



Risk in Perspective

Regulatory Reform: Moving Forward in the States

"Regulatory reform has not been confined to the level of government."

Lisa Greene, HMS Media Services



John D. Graham, Ph.D.
Center Director

Lisa Greene, HMS Media Services



Kristin Loevel
Research Assistant

In recent years, it has become clear that the high costs of federal regulations are not always justified by public health or environmental benefits, and the public and private sectors are devoting substantial resources toward reducing speculative or insignificant risks. In response to these concerns, the U.S. Congress has actively considered regulatory reform proposals which would require federal agencies to analyze the risks, costs and benefits of new environmental regulations. At the same time, there has been discussion of a devolution of power to the states, because states agencies are more knowledgeable about regional and local environmental problems and thus better able to establish budget and policy priorities.

Indeed, according to an August 1996 survey we conducted, regulatory reform has not been confined to the federal level of government.

Partially stimulated by the regulatory reform debate in the 104th Congress, many governors and state legislatures are now expressing interest in the reform of state environmental policies based on the principles of risk analysis and risk management. We believe these efforts are interesting and important, because they have the potential to change the development and implementation of both state-specific regulation and those federal regulations for which states are given more authority.

By telephone, we surveyed officials in 35 state governments to determine: (1) the extent of reform activity since 1990; (2) any use of risk assessment, cost-benefit analysis, and comparative risk assessment specifically; and (3) the perceived barriers to more widespread adoption of risk-based reforms at the state level. In this issue of **RISK IN PERSPECTIVE**, we present three state cases, our general findings, and recommendations for further state-level reforms.

REGULATORY REFORM CASES

New York. In 1995, Governor George Pataki signed Executive Order 20, formally establishing the Governor's Office of Regulatory Reform (GORR) and the structure for how regulations are reviewed. The Director of the Office, along with four other senior cabinet advisors, evaluate

both current and proposed rules using several criteria, including whether the rule (1) will produce public benefits which outweigh the costs for affected parties; (2) "is based on credible risk assessments, using recognized standards, of the degree and nature of the risks which may be regulated, including a comparison with the everyday risks familiar to the public;" (3) is based on sound scientific and economic information; and (4) favors market-oriented solutions over command-and-control approaches. Interestingly, under an existing state statute, state agencies were already required to consider costs and benefits in the rulemaking process, but the provision had been often ignored. In order to help agencies comply with the new, enforceable cost-benefit requirement, GORR created the "Cost-Benefit Handbook: A Guide for New York State's Regulatory Agencies."

North Carolina. On December 1, 1995, legislation became effective requiring an economic analysis for all proposed rules with "an aggregate financial impact on all persons affected of at least \$5 million in a 12-month period." The economic analysis must describe the affected persons, estimate their compliance expenditures, and explain how the estimates were calculated. The analysis may be conducted by the relevant state agency and approved by the Office of State Budget and Management (OSBM), or the analysis may be done by the OSBM alone. The Department of Environment, Health, and Natural Resources (DEHNR) is one of the agencies which chose to conduct its own analyses, believing that no one else understands the consequences of a rule change as well as those who administer the rule. Since the DEHNR staff includes few economists, the agency developed computer software to coach rulewriters through an economic analysis. The software, through tutorials, examples, and series of structured queries, translates the knowledge of program personnel into an economic framework of impacts and costs.

Virginia. On June 21, 1994, Governor George Allen signed two executive orders in an attempt to reduce the burden of regulation on Virginia citizens and businesses. Executive

Harvard Center for Risk Analysis
Harvard School of Public Health
718 Huntington Avenue
Boston, Massachusetts 02115

617 432-4497
www.hsph.harvard.edu/organizations/hcra.html



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FURTHER READING

R Whisnant and D Dewitt Cherry, "The Economic Analysis of Rules: Devolution, Evolution, and Realism," *Wake Forest Law Review* 31,3 (1996): 693-743.

PEER REVIEWERS

George Gray, Ph.D.
Cary Coglianese, M.P.P./J.D./Ph.D.

