Obama, Ryan, and the Future of Regulatory Reform

An "upstream" approach to reform would reassert congressional authority, saving jobs and lowering compliance costs.

By IKE BRANNON and SAM BATKINS | *American Action Forum*

Washington, D.C. may have once been known for politicians ignoring the fiscal realities of its making, but it now appears awash in budget blueprints. Rep. Paul Ryan's (R, Wisc.) plan, "The Path to Prosperity," aims to cut $6.2 trillion in government spending over the next decade. President Obama's vision, as outlined in his April 13 speech at George Washington University, seeks to reduce the deficit by $4 trillion over the next 10 years.

How these competing visions for the role of government arrive at their reductions is drastically different. However, both plans provide few details about the future of our regulatory environment and the burden it imposes on businesses and consumers.

Ryan's plan does at least address the $1.75 trillion in estimated regulatory costs. It goes further to propose a streamlined regulatory process and measures to reduce America's dependence on foreign oil. President Obama's budget is mostly silent on regulatory reform, but his Executive Order 13563 and his budget for Fiscal Year 2012 shed light on the impact regulations have on job creation and destruction. Regardless of the budget plan put forth, U.S. businesses will suffer if Washington does not begin to regulate its regulators at the same time it tries to put its fiscal house in order.

Attempts at Reform

Although attempts at federal regulatory reform stretch back 65 years to the Administrative Procedure Act (APA), the results of "major" overhauls have produced only modest results and higher price tags for compliance. As George Washington University professor Susan Dudley has found, the cost of regulations has more than doubled over the past 20 years and the *Federal Register* continues to eclipse 70,000 pages a year.

What is missing? Previous reform attempts have all focused on "downstream" approaches by trying to rein in onerous regulations after they have been promulgated. One pitfall of this strategy is that agencies generally have a legal obligation to enforce laws passed by Congress and many independent regulatory authorities escape the scrutiny of reform efforts. Subsequent Congresses might try to curb administrative authority, but as long as each regulation withstands the "arbitrary and capricious" standard of the APA, federal courts are usually willing to uphold agency rules.

In a perfect world, Congress would simply stop passing laws that contain countless federal mandates and unchecked rulemaking authority. Absent this utopian reality, a better approach would focus "upstream," allowing Congress to restrict administrative agencies before giving them rulemaking authority during the legislative process. This could yield fewer and less costly regulations and, unlike the legislative veto, it would be constitutional. This approach would insert specific guidelines into all major legislation imposing federal mandates, including:

- requiring agencies to conduct reviews of regulations once implemented,
- demanding agencies rescind duplicative rules,
- placing a limit on the number of regulations an agency

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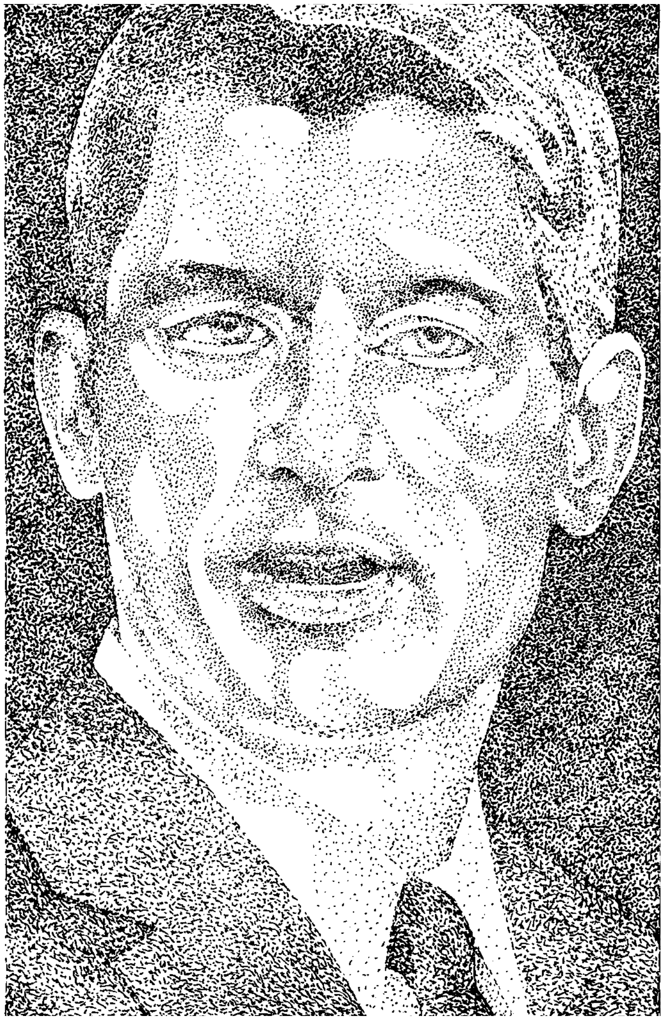

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could promulgate during implementation of a particular law,

- establishing regulatory "pay as you go" that would require the elimination of a rule whenever a new rule is adopted, and
- prohibiting new regulations where costs exceed benefits.

