

Comment to the Office of Management and Budget: Proposed OMB Circular A-4, “Regulatory Analysis”

**Document ID OMB-2022-0014-0001
Federal Register Number 2023-07364**

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June 20, 2023

**Submitted through the regulations.gov portal at
<https://www.regulations.gov/commenton/OMB-2022-0014-0001>**

This comment paper addresses the revision of guidelines for regulatory benefit/cost analysis by federal agencies, as proposed by the Office of Management and Budget in its draft Circular A-4 of April 6, 2023.¹ For the reasons discussed below, the draft guidelines are fatally flawed analytically, and should be withdrawn. This comment is organized as follows:

Summary

- I. The Central Implication of the OMB Rationales for Regulation.
- II. Fallacy 1: The Interest Rate on Government Debt as the Discount Rate for Public Resource Consumption or Regulatory Resource Reallocation.
- III. Further Observations on Discount Rates and the Interests of Future Generations.
- IV. Fallacy 2: Majoritarian and Agency Internalization of Externalities and Provision of Collective Goods.
- V. Fallacy 3: “Imperfect” or Asymmetric Information As a “Market Failure.”
- VI. Fallacy 4: “Market Power” and “Behavioral Biases” As “Market Failures.”
- VII. Fallacy 5: “Environmental Justice.”
- VIII. Conclusions.

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¹ See <https://www.whitehouse.gov/wp-content/uploads/2023/04/DraftCircularA-4Preamble.pdf> and <https://www.whitehouse.gov/wp-content/uploads/2023/04/DraftCircularA-4.pdf>.

Summary

The Office of Management and Budget in its draft revision of Circular A-4 justifies the implementation of regulatory policy as a tool with which to correct “market, institutional, or behavioral distortions,” an orientation vast in its implications, even without the immediate expansion that “these concepts do not capture all the underlying circumstances that spur regulatory action.” It is obvious from the OMB discussion that the “distortions” of interest are those that lead away from allocational outcomes that can be described as Pareto optimal (“efficient”) in a textbook sense. There is nothing original about this orientation; it is consistent with the analytic principles underlying the earlier version of Circular A-4, and with the broad sweep of analytic thinking underlying the analysis of “efficiency” in traditional welfare economics.

This means that the motivating principle underlying the OMB regulatory guidelines — an improvement in allocational efficiency — carries a central implication, to wit, any given regulatory initiative may not introduce its own set of distortions the net effect of which is an increase in the inefficiency of resource allocation.

The central problem is that this central regulatory efficiency objective is inconsistent with much of the analysis and parameters promulgated in the draft OMB guidelines. The use of a discount rate of 1.7 percent rather than the 7 percent specified in the 2003 OMB circular A-4 would introduce a substantial distortion in the allocation of capital between private investment and that driven by regulatory requirements. OMB fails to recognize this because OMB fails to distinguish between two very different kinds of risks confronting investors choosing between investments in private-sector projects and investments in government bonds. For prospective investments in private projects, the potential investor confronts the risk that the project will fail to yield a rate of return competitive with those offered by alternative possible investments taken as a class. For government resource consumption, whether direct through spending or indirect through regulation, the analogous risk is that the regulation in question will fail to reduce economic distortions sufficiently so as to justify that particular use of resources in terms of the opportunity cost of capital. But that is not the relevant risk confronting the potential investor in government bonds, which is instead the risk that the government will fail to service the debt as promised in real terms. For this reason alone, the draft guidelines should not be finalized as written.

The “consumption rate of interest” is not the correct conceptual discount rate for regulatory analysis because the regulatory reallocation of resources in pursuit of increased economic efficiency is an investment, the opportunity cost of which is the marginal social return to investment.

The common argument that a low discount rate is needed to further the goal of intergenerational equity is not correct. Future generations prefer to receive a bequest of an aggregate capital stock both natural and manmade more- rather than less valuable, an objective that requires efficient resource allocation by the current generation, and therefore the application of the correct discount rate.

The OMB treatment of private and public incentives is wholly inconsistent, in that the draft guidelines delve in great detail into the purported problems attendant upon private incentives while ignoring the blatant problems inherent in government policymaking driven by the incentives created by majoritarian decision processes and bureaucratic efforts to maximize budgets. The

OMB draft guidelines simply assume that government action will improve resource allocation by increasing the output of collective goods toward the efficient level, but that assumption ignores the incentives of government also to underprovide collective goods in favor of transfers to members of the majority coalition.

