration will go a step further and incorporate this cost estimate into a revised Circular A-4, thereby ensuring that every regulatory decision has to weigh its climate change impact. Since that impact will yield greater estimated benefits, more regulatory decisions can be justified on a benefit-cost basis.

Distributional Effects of Regulation

The existing Circular A-4 calls for agencies to describe the distributional effects of their actions in regulatory analyses, which considers instances when those bearing the costs of regulation and those benefitting from it are not the same (or vice versa). It does not, however, go into much detail on how these effects should be weighed. The Biden Administration may aim to get more prescriptive in how these effects should be applied. For example, in analyzing a hypothetical pollution emissions regulation, it could require that the benefits of reduced emissions in lower-income communities be valued at a larger amount than those same reductions in higher-income communities. While this approach makes sense given the reality that certain problems harm some communities more than others, the uncertainty around how to differentiate these values may lead to inflated estimates of benefits or costs.

OIRA's Role in Regulatory Advocacy

Under current practice, agencies largely send OIRA rules to review that the agencies themselves deem worthy of promulgation, generally making OIRA a passive actor in this process. There are instances where OIRA will send agencies "prompt letters" to push regulatory action, but those are relatively rare – with just 14 sent since 2001. The Biden Administration's memorandum is clear that OIRA should be more involved in encouraging agencies to pursue certain policy priorities. How this manifests itself is almost entirely up to how much the administration wants to centralize regulatory decision-making. One possibility is that OIRA takes a more

proactive role in setting an agency's regulatory agenda to ensure agencies address the serious challenges identified in the memorandum.

IMPLICATIONS OF LIKELY CHANGES

The day-one memorandum made no secret that the Biden Administration sees regulatory action as a primary means of enacting its policy agenda. The likely changes discussed above all play an important role in assisting that effort. The changes to Circular A-4, some of which may have merit, will nevertheless have the effect of increasing the estimated benefits of regulation. As a result, regulatory impact analyses will show more rules to be significantly net beneficial than they would have been previously. Accordingly, expect the Biden Administration to rely on these increased benefits to make the political and legal case for increased regulatory activity.

Relying on OIRA to be more proactive in helping agencies find areas to regulate also will clearly help the administration use regulations to advance its agenda, but it also will call into question OIRA's long-standing reputation of being a neutral analyzer of regulatory analyses. It is unclear how OIRA can fairly evaluate regulations and analyses of rules it actively worked with an agency to promulgate. The Biden Administration should address how OIRA will handle this new dual role in its final document detailing the administration's regulatory-review principles.

CONCLUSION

In the coming months, the Biden Administration is likely to make the most thorough changes to regulatory review since the Clinton Administration. Based on the memorandum calling for significant changes, it is clear that the new regulatory review will be designed to make regulation appear more net beneficial than it would have previously. It also will put OIRA more at the forefront of regulatory activity.