

June 11, 2011

The Honorable Darryl Issa
Chairman
Committee on Oversight and Government Reform
House of Representatives
U.S. Congress
2157 Rayburn House Office Bldg.
Washington, DC 20515

The Honorable Jim Jordan
Chairman
Subcommittee on Regulatory Affairs, Stimulus Oversight, and Government Spending
House of Representatives
U.S. Congress
2157 Rayburn House Office Bldg.
Washington, DC 20515

Dear Chairman Issa and Chairman Jordan:

Your letter of May 16 to Mercatus Center General Director Tyler Cowen asks for examples of regulations “where it is believed a federal agency did not fully and effectively comply with the rulemaking process.” Economic analysis is a crucial component of the rulemaking process. A major portion of the Mercatus Center’s regulatory research evaluates the quality of the regulatory impact analysis that is supposed to inform agencies, the White House, and Congress when they make decisions about regulations and regulatory policy. As a result of our research, we have reached three main conclusions that may be of interest to the committee:

1. The extent and quality of regulatory impact analysis is insufficient to justify claims that the total benefits of recent regulations significantly exceed their costs.
2. The deficiencies are especially severe with respect to analysis of employment effects.
3. The situation is not likely to improve soon. The quality of analysis for “midnight” regulations rushed into place at the end of a presidential term is especially substandard.

Benefits and Costs of Regulations

Administrations of both parties regularly cite aggregate benefit and cost information as an indicator that they have adopted high-quality regulations whose benefits exceed their costs. For example, the recent Office of Management and Budget (OMB) *Draft Report on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local and Tribal Entities* includes a graph that compares the net benefits of major rules adopted through the third year of the Clinton, Bush, and Obama

administrations.¹ The graph shows \$14 billion in net benefits for the first three years of the Clinton administration, \$3.4 billion for Bush, and \$91.3 billion for Obama.

For the past 15 years, the Office of Management and Budget has provided Congress with reports on the combined annual benefits and costs of federal agency regulatory programs. All have reported benefits exceeding costs, although it is impossible to tell whether that is actually true. OMB's comparisons are inaccurate, for three reasons:

1. The figures are all drawn from agencies' own projections of the benefits and costs of regulations. The problem is the analyses are often incomplete and poor quality.
2. There is a vast disparity between the total number of major rules and the number of major rules with monetized benefits and costs. Fewer than half of all major regulations in any given year have monetized benefits and costs.
3. Benefit projections often involve significant uncertainties that the agencies' analyses fail to acknowledge.

Poor-Quality Analysis

The estimates used in OMB's reports are prepared by the agencies themselves, which means that the agencies are analyzing their own decisions. Research shows that agencies often make decisions early in the regulatory process and agency economists are pressured to make their analyses support those decisions.² In fact, agencies do an overall poor job of preparing economic analysis for new rules.

For more than three decades, executive orders have required executive branch agencies to conduct economic analyses (Regulatory Impact Analyses, or RIAs) of major regulations. Since 2008, the Mercatus Center at George Mason University has conducted a project known as the Mercatus Regulatory Report Card (Report Card) that evaluates federal agencies' economic analyses for proposed, economically significant regulations. The project also assesses the extent to which agencies claim to have used the analysis to make decisions about regulations.³ To date, more than 125 proposed rules have been evaluated.

Rulemakings evaluated by the Report Card receive a score ranging from 0 (no useful content) to 5 (comprehensive analysis with potential best practices) on each of 12 criteria based on requirements imposed under Executive Order 12866, as well as RIA guidelines laid out in OMB's Circular A-4.⁴

Unfortunately, the Report Card findings have not been reassuring. Agencies consistently do a poor job on economic analysis. For the period from 2008 to 2010, the average Report Card score was 28 out of a total of 60 points.⁵ That's an "F." In 2011, the average score was a disappointing 29. Analysis by other researchers in the past confirms the poor quality of federal regulatory impact analyses.⁶ This

¹ Office of Management and Budget, *Draft 2012 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities* (Washington, DC, 2012), http://www.whitehouse.gov/sites/default/files/omb/oira/draft_2012_cost_benefit_report.pdf.

² Richard Williams, "The Influence of Regulatory Economists in Federal Health and Safety Agencies" (working paper, Mercatus Center at George Mason University, Arlington, VA, July 2008).

³ Mercatus Center at George Mason University, *Regulatory Report Card*, <http://mercatus.org/reportcard>.

⁴ Office of Management and Budget, *Circular A-4*, September 17, 2003, http://www.whitehouse.gov/omb/circulars_a004_a-4.

⁵ Jerry Ellig and John Morrall, "Assessing the Quality of Regulatory Analysis" (working paper, Mercatus Center at George Mason University, Arlington, VA, December 15, 2010).