FOR MORE INFORMATION

For a copy of the full report on state regulatory reform initiatives, contact the Harvard Center for Risk Analysis by mail at 718 Huntington Avenue, Boston, MA 02115, or by phone at (617) 432-4497.

Order 13 requires the Virginia Department of Planning and Budget (DPB) to provide an economic impact statement for all proposed and existing rules. The role of DPB is unique in this regard—Ph.D. economists at the DPB conduct the economic analyses, and promulgating agencies only prepare fiscal analyses. Executive Order 15 directs agencies to review existing rules and regulations and recommend to their respective cabinet secretaries which should be amended or repealed. Under both executive orders, regulations are evaluated to ensure they are essential to the public's health, safety, or welfare and that they are clear and readily understandable by regulated entities. Along with these executive orders, Governor Allen also encouraged the state legislature to pass a law which would make economic impact analysis a statutory requirement. Legislation did pass in 1994. Then, in 1995, the state legislature expanded the economic impact statement to include an assessment of the impacts on private property and localities.

GENERAL FINDINGS

New York, North Carolina, and Virginia are not the only states with regulatory reform initiatives. Officials in 25 states reported that there is currently a regulatory reform effort in their state. Most defined regulatory reform as either a comprehensive review of existing regulations, the establishment of new criteria for the promulgation of regulations, or the streamlining of the permit process. Other officials discussed comparative risk assessment projects, performance partnership agreements with the U.S. EPA, and the development of environmental management systems for industry self-audits. Nineteen of the 25 state regulatory reform efforts are executive branch initiatives, and about half of those were signed by governors in executive orders. Only a few of the reform packages were legislative initiatives. However, officials in 19 states acknowledged that their state legislatures had considered regulatory reform bills in the last two years.

Economic analysis seemed to be more prevalent in state environmental agencies than risk assessment. Officials in 25 states reported that their state agencies have used risk assessment in environmental regulatory decisions, but, of those, only seven states actually require the use of risk assessment. In comparison, officials in 25 states said that state agencies are required to analyze the costs of new environmental regulations. Of those, eleven states require an actual cost-benefit analysis, or a direct comparison of costs and benefits, including Arizona, Kansas, Louisiana, Massachusetts, Michigan, Mississippi, New Jersey, Pennsylvania, and Washington. Interestingly, at least 27 states have executive orders or statutes which direct agencies to justify regulations which are more stringent than

federal standards, and several require a cost-benefit analysis to be included in the justification.

Among the states with regulatory reform efforts as well as those without, "lack of resources" was perceived to be the most significant barrier to the adoption and/or implementation of cost-benefit and risk assessment requirements. State officials feel they lack the funds, staff, and data to conduct extensive analyses. Officials also expressed concern that policy makers do not fully understand the uses and limitations of risk assessment and cost-benefit analysis, particularly with regard to uncertainty. Due to significant data gaps, risk and cost estimates are often uncertain and even subjective, and officials fear any estimate will be a target for criticism by both policy makers and interest groups.

POLICY RECOMMENDATIONS

- To conduct risk assessments and economic analyses, state agencies need data and trained staff to analyze that data. Governors and legislatures should ensure that agencies have the necessary resources to meet new cost-benefit and risk criteria.
- Policy makers should also educate themselves about the potential uses and limitations of risk assessment and cost-benefit analysis. Specifically, governors, legislators, and agency heads should understand and appreciate the uncertainty involved in risk, cost, and benefit estimates, and, for example, feel comfortable receiving estimates as ranges rather than as point estimates.
- Practitioners, such as program personnel and rulewriters in state agencies, need better training in risk assessment and economic analysis. State governments should partner with state universities and with each other to provide written guidance and training workshops on the mechanics of these tools.
- Academic institutions, research centers, consulting firms, and/or the federal government should be involved in developing simple risk, comparative-risk, and cost-benefit models which could be used by state agencies with minimum data, limited trained staff, and modest funds.
- Finally, policy makers should consider how to measure the performance of regulatory reform efforts. Many states have created new, often more complex, processes for the promulgation of regulations, but have not determined how results will be measured and what would constitute success or failure. Attention to such details could transform the current reform efforts into a longer term process of continuous review and innovation in state environmental policy.