This "upstream" approach would end the regulation "whack-a-mole" strategy that has dominated the conversation for generations and instead focus on Congress placing limits on regulations before agencies implement federal mandates. The benefit of this approach is to (reasonably) restrain regulators before they exceed power given to them by Congress.

Ideally, a comprehensive reform package that implements each of these reforms would pass Congress. Absent that scenario, the House Committee on Rules would require that all major legislation include these reform proposals, similar to the recent move to include "Constitutional Authority Statements" in all legislation.

The Ryan Plan

Although not specifically designed to alter the regulatory environment, Ryan's budget proposal does envision some reform. For example, he would loosen "regulation[s] for the disposal and sale of federal property." This move is not a wholesale overhaul of the regulatory state, but it would generate federal revenue without raising taxes.

The Ryan plan also singles out the 2010 Wall Street Reform and Consumer Protection Act (better known as Dodd-Frank) for criticism, although Ryan's plan is silent on specifics, stating only the need to "revisit the financial-reform regulation enacted hastily last year and eliminate provisions that make future bailouts more likely." Given the massive direct compliance costs of Dodd-Frank and its hidden economic costs, paring back the most expensive and the least essential aspects of the legislation could aid businesses without harming market stability.

In addition, Ryan's plan adopts the "American Energy Initiative," a House Republican plan designed to increase domestic energy production. This proposal, while not directly related to broad regulatory reform, does seek to reduce the Environmental Protection Agency's ability to regulate greenhouse gases. Ryan's plan "scales back spending on government bureaucracies seeking to impose a job-destroying national energy tax."

The final regulatory piece of the Ryan plan would free up oil and natural gas leases on the Outer Continental Shelf (OCS) to encourage greater domestic energy production. This measure would not necessarily reform the Interior Department, the

Bureau of Ocean Energy Management Regulation and Enforcement, or the EPA, which are the agencies primarily responsible for OCS regulation, but it could ease the regulatory process for companies seeking to expand in the OCS.

The President's Plan

President Obama's FY 2012 budget said little about reform and proposes to greatly enhance the regulatory state. The EPA, Internal Revenue Service, and new financial regulatory agencies were among the recipients of larger federal outlays.

For its role in regulating greenhouse gases, the president allocated $46 million in funds for the EPA's new program. Though the agency's actual budget will decline from past levels, the administration viewed the greenhouse gas money as necessary to fund what could be the most massive undertaking in the agency's history: regulating 6,633 million metric tons of carbon dioxide and other gases.

Because of compliance standards contained in the president's health care overhaul, new burdens will be placed on taxpayers and the IRS, as the agency will require more auditors to determine whether individuals have adequate health insurance. The president's budget proposes to add more than 5,100 IRS agents to monitor compliance, which would bring the IRS's workforce to more than 100,000.

Furthermore, Dodd-Frank and its 243 new regulations place a burden on the Commodity Futures Trading Commission, not to mention financial firms. The administration proposed a robust 45 percent increase in spending for the agency, part of the budget to hire 534 new CFTC employees to implement Dodd-Frank.

In response to public criticism over the rapidly encroaching regulatory state, and perhaps in response to his party's poor showing in the 2010 midterm elections, President Obama wrote a January 18 op-ed in the *Wall Street Journal* explaining his executive order to reform the regulatory process. In it, he ordered a government-wide review of existing rules to "remove outdated regulations that stifle job creation and make our economy less competitive." The order has already been incorporated into the *Federal Register* and into Regulatory Impact Analyses (RIAs). As a result, the EPA no longer lists saccharin as a hazardous material and milk is no longer regulated under stringent oil spill prevention rules, which is expected to save dairy farmers approximately $146 million per annum.

EO 13563 is still in its infancy, so its consequences cannot yet be fully appreciated. The deregulatory moves as a result of the order have been promising but hardly earth-shattering. The president's measure largely copied the reform ideas of previous presidential orders, but given the current state of the economy, even piecemeal reforms are welcome.

Other Reform Proposals

In addition to the president's efforts, there has been no shortage of outside proposals to reform the regulatory state. Dudley, a former administrator of the Office of Information and Regulatory Affairs (OIRA), proposes to amend the APA to expand formal rulemaking. Because most federal rulemaking is informal (publication of a proposed rule, public comments, review of the final rule proposal, and publication of the final rule), an expansion of formal rulemaking would subject regulations to more scrutiny, such as trial-like hearings with witnesses and evidence standards.

Dudley also suggests amending the APA by changing the standard of review for administrative actions. Agencies are currently held to an "arbitrary and capricious" standard for rulemakings, meaning that as long as the agency can prove that there is at least a reasonable basis for the rule and the administration did not abuse its power, the rulemaking will stand. Not surprisingly, few administrative actions are struck down in court.

Raising the standard of review to the "substantial evidence" test ("such relevant evidence as a reasonable person would accept as adequate to support a conclusion") could yield more transparency. According to Dudley, "Substituting a substantial evidence test could motivate agencies to develop and provide better scientific and technical data and analysis in support of regulations."