Agencies seeking larger budgets have incentives to exaggerate the importance of the problems that they seek to address through regulation, and to increase the range and complexity of their activities, thus increasing the difficulty of the information problem confronting Congress. A good example is the use of the “social cost of carbon” (SCC) as driven by analysis of climate phenomena with models that cannot predict the actual record on temperatures and other climate parameters, rather than the application of those actual data. The SCC is wholly artificial, driven by modeling projections of large and adverse climate impacts resulting from increasing atmospheric concentrations of greenhouse gases (GHG), despite the reality that there is no actual evidence of such serious adverse effects. Because the SCC framework exaggerates the economic costs of GHG emissions, it exaggerates also the benefits of reductions in those emissions. Regulations yielding a purported given reduction in GHG emissions can be asserted to yield large net economic benefits even if it yields changes in future climate phenomena effectively equal to zero or unmeasurable.

Thus have models replaced data in vast swaths of environmental analysis, public health and pandemic matters, and much more, and there is no obvious constraint preventing such analytic gameplaying in other contexts by the regulatory agencies supposedly required to adhere to the previous and newly proposed OMB analytic standards. Such politicized “analysis” will prove ubiquitous among the federal agencies because their budget maximization incentives are powerful, because regulation is and always must be shaped by political pressures, and because the regulatory bureaucracies are powerful interest groups both ideologically and in terms of their budgetary imperatives. The OMB draft guidelines offer no constraints on such analytic approaches.

The description in the draft guidelines of imperfect information as a “market failure” is preposterous. Because resources are limited always and everywhere, not all information is produced — even at a conceptual level, that is close to an impossibility — and all individuals must pursue their myriad activities in a state of substantial ignorance. There is nothing inefficient about this state of affairs, and it does not represent a “market failure.”

Nor do information asymmetries — lower information costs in a given context for one set of parties than for others — change this central truth. Cheaper information would be welcome from the viewpoint of those confronted with information costs higher than those faced by others. That information costs are what they are is a reality; it is not a source of “inefficiency.”

The cost of acquiring information is what it is, and some transactions are lost because of it. At most, the presence of asymmetric information might yield a wealth transfer between parties to a transaction — the price might be higher or lower than would be the case in the absence of an information asymmetry — but that is not an inefficient outcome and certainly is not a “market failure.” Economics does not offer a theory of why one distribution of wealth is to be preferred — is more “efficient” — than another, and a regulatory analytic framework for government agencies that ostensibly pursues improvements in the efficiency of resource allocation has no business promulgating one.

The definition of “market power” in the draft guidelines is more-or-less a standard one, but the application of that definition in the draft guidelines is deeply problematic. How is “market

power” to be measured? What is the appropriate tradeoff between market power and the exploitation of scale economies? What degree of market power under a given measurement metric is “too much?” How are market forces that reduce market power in a dynamic context — entry by new competitors or new technologies is the classic process — to be evaluated?

Moreover, the OMB discussion of why “market power” exists is poor. Precisely what constitutes a “barrier to entry for competitors?” OMB does not tell us, perhaps because much policy discussion of such “barriers” shunts aside the relevant issues under an apparent assumption that the answer is obvious. It is not, and the larger problem ignored by OMB is the question of why such “barriers,” however defined, exist. The implicit premise in the (cursory) OMB discussion is the absence of conditions that loosely would characterize a perfectly competitive market. But the competitive process itself is costly in terms of resource allocation; the “efficient” degree of competitiveness is unlikely in most contexts to be something approximating “perfect” competition. Accordingly, some “market power” is efficient, a subtlety that the OMB discussion ignores.

OMB fails to examine carefully the tradeoff between the achievement of scale economies — reduced costs — and a reduction of “market power,” a gap in the draft guidelines that allows for expansive regulatory activity driven by the whims of the regulators. The “control of inherently scarce resources” as a source of “market power” is a tautology: monopolization of an input yields monopoly power. More broadly, all resources are “scarce”; that is why their market prices are greater than zero. How “scarce” does a resource have to be in order to create “market power” sufficiently important to justify regulatory intervention? OMB fails to tell us.