⁶ See, for example, Winston Harrington, "Grading Estimates of the Benefits and Costs of Federal Regulation: A

research indicates there are no significant differences in the quality of economic analysis across administrations, suggesting the problem is institutional, rather than just a case of poor management by one administration or political party.⁷

Some of the most problematic areas the Report Card identifies are a failure to define the systemic problem or market failure the agency sought to solve through the regulation, a lack of consideration of serious alternatives to the regulation being proposed, and a failure to set forth procedures to track the results of the regulation once it has been implemented.⁸ If an agency cannot define and demonstrate the existence of the problem it seeks to solve, the claimed benefits of the regulation are suspect. If an agency did not seriously consider alternatives, there is no way of knowing whether the agency adopted the most effective or cost-effective approach. And if the agency makes no effort at retrospective analysis, there is no way to tell whether the predicted benefits and costs actually occurred.

Small Number of Rules with Monetized Benefits and Costs

As OMB correctly notes, the number of rules with monetized benefits and costs is only a fraction of the total number of rules and the total number of major rules. Figure 1 shows that this has always been the case. In any given year, fewer than half of all major rules have monetized benefits and costs. For each year reported, the actual number of regulations that have quantified benefits and costs is only a tiny fraction of the overall number of final rules. There are typically 3,000 to 4,000 total rules added each year.

In fiscal year 2010 report there were more than 3,000 final rules, and only 18 of them had quantified benefits and costs. However, RIAs are only required only for economically significant rules, those with impacts greater than \$100 million in any given year. But agencies aren't even complying with that requirement. According to the Government Accountability Office, in fiscal year 2010 there were 104 major (economically significant) rules finalized; 66 of which are discussed in that year's OMB report to Congress and only 18 received a full analysis of benefits and costs. In FY 2011, the OMB report notes that there were 54 major rules. This is out of a total of 3,716 rules finalized that year, and only 13 had both quantified benefits and costs.⁹

Review of Reviews,” (Discussion Paper 06-39, Resources for the Future), October 15, 2006; and Robert W. Hahn and Paul C. Tetlock, “Has Economic Analysis Improved Regulatory Decisions?,” *Journal of Economic Perspectives* 22, no. 1 (Winter): 67–84.

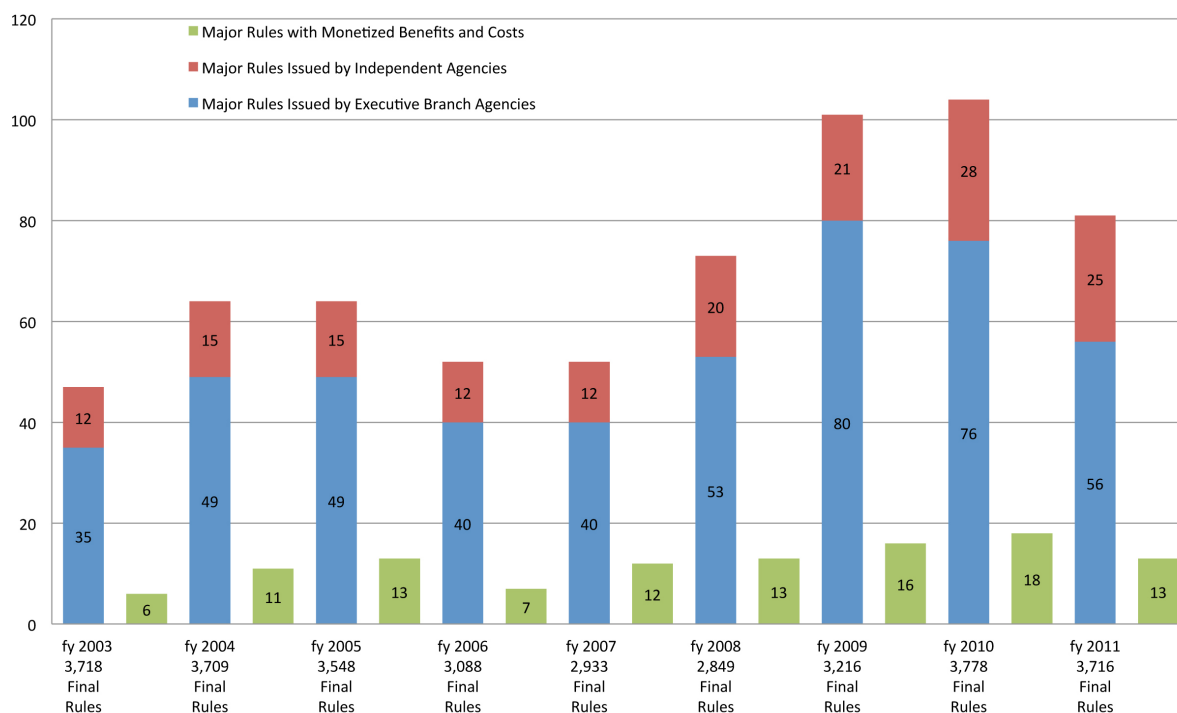
⁷ Jerry Ellig and P. McLaughlin, “The Quality and Use of Regulatory Analysis in 2008,” *Risk Analysis*, November 2011; and Ellig and Morrall, “Assessing the Quality of Regulatory Analysis.”