Finally, several scholars have suggested a separate office to focus on reviewing "economically significant" regulations and other major rules. However, there are some issues related to the separation of powers when it comes to assigning the Congressional Budget Office or the Government Accountability Office to review administrative actions. The Office of Management and Budget, under the direction of the White House, reviews agency rules, but there are obvious conflict-of-interest issues associated with the administration reviewing its own regulations.

Dudley and others have proposed the creation of a wholly separate office under the legislative branch dedicated to reviewing regulations, which would "provid[e] an independent check on the analysis and decisions of regulatory agencies and OMB." The one drawback to this new office would be to treat "big government" with more government, but a credible case could be made that the office would save businesses and taxpayers money over the long term.

The "Upstream" Approach to Reform

Instead of attacking the regulatory state after it has promulgated rules required by legislation, an "upstream" approach that governs regulators before implementation could yield better results. In each bill imposing federal mandates, Congress would pass a regulatory overhaul that imposes five basic requirements on administrative agencies. Ideally, Congress would introduce a comprehensive regulatory reform package (similar to the Regulatory Flexibility Act or the Unfunded Mandates Reform Act) that would codify these requirements for agencies.

The first requirement would be to review existing regulations for inefficiency. EO 13563 already establishes such a requirement, but codifying it into law would ensure continuity. In addition to one-time reviews suggested by the president, subsequent cost-benefit analyses performed three and five years after implementation of a new rule would allow the public and subsequent administrations to more easily discern the efficacy of the regulation.

The second requirement would be to rescind duplicative rules. This is already done today, albeit in a haphazard way, by administrative agencies. The proposal would require agencies to review major legislation and determine if new laws would supersede past regulations, allowing for a continual review process where unneeded rules are scrapped.

The third requirement would be to limit the total number of regulations. This requirement is tricky for Congress to implement because administrative agencies generally have broad latitude to implement federal law. But Congress still has the power to pass legislation reforming the regulatory process by inserting language curtailing administrative action. Constitutional concerns (most notably separation of powers) would be allayed because the president would ultimately have to sign the legislation.

This measure places a cap on the number of regulations issued by administrative agencies during implementation of a new law. For example, Dodd-Frank, which may contain the largest number of federal mandates in recent history, was projected to produce at least 243 new rules. During conference report negotiations between the House and Senate, Congress would simply insert language capping the number of rulemakings that result from the legislation.

One possible benefit of this approach would be to restrain regulators before they exceed their grant of authority. If the cap proved to be woefully inadequate, the administration would ask for a simple increase. This way Congress controls not only the purse strings but also some procedure, without evolving into a super-regulatory body bogged down by mandating every facet of implementation.

The fourth requirement would establish a regulatory "pay as you go." There has been no formal legislative language released, but in a *Washington Post* op-ed last December 13, Sen. Mark Warner (D, Va.) suggested it would require "federal agencies to identify and eliminate one existing regulation for each new regulation they want to add … [requiring] agencies to produce a baseline catalogue of their existing regulations and a credible, quantifiable estimate of the economic impact for each one."

Senator Warner, who first floated this proposal, modeled it after Britain's "one-in, one-out" regulatory system. A way to improve on Warner's plan would be to require proportionate cuts in regulations, since if a new "economically significant" regulation is issued but is counterbalanced with the elimination of a relatively minor rule like the removal of saccharin from a list of hazardous substances, the nation's regulatory bill still becomes larger.

A problem with this proposal is its questionable constitutional status. Agencies are required by law to implement acts of Congress, and so a mandate that agencies choose which rules to eliminate would violate that obligation. Passing the burden of managing the regulatory state onto the agencies begets other questions. For example, after Dodd-Frank, what would the Securities and Exchange Commission do with the flood of new regulations and its previous obligations under Sarbanes-Oxley? If a new law imposed more clean air standards, would the EPA have the authority to remove other clean air regulations that have protected health and safety in the past?

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The final requirement would be to prohibit new regulations where costs exceed benefits. This would push agencies to arrive at the most cost-effective means of regulation. Even though there is widespread evidence that agencies game their cost-benefit analyses, a mandate from Congress and OIRA oversight of the analyses would increase scrutiny. This proposal would also require formal cost-benefit analyses and RIAs from the agencies during implementation.

Currently, as long as an agency believes a regulation will not cost more than $100 million, there is no formal requirement to submit the rule to OIRA or conduct a RIA. The new measure would mandate RIAs rather than allow agencies to skirt review by drastically underestimating costs.

Absent legislation implementing these reforms, Congress could insert these requirements into all major pieces of legislation that would impose unfunded or private-sector mandates. Thus, Congress could manage regulatory agencies through each piece of legislation, controlling bureaucrats one bill at a time, and before unaccountable agencies have the opportunity to promulgate rules that frequently survive the lenient "arbitrary and capricious" test in courts.

A New Regulatory Future

The tentative attempts to reform the regulatory process thus far have failed to curtail administration power and rulemaking excess. By inserting specific instructions for agencies to follow in legislation, an "upstream" approach could at least provide some predictability for Congress and, more importantly, for businesses. The administration will always spar with Congress over the keys to power, but this new approach could at least curtail regulatory overreach before jobs are lost and compliance costs skyrocket. R