“Intellectual property protections” certainly are a source of (temporary) market power — as they are designed to be — but it is not clear what point OMB is trying to make by including this parameter in its list of sources of market power. The cursory OMB reference to “privileged access to infrastructure” is wholly ambiguous; precisely who is offering such privilege? If the “privileged access” is the result of proximity to “natural infrastructure,” then such proximity ought to be reflected in land prices, thus eliminating any cost advantages attendant upon a purported “privileged access to infrastructure.” Any “control over commercial platforms or networks,” whatever “control” means in this context, would carry an opportunity cost, again eliminating any cost advantage; and in the context of “market power,” OMB fails to tell us (or the regulatory agencies) how such control was achieved. Was there not some efficiency dynamic at work?

Nor does OMB discuss the “market power” of government generally, and the federal government in particular. The central purpose of a compound republic — federalism — is the imposition of competitive constraints upon government, and there is an obvious tradeoff between such competition and the achievement of scale economies in the provision of government services. The exercise of market power by regulatory agencies already has been discussed above in the context of efforts by agencies to maximize their budgets, but the same consideration affects the nature and stringency of the regulatory initiatives — the regulatory “prices” — that agencies can impose upon the private sector. OMB ignores this issue.

The OMB discussion of “behavioral biases” is no better. “Limitations on information processing” are a fact of life; the use of rules of thumb as a response is not a “market failure,” and OMB implicitly recognizes this reality in its observation about “limited attention, focus, and time.” The “decision-making biases” referenced by OMB also are the result of information costs; they are not a source of “inefficiency.”

The comedy highlight of the OMB discussion is the classification of “imperfect self-control” as a behavioral bias that “increases short-term well-being by less than it decreases future well-being,” that is, the use by individuals of discount rates too high. Is it the position of OMB that the inexorable political pressures shaping regulatory outcomes will not be driven by the political dynamics of the next election? Precisely what public choice model of policy formulation does OMB have in mind in its implicit assumption that private individuals use discount rates too high, but government officials systematically do not? At a more general level, what is the basis for the OMB premise that individuals exhibit systematic behavioral biases, but the staffs and officials of regulatory agencies will not?

The “environmental justice” concept is too narrow. Environmental quality is one component of “health” broadly defined, and it is clear from the scholarly literature that “health” is a “normal” good, that is, one the consumption of which rises with income or wealth. This is true for individuals and for economies as a whole. Lower-income individuals and households, precisely because their incomes are lower, consume less environmental quality, lower-quality diets, *ad infinitum*. Therefore, it is unsurprising that lower-income individuals and households tend to be located in areas with lower environmental quality; that is what they can afford. This is a reality regardless of the impacts of differences in environmental quality on “health,” that is, mortality and morbidity. Even if a lower level of environmental quality is merely unpleasant, that is a factor relevant to the ways in which individuals and households allocate their limited resources. Accordingly, the “environmental justice” issue is little more than the observation, or complaint, that the poor consume less environmental quality than others, that is, that they choose to allocate their resources in ways different from those exhibited by individuals and households wealthier.

More broadly, OMB fails to define the “distributional fairness” and “equity” concepts, undoubtedly because they are wholly subjective, and thus not measurable in any “objective” sense, leaving the definitions to the imaginations of the regulatory agencies. Nor does OMB explain why we should expect regulatory policies to advance such goals however defined, and the same is true for the longstanding problem traditionally described as the equity/efficiency tradeoff. Efforts by government to effect changes in the distribution of income or wealth necessarily affect resource allocation in ways reducing aggregate productivity. Perhaps a given change in “distributional fairness” and “equity” is worth the attendant reduction in aggregate wealth; perhaps not. There is no “objective” measure of this tradeoff because we do not have an efficiency theory of the relative virtues of different distributional outcomes. OMB attempts to circumvent this obvious problem by arguing that the declining marginal utility of income means that a transfer from those better off to those worse off improves aggregate wellbeing. This is an utter *non sequitur*.

The draft guidelines are fatally flawed — indeed, perverse — and should not be finalized in the current draft form.

I. The Central Implication of the OMB Rationales for Regulation

The draft OMB guidelines for regulatory analysis Circular A-4 summarizes the analytic rationale for regulatory activity as follows.²

The need for a regulation may take different forms. Modeling underlying

² See the draft guidelines at 15-16.

market, institutional, or behavioral distortions is a standard starting point for conducting benefit-cost analysis of a regulatory action or other government intervention, but these concepts do not capture all the underlying circumstances that spur regulatory action. Common needs for regulation include, but are not limited to:

- correcting market failure, which may implicate externalities, common property resources, public goods, club goods, market power, and imperfect or asymmetric information[;]
- addressing behavioral biases;
- improving government operations and service delivery;
- promoting distributional fairness and advancing equity; and
- protecting civil rights and civil liberties or advancing democratic values.