⁸ See, for example, James Broughel and Jerry Ellig, “Regulatory Alternatives: Best and Worst Practices,” *Mercatus on Policy*, February 21, 2012; Jerry Ellig and James Broughel, “Regulation: What’s the Problem?,” *Mercatus on Policy*, November 21, 2011; and Hahn and Tetlock, “Has Economic Analysis Improved Regulatory Decisions?”

⁹ Many of the economically significant rules are from “transfer” rules, which receive much less scrutiny from OIRA and so generally have poor or missing analyses. They often implement only precise congressional direction. However, these rules can have significant resource-allocation effects.

Figure 1: Minority of Major Rules Have Monetized Benefits and Costs¹⁰

Comparison of Final Rules With Monetized Benefits and Costs



Unacknowledged Uncertainties in Benefit Estimates

Many RIAs contain benefit estimates that are subject to a much wider range of uncertainties than the agency acknowledges. A broader range reflects more uncertainty in the calculations. When the estimates are presented with more certainty (e.g., narrower ranges of values or use of exact numbers such as “4,807 deaths prevented”), it misinforms decision makers about what is really known and not known. In the current report to Congress, the benefits of rules are taken from agency estimates that sometimes appear to be too narrow. Two examples are (1) a set of regulations that calculate benefits based on correcting presumed “bad” energy choices by consumers and (2) benefits associated with improving air quality, where the lower bound of benefits for some of the rules that OMB includes in its calculation of total benefits and total costs of the 2011 regulatory program may be much lower than acknowledged.

¹⁰ Data in the chart above are taken from GAO Congressional Review Act reports at <http://gao.gov/legal/congressact/fedrule.html>, except for the number of major rules with monetized costs and benefits, which is taken from the OMB report to Congress relevant to that fiscal year. A major rule is a rule “that may result in expenditures of more than \$100 million (adjusted for inflation) in any one year by State, local, and tribal governments, or by the private sector” (OMB, *Draft 2012 Report*, 8). Major rules issued by executive agencies were calculated by taking the total number of major rules for all agencies and subtracting the number of rules from independent agencies and government corporations. Final Rules represent the total number of final rules reported to GAO for each fiscal year (October through September).

Why are uncertainties important? First, decision makers should have the best possible information about what is known and what is not known. Decision makers must be able to accurately compare the costs of a policy option with the benefits. In some cases, when there is uncertainty in one or both measures, the ranges may overlap (e.g., upper bound costs exceed lower bound benefits) and that may affect the decision about which policy option to adopt. In other cases, as uncertainty is theoretically reducible by obtaining more information, the decision may be to gather more information. This would preclude making a policy decision until the information is obtained. The key point to all this is that managing (i.e., making decisions in the presence of) uncertainty is an exercise in value judgment. That is, it is not science: it is policy. Failure to reveal the full extent of uncertainty usurps the policy maker's role.

Conservative Risk Assessments

It has been widely known for more than 25 years that agencies tend to produce “conservative” estimates of risk.¹¹ OMB acknowledged as much in 1990: “Unfortunately, risk assessment practices continue to rely on conservative models and assumptions.”¹² This practice continues. Too frequently, rather than reporting the full range of possible risks, health and safety agencies are continuing a practice of nontransparency, only reporting upper bound risk estimates. The use of upper bound risk estimates inflates benefit estimates by overstating the extent of the risk the regulation seeks to reduce. When only conservative risk estimates are reported, the range of uncertainty reported is artificially attenuated. Given that OMB has known this for over two decades, it is inappropriate for OMB to support this practice by continuing to report these estimates in its annual report to Congress.

In fact, in a footnote in its 2012 draft report, OMB acknowledges that some of the assumptions used to estimate the benefit bounds of the fine particulate matter (PM) rule are insufficient, stating, “The wide range of benefits estimates for particle control does not capture the full extent of the scientific uncertainty in measuring the health effects associated with exposure to fine particulate matter and its constituent elements.”¹³ However, simply stating that in a footnote and then repeating the benefit ranges reported by EPA in this report does not shed any light on the true uncertainty.

