Regulatory Alert

Regulatory Insights

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Analysis of Regulations: OMB Circular A-4 Cost-Benefit Updates

KPMG Insights:

— *First updates to OMB Circular A-4 in 20 years.*

— *Updates respond to Administration directive to promote public health and safety, economic growth, social welfare, racial justice, environmental stewardship, human dignity, and equity through the regulatory review process.*

— *Heightened attention to regulations impacting "technological advances, demographic changes, changes in the economy, or alterations to the climate."*

— *Geared to agencies but companies may consider any changes for cost/benefit analysis of proposed/final regulatory impacts to relevant individuals/companies/sectors.*

The Office of Management and Budget (OMB) issues updates to its Circular A-4 guidance on federal agencies' regulatory impact analyses for "significant" rulemakings (as defined in Executive Order (EO) 12866, September 1993, as amended). The revised guidance responds to EO 14094 (April 2023) and a January 2021 Presidential Memorandum directing modernization of the regulatory review guidelines. Prior to these updates, Circular A-4 has not been updated since its original release in2003. The updated Circular supersedes and rescinds the previous version.

The updates are intended to "aid agencies in their analysis of the benefits and costs of regulations" and focus on several key aspects of regulatory impact analyses, including:

Guidance Section	Key Updates
Scope of Analysis	— *Spatial scope*. Recognizing the increasing interconnectedness of the global economy and increasing international regulatory cooperation, primary analyses of regulations should focus on effects experienced by U.S. citizens and residents, but in certain contexts, analyses of the effects experienced by non-citizens residing abroad may be "appropriate" (e.g., providing proxies for effects on U.S. citizens and residents that are otherwise difficult to estimate, regulating an externality on the basis of its global effects, international or domestic legal obligations). — *Temporal scope*. The selection of a time horizon for analysis should be long enough to encompass all "important benefits and costs" that are likely to result from a regulation.
Developing Analytic Baselines	— When choosing an analytic baseline, consideration should be given to transparency, data availability, empirical evidence about current conditions, and related ongoing and anticipated trends. The baseline should attempt to reflect the timing of interrelated policies and relevant final and proposed rules that are reasonably certain to be finalized before the rule under

	consideration is finalized. Agencies are encouraged to consider the likely paths of future government programs and policies when relevant and appropriate, either reflecting them in the primary or in a supplemental baseline. — An "appropriate" standard (i.e., no-action) baseline is not a description of the status quo, but rather an "analytically reasonable forecast of the way the world would look absent the regulatory action being assessed, including any expected changes to current conditions over time." "Particular attention should be paid to ways in which conditions will change absent the regulation," in areas such as "technological advances, demographic changes, changes in the economy, or alterations to the climate."
Identifying the Need for Federal Regulatory Action	— The need for a regulation should be described qualitatively and (when applicable) quantitatively. The statements about the need for regulatory actions should be supported by evidence in the regulatory analysis. — Examples of various needs for federal regulatory action have been expanded and clarified, and include: – Correcting market failures (e.g., externalities, common property resources, club goods, public goods, market power, asymmetric and imperfect information) – Addressing behavioral biases – Improving government operations and service delivery – Promoting distributional fairness and equity – Protecting civil rights and civil liberties as potential needs for federal regulation.
Additional Benefit and Cost Estimates	— The term "ancillary benefits and countervailing risks" has been revised to "additional benefits and costs". The guidance encourages agencies to consider additional benefits (a favorable impact unrelated to the main purpose of the regulation) and costs (an adverse impact that occurs as a result of the regulation not already accounted for) and emphasizing that estimate should be quantified and monetized if possible. — The guidance includes discussion of various aspects and methods of valuing benefits and costs, including revealed preference methods, stated preference methods, benefit-transfer methods, general equilibrium analysis, and accounting for non-monetized effects.
Transfers	— Agencies may opt to use either of two approaches to accounting for transfers in regulatory analysis, both of which will result in equal sums of transfers: – Accounting for Transfers Separately from Benefits and Costs – Accounting for Transfers as Offsetting Benefits and Costs. (Note: The guidance states this approach may be useful when conducting a distributional analysis, allowing for more transparent representation of the underlying redistribution of resources). — The guidance includes a discussion of the marginal cost of public funds (MCPF), which is an estimate of the distortionary cost of taxation, when analyzing changes in government revenues and expenditures caused by regulations. The updates recommend that agencies avoid attributing future changes in the tax system to regulations that affect federal revenues or expenditures.
Distributional Effects	Guidance is provided on undertaking distribution analysis when agencies "choose to do so." Detailed distributional analyses estimate how benefits, costs, and transfers will likely be experienced across the population and economy in various ways (i.e., income groups, race or ethnicity, sex, gender, disability, occupation, geography, firm size, industrial sector). Agencies may apply weights to the benefits and costs accruing to different groups. Targeted analysis of regulations that have the most significant distributional consequences are encouraged (including distinctions between parties that experience the benefits of the regulation and those that bear the costs), allowing for a more informed assessment of the implications of different policy options.

Treatment of Uncertainty	— Agencies are encouraged to: – Develop probability distributions for key elements. – Use a variety of analytical approaches, including sensitivity and formal probabilistic analyses. – Use new methods to analyze uncertainty, in certain cases. — Emphasizes use of summary statistics or figures in measuring uncertain outcomes; accounting for risk preferences, including risk aversion, when valuing uncertain outcomes; and utilizing certainty-equivalent valuations to compare uncertain outcomes. — Testing the sensitivity of regulatory outcomes to "plausible" alternative assumptions or methods. If the value of net benefits changes from positive to negative (or vice versa) or if the relative ranking of regulatory options changes with alternative plausible inputs, approaches, or assumptions additional analysis should be considered.
Discount Rates	— The existing method of estimating the social rate of time preference is retained but has been updated using data on the 30-year average of the yield on 10-year Treasury marketable securities from 1993 to 2022, resulting in an updated estimate of the social rate of time preference of 2.0 percent, equal to a real rate of 1.7 percent per year to which OMB adds a 0.3 percent per-year rate to reflect inflation as measured by the personal consumption expenditure (PCE) inflation index (down from the 2003 rate of 3.0 percent). This number will be updated every three years and published as an appendix to the Circular. (The social rate of time preference corresponds to the rate at which society is willing to trade current consumption for future consumption. — An extensive discussion on discounting over the long term is provided, including presenting different approaches to estimating long-term discount rates (e.g., using an updated schedule of default discount rates spanning a 150-year horizon, addressing special ethical considerations related to comparing benefits and costs across generations). — The guidance elaborates on accounting for capital and risk in regulatory impact analysis, including the importance of considering capital displacement and resource effects. The update also introduces an alternative approach based on the shadow price of capital that seeks to improve accuracy in capturing regulatory effects on capital flows and distributional effects on different population. — The use of private discount rates versus social discount rates when modeling private behavior in regulatory impact analysis is considered, including clarification of the need to use appropriate private discount rates faced by relevant populations before applying the social discount rate to ascertain the social benefits and costs of a regulation.

Effective Dates. The effective dates of the updated Circular are:

— March 1, 2024, for regulatory analyses in support of proposed rules, interim final rules, and direct final rules submitted to OMB after February 29, 2024.

— January 1, 2025, for regulatory analyses in support of draft final rules submitted to OMB after December 31, 2024.

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