In the most recent draft report, most of the benefits of regulation come from reductions in fine PM. In fact, PM reduction is a “co-benefit” that just happens to occur when other national ambient air quality standards are addressed, “accounting for 90% in most cases.”¹⁴ These benefits are based on a concentration-response relationship, which posits that reducing the concentration of particulate matter reduces mortality.

OMB has apparently disagreed with the EPA over these benefits for at least 14 years. In its 1998 report, OMB noted that the EPA report on the success of the Clean Air Act implied that “the average citizen was willing to pay over 25 percent of her personal income per year to attain the monetized benefits of the Clean Air Act.”¹⁵ Apparently, OMB was somewhat skeptical about this claim. For the 1997 National Ambient Air Quality Standards (NAAQs) rules on fine PM, OMB noted, “In this area, as in

¹¹ See, for example, Albert L. Nichols and Richard J. Zeckhauser, “The Perils of Prudence: How Conservative Risk Assessments Distort Regulation,” *Regulatory Toxicology and Pharmacology* 8 (1988).

¹² Office of Management and Budget, “Current Regulatory Issues in Risk Assessment and Risk Management,” Regulatory Program of the United States, April 1, 1990–March 31, 1991 (Washington, DC: Office of Management and Budget, 1990), 13–26.

¹³ Office of Management and Budget, *2011 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities* (Washington, DC, 2011), page 16, fn. 19.

¹⁴ Art Fraas, “The Treatment of Uncertainty in EPA’s Benefit Analysis of Air Pollution Rules: A Status Report,” *Journal of Benefit-Cost Analysis* (forthcoming).

¹⁵ Report to Congress on the Costs and Benefits of Federal Regulations, OIRA, OMB, 1998, 26.

others, the academic literature offers a number of methodologies and underlying studies to quantify the benefits. There remain considerable uncertainties with each of these approaches.”¹⁶

Perhaps more importantly, the National Academy of Sciences weighed in on the EPA’s reporting of uncertainty in 2002: “The committee agrees with the agency’s judgment that its current practice produces health benefits probability distributions that give ‘a misleading picture about the overall uncertainty in the estimates’¹⁷ In particular, the distributions suggest that there is less uncertainty, perhaps much less, than is actually present.”¹⁸

As fine PM benefits are the major source of benefits for the 2011 regulatory program, failure to report the full range of uncertainty results in a biased self-assessment of the administration’s program.

Forgone Private Benefits

OMB’s most recent draft report on the benefits and costs of regulations includes four final rules that have been justified using findings from behavioral economics:

1. Energy Efficiency Standards for Clothes Dryers and Room Air Conditioners, DOE, costs \$132 million (\$129–\$182) / benefits \$191 (\$169–\$310 million).
2. Energy Efficiency Standards for Residential Furnaces, Central Air Conditioners and Heat Pumps, DOE, costs \$538 million (\$475–\$724) / benefits \$940 million (\$719–\$1,766).
3. Energy Efficiency Standards for Residential Refrigerators, Refrigerator-Freezers and Freezers, DOE, costs \$84 billion (\$803–\$1.281 billion) / benefits \$1.837 billion (\$1,660–\$3,034 million).
4. Commercial Medium and Heavy Duty on Highway Vehicles and Work Truck Fuel Efficiency and Greenhouse Gas Emissions Standards, EPA/DOT/ costs \$496 million (\$331–\$496) / benefits \$2,654 million (\$2,150–\$2,564).

A forthcoming paper by Mercatus Center contributing authors Kip Viscusi and Ted Gayer examines the benefits of regulations that purport to address consumer and producer flaws in decision making, such as the ones listed above. They find that:

1. The vast majority of the benefits are derived by agencies claiming that energy-efficiency standards prevent consumers from inflicting self-harm by buying inefficient products (that is, private benefits to the individual, not society). The primary benefits are not social benefits, such as reductions in pollutant emissions, but energy savings to consumers—benefits consumers have chosen to forgo in favor of other revealed preferences.¹⁹ The private benefits are derived by agencies’ assuming the choices made by consumers are irrational and regulators are better able to decide what is in consumers’ best interest.

¹⁶ Ibid., 72.

¹⁷ EPA, Final Report to Congress on Benefits and Costs of the Clean Air Act, 1990 to 2010 (Washington, DC, 1999).

¹⁸ National Academy of Sciences, “Estimating the Public Health Benefits of Proposed Air Pollution Regulations,” Board on Environmental Studies and Toxicology, 133.

¹⁹ There are benefits from pollution reduction, but they are relatively small.

2. Other attributes of the product choices that consumers may value—such as safety, durability, performance, and style—are ignored in the RIAs.
3. There is virtually no empirical evidence in the RIAs demonstrating consumer irrationality for the regulated products. In fact, there is no systemic evidence of behavioral biases leading consumers to harm themselves. Therefore, agency-imposed preferences for efficiency over other attributes constitute a net cost for consumers.
4. Beyond federal mandates to alter the products to increase energy efficiency, few regulatory options (such as information provision) are seriously considered to address the assumed consumer irrationality.²⁰

The only way these rules pass a benefit-cost test is if one assumes, contrary to all economic theory, that restricting consumers' well-informed choices actually benefits consumers. Yet the economics literature and OMB guidelines suggest that restricting consumer choices is, in fact, harmful. There is no benefit to doing so, and restricting choice actually imposes a cost on consumers.

In fact, it is not clear that such standards should ever be promulgated, given the absence of a demonstrated market failure. Viscusi and Gayer note that OMB had voiced similar misgivings in Circular A-4, its guidance to agencies on the best practices in regulatory analysis, issued in 2003. OMB noted that there was no failure in the market for fuel economy: "Consumers or producers bear the costs of fuel-saving technology with their purchases, and they get the benefits of the enhanced fuel economy. They choose how much fuel economy to purchase."²¹

This kind of logic also occurs in some recent Food and Drug Administration (FDA) food labeling proposals. In the FDA's proposal to label calories in vending machine products, there is a presumption that there are "systematic biases in how consumers process information and weigh current benefits (from consuming higher calorie foods) against future costs (higher probability of obesity and its comorbidities)."²² Despite admitting that the private market is "robust and competitive" and that it does not appear that most consumers want to have calorie information on vending machines, the FDA concluded that consumers are too "present biased" because they are too "optimistic" about their future food choices (and therefore don't realize they *need* the information).

This is pure paternalism, reflecting the FDA's disagreement with consumers about what values consumers ought to have. Economic calculation of benefits, however, takes consumer preferences as the ultimate determinant of value. Asserting that a regulation produces benefits because consumers have the wrong values is a blank check to invent benefits out of thin air.

Another recent FDA proposal, to put warning signs on cigarette packages, uses the same logic.²³ Despite the fact that cigarette smoking has declined, and that smokers in general overestimate the risk of

²⁰ Ted Gayer and W. Kip Viscusi, "Overriding Consumer Preferences with Energy Regulations" (working paper, Mercatus Center at George Mason University, Arlington, VA, forthcoming).

²¹ Office of Management and Budget, *Circular A-4*. The quote from A-4 is: "These fuel savings will normally accrue to the engine purchasers, who also bear the costs of the technologies. There is no apparent market failure with regard to the market value of fuel saved because one would expect that consumers would be willing to pay for increased fuel economy that exceeded the cost of providing it."

²² DHHS, "Food Labeling: Calorie Labeling of Articles of Food in Vending Machines NPRM," Preliminary Regulatory Impact Analysis, Docket No. FDA-2011-F 0171, March 2011, 2.

²³ FDA, "Required Warnings for Cigarette Packages and Advertisements," *Federal Register* 75 (November 12, 2010): 69524–69565.

smoking, the FDA has concluded that smokers must be “irrational.” As Michael Marlow and Sherzod Abdukadirov analyze it,

However, the extent to which smokers understand the detrimental effects of smoking clearly impacts the effectiveness of stronger FDA health warnings. [Nicolas] Rodondi and colleagues recently concluded that smokers who viewed images of plaque accumulating inside their carotid arteries as part of an intensive smoking-cessation program were no more likely to improve their cardiovascular risk factors or quit smoking than others oblivious to the appearance of their carotids.²⁴ Assuming that paternalists view smokers as ill-informed about health risks associated with smoking, the randomized controlled trial study offers little support for the view that scare tactics promote the behavioral changes that paternalists seek. Despite dramatic reduction in smoking prevalence over time, it appears paternalists believe that irrationality persists as long as smokers persist in smoking.²⁵

These two issues demonstrate that there is more uncertainty in the benefit estimates than OMB acknowledges. If in fact the lower bounds on benefits for the energy and PM rules are substantially lower than is cited in the report, then the report provides a distorted view of the success of the 2011 regulatory program. As Robert Hahn and Cass Sunstein have written, “When the costs are high and the benefits low or nonexistent, something seems seriously amiss, especially because an absence of significant benefits signals a likely absence of significant savings in terms of health, safety, or the environment.”²⁶

Analysis of Employment Effects

Regulatory impact analyses are potentially an important tool for forcing a federal agency to consider a proposed regulation’s potential impact on the economy as a whole without paying undue attention to the welfare of private interests that may be lobbying for regulation. For the analyses to be genuinely helpful, however, agencies need to (1) offer considerably more transparency in the methodology, assumptions, and data used in each analysis, and (2) follow a single, consistent methodology throughout the analysis.

The frequent lack of transparency and inconsistent methodologies are particularly evident in agency efforts to estimate the likely employment impact of a regulation. The estimates are often inconsistent with the rest of the regulatory impact analysis, inconsistent with basic economic theory, and incomplete in that they do not consider all the likely employment effects. For example, they sometimes use employment multipliers from an often-cited paper by R. D. Morgenstern, W. A. Pizer, and J. S. Shih that estimates the difference between a possible increase in hiring to comply with the regulation and the lost employment from reduced sales due to higher prices.²⁷ These multipliers were estimated in the original paper for four specific industries using data primarily from the 1980s. They should not be used for current analyses on different industries. Additionally, this approach implicitly assumes that the increase in hiring for regulation compliance is an economic benefit, which is inconsistent with a standard benefit-cost analysis.

²⁴ Nicolas Rodondi et al., “Impact of Carotid Plaque Screening on Smoking Cessation and Other Cardiovascular Risk Factors: A Randomized Controlled Trial,” *Archives of Internal Medicine*, published electronically January 23, 2012, <http://www.ncbi.nlm.nih.gov/pubmed/22269590>.

²⁵ Marlow, Michael and Sherzod Abdukadirov, “Fat Chance: An Analysis of Anti-Obesity Efforts,” (working paper, Mercatus Center at George Mason University, Arlington, VA, 2012), 8.

²⁶ Robert Hahn and Cass Sunstein, “A New Executive Order for Improving Federal Regulation? Deeper and Wider Cost-Benefit Analysis” (working paper, John M. Olin Law and Economics Center 150 2D Series, University of Chicago Law School, Chicago), 2002, 1. http://www.law.uchicago.edu/files/files/150.CRS_Cost-Benefit.pdf

²⁷ R. D. Morgenstern, W. A. Pizer, and J. S. Shih, “Jobs versus the Environment: An Industry-Level Perspective,” *Journal of Environmental Economics and Management* 43, no. 3 (2002): 412–36.

For example, the EPA's regulatory impact analysis on the Toxics Rule regulation for 2016 used this methodology to find a net gain of 9,000 jobs.²⁸ What the analysis really found was that the regulation would require the hiring of about 30,000 new compliance workers at a cost of 21,000 production worker jobs and, at the same time, would raise the cost to consumers by \$8.4 billion. The cost of hiring those compliance workers is part of the \$8.4 billion cost to consumers, not a benefit. The total cost to consumers works out to more than \$900,000 per net job created.

The likely employment effects that are generally not even considered in regulatory impact analyses include:

- The negative impact on economy-wide employment from a loss of consumers buying power due to the higher prices of regulated products or services.
- The economic cost of the unemployment created by the regulation. The typical analysis looks at the long-run economic effect after all factors of production have found new long-run employment and completely ignores the economic cost of temporary unemployment. However, this cost can be significant, especially now when the United States is in a period of high unemployment.²⁹
- The indirect dynamic effects of regulation that can slow economic growth and therefore employment. These include the possible negative impact on competition, a decreased ability to develop and market new products, and lower levels of innovation. As the Swedish Agency for Growth Policy Analysis finds, these indirect costs "are considerable and probably more important than the direct costs related to complying" with regulations.³⁰

Without substantial improvement in theory and implementation, we cannot be confident that agency analysis of employment effects of regulations provides much meaningful information.

Midnight Regulations

It is possible that the quality and use of economic analysis by regulatory agencies could actually deteriorate during the remainder of this year due to a phenomenon scholars call "midnight regulation." The term "midnight regulation" refers to the last-minute regulatory activity at the end of a presidential term, between Election Day and Inauguration Day. Research indicates that the number of proposed and final regulations surges during the midnight period, and the magnitude of the midnight surge depends on the presidential election outcome.

A higher proportion of *Federal Register* pages get published during midnight months than during the other months of the election year, indicating that more of the federal government's regulatory activity occurs in the midnight months. The proportion is 17 percent higher during midnight months than during non-midnight months. It increases to 18 percent when the administration is leaving office and 20 percent

²⁸ Environmental Protection Agency, *Regulatory Impact Analysis of the Proposed Toxics Rule: Final Report* 1-1 (2011).

²⁹ Alan B. Krueger and Andreas Mueller, "Job Search and Job Finding in a Period of Mass Unemployment: Evidence from High-Frequency Longitudinal Data," forthcoming in *Brookings Papers on Economic Activity* (2011).

³⁰ Swedish Agency for Growth Policy Analysis, "The Economic Effects of the Regulatory Burden," Report 2010:14. The study analyzes how regulations can create barriers to entry and market rigidities across a sample of countries that includes the United States.

when control of the presidency switches parties.³¹ Thus, midnight periods typically have a regulatory surge even when a president gets reelected, but the surge is larger when a president is leaving office.

Midnight regulations are of concern for two related reasons: (1) lack of political accountability, and (2) the poor quality of regulatory analysis.

Lack of Accountability

In the quarter following Election Day, an outgoing administration faces few constraints from either Congress or voters. Lack of political accountability provides an opening for both the president and his political appointees in the executive agencies to push through sweeping, controversial regulations that would normally arouse considerable opposition.³² Outgoing administrations typically use this period to pass regulations reflecting their preferences that bind the following administrations to a particular course of action. Once finalized, regulations are hard to repeal.

Since the turnover among political appointees is the highest during the change in administration, it produces the greatest regulatory surge. Yet even if an incumbent president is reelected, a number of agency heads depart the administration, producing a mini-surge.³³ Since these appointees are leaving and the president is limited to two terms, accountability is diminished even if the president has just been reelected.

Within the administration, the Office of Information and Regulatory Affairs (OIRA) provides some accountability by reviewing significant regulations and their accompanying RIAs. However, OIRA's ability to provide effective oversight during the midnight period is limited, since the regulatory surge is rarely accompanied by a commensurate increase in OIRA's budget or staff.³⁴ The number of economically significant rules submitted for OIRA review during midnight months increases by approximately 7 percent, resulting in shorter review times. While an average review time lasts about 50 days, for midnight regulations it drops to 25 days—half the normal review time.³⁵

Low-Quality Regulatory Analysis

The quality of analysis for some regulations drops during the midnight period. The Mercatus Center's Regulatory Report Card covers 2008, so it evaluated the quality and use of analysis for the Bush administration's midnight regulations adopted in 2008. The Bush administration attempted to curtail midnight regulations; a memo from the chief of staff instructed agencies to propose regulations before June 1 and finalize them by November 1.

Figure 2 compares total Report Card scores for prescriptive midnight regulations and other groups of regulations. "Prescriptive" regulations contain mandates or prohibitions, as opposed to

³¹ Veronique de Rugy and Antony Davies, "Midnight Regulations and the Cinderella Effect," *Journal of Socio-Economics* 38, no. 6 (December 2009): 886–90.

³² Jerry Brito and Veronique de Rugy, "Midnight Regulations and Regulatory Review," *Administrative Law Review* 61, no. 1 (2009): 163–96.

³³ Jay Cochran, "The Cinderella Constraint: Why Regulations Increase Significantly During Post-Election Quarters," (working paper, Mercatus Center at George Mason University, Arlington, VA, March 2001), http://mercatus.org/sites/default/files/publication/The_Cinderella_Constraint%281%29.pdf.

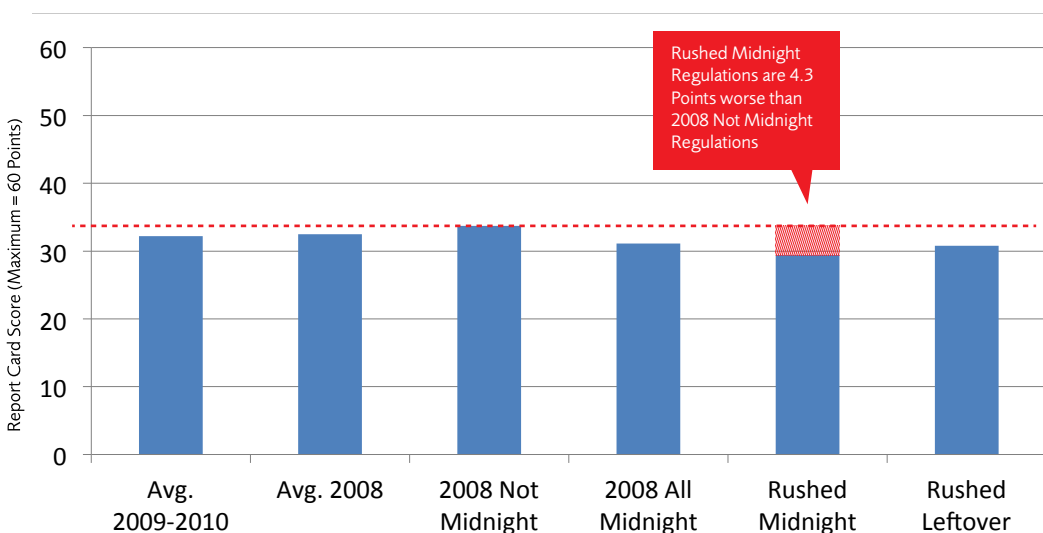
³⁴ Brito and de Rugy, "Midnight Regulations and Regulatory Review."

³⁵ Patrick A. McLaughlin, "The Consequences of Midnight Regulations and Other Surges in Regulatory Activity," *Public Choice* 147 (2011): 395–412.

“budget” regulations that implement federal spending or revenue collection programs.³⁶ Several facts are obvious from the graph:

- Midnight regulations have lower Report Card scores than other regulations proposed in 2008 or in 2009–10.
- Rushed midnight regulations—that is, midnight regulations proposed after the Bush administration’s self-imposed June 1, 2008, deadline—have much lower scores.
- Some regulations proposed after June 1 were not finalized by the Bush administration but instead left for the Obama administration to finalize (“rushed leftover regulations” in the chart). These also had lower scores. Either these were intended to be midnight regulations but the clock ran out before they could be finalized or less effort went into their analysis because they would be left for the next administration to finish.

Figure 2: Total Report Card Scores for Midnight and Other Regulations



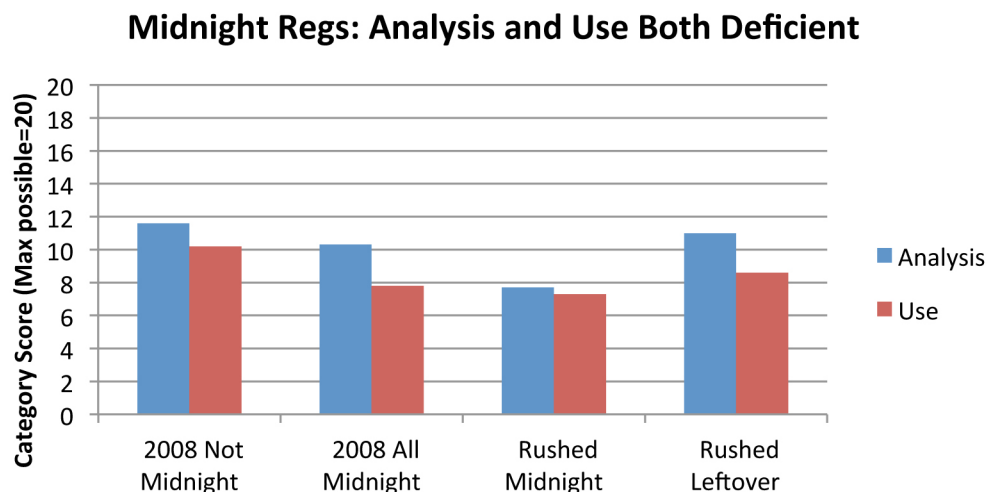
The Report Card divides score criteria into three categories: Openness, Analysis, and Use. On Openness, midnight and rushed midnight regulations had about the same scores as other regulations—about 11 to 12 out of 20 possible points. Figure 3 shows, however, that midnight regulations have lower-quality analysis and less use of analysis than other regulations. Rushed leftover regulations have about the same Analysis scores as non-midnight regulations, but lower Use scores.

If history repeats itself in 2010, the regulations most likely to have lower-quality analysis and less use of analysis will be those proposed in the second half of 2012. The average Regulatory Report Card score for 2008–10 is approximately 32 out of a possible 60 points—hardly stellar. The fact that scores for

³⁶ The Report Card evaluated budget regulations for 2008 and 2009 but not for subsequent years. Since policy makers are most concerned about prescriptive regulations, all the following charts and figures omit budget regulations.

rushed midnight regulations are even lower suggests that these regulations may be based on especially deficient analysis.

Figure 3: Analysis and Use Scores for Midnight and Other Regulations



Conclusion

When federal agencies conduct economic analysis of regulations, they often fail to comply with requirements first enunciated in executive orders more than 30 years ago and reaffirmed by presidents of both political parties. As a result, agency estimates of the benefits, costs, and employment effects of regulations are often fragmentary and unreliable. Contrary to OMB reports, the federal government cannot derive firm conclusions about the net effect of all regulations or the specific effects of some individual regulations based on the data presented by agencies. Federal agencies have not fulfilled their rulemaking duty adequately, given the critical flaws in analyses of regulatory costs and benefits, as well as employment effects. Moreover, these flaws are further amplified by the incentives faced by administrations at the end of a presidential term. Based on these long-standing factors, we see little likelihood of improvement in the remainder of the year. Removing institutional barriers to the production and use of high-quality regulatory impact analysis should remain a priority for Congress and the president.

Sincerely,

Dr. Richard A. Williams, Ph.D.
Director for Policy Research

Cc: The Honorable Elijah Cummings, Ranking Minority Member,
Committee on Oversight and Government Reform

The Honorable Dennis Kucinich, Ranking Minority Member,
Subcommittee on Regulatory Affairs, Stimulus Oversight and Government Spending