The phrase “market, institutional, or behavioral distortions” is vast in its implications, even without the immediate expansion that “these concepts do not capture all the underlying circumstances that spur regulatory action,” but it is obvious from the OMB discussion that the “distortions” of interest at a minimum are those that lead away from allocational outcomes that can be described as Pareto optimal (“efficient”) in a textbook sense.³ In other words, a “distortion” in the OMB analytic framework is a market nonoptimality or adverse behavioral factor that yields a reduction in the value of the aggregate output basket and thus in the value of the aggregate consumption basket available to individuals. Because it is market prices rather than the opinions and whims of agency observers that determine value — in the OMB terminology “willingness to pay” or “willingness to accept” — the implicit but clear OMB stance is that systematic deviations from efficient prices are a function of individual preferences as reflected in market prices, and opportunity costs defined similarly. It is individual preferences that determine “value” and thus the efficiency or inefficiency of allocational outcomes.⁴

Accordingly, in the draft OMB framework, correction of economic distortions yielding a purported increase in economic efficiency is the central goal driving “the need for a regulation.”⁵ There is nothing original about this orientation; it is consistent with the analytic principles underlying the earlier version of Circular A-4, and with the broad sweep of analytic thinking underlying the analysis of “efficiency” in traditional welfare economics.⁶ Note that “economic efficiency” or “distortions” are not defined in a rigorous manner in the proposed guidelines, but

³ An allocational outcome that is Pareto optimal is one from which no one can be made better off without making someone else worse off. See, e.g., Francis M. Bator, “The Simple Analytics of Welfare Maximization,” in William Breit and Harold M. Hochman, eds., *Readings in Microeconomics*, New York: Holt, Rinehart and Winston, 1971.

⁴ The axiom that it is individual preferences that determine “value” is normative, that is, it is itself a value judgment. It is not a “scientific” finding; but it is the only definition of “value” consistent with individual freedom. See Robert Nozick, *Anarchy, State, and Utopia*, Basic Books, 1974, 2013.

⁵ Because of the assumed distortions, the allocational outcome *ex ante* is not efficient or Pareto optimal; the regulations by assumption yield a Pareto improvement that makes at least one person better off without making anyone else worse off.

⁶ For the original Circular A-4, see https://obamawhitehouse.archives.gov/omb/circulars_a004_a-4/. For a useful summary discussion of the traditional view of deviations from “efficient” resource allocation, see, e.g., Harvey S. Rosen, *Public Finance*, Boston: Irwin McGraw-Hill, fifth edition, 1999, at 61-111.

must be driven by some concept of individual preferences aggregated in some manner; after all, surely OMB is not proposing that a “distortion” is whatever a federal agency classifies as such.

But because an allocational distortion — inefficiency in resource allocation — must be defined relative to an efficient outcome resulting from “undistorted” market forces, there exists in the OMB guidelines a blatant inconsistency inherent in the inclusion of “behavioral biases” as one rationale for regulatory action. If there are “behavioral biases” that systematically prevent a Pareto optimal allocational outcome, does there exist a conceptual world in which a regulatory action would be inconsistent with the OMB guidelines? After all, “behavioral biases” must be defined relative to some norm, but it is not clear what that defines that norm in the OMB discussion, other than a series of assertions that individuals make systematic mistakes. If individuals fail to behave as economic theory predicts that they “should,” then it is the theory that is in need of rethinking, rather than individual choice behavior. This problem is discussed briefly in section V. The more important point is that regulatory actions might introduce a set of “distortions” of their own, an obvious problem that the draft OMB guidelines essentially shunt aside.

This means that the motivating principle underlying the OMB regulatory guidelines — an improvement in allocational efficiency — carries a central implication, to wit, any given regulatory initiative may not introduce its own set of distortions the net effect of which is an increase in the inefficiency of resource allocation. This is a serious problem throughout the OMB discussion, in particular with respect to the explicit OMB assertion “that the real (inflation-adjusted) rate of return on long-term U.S. government debt provides a fair approximation of the social rate of time preference.”⁷ This simply is not correct, an observation to which we now turn.

II. Fallacy 1: The Interest Rate on Government Debt as the Discount Rate For Public Resource Consumption or Regulatory Resource Reallocation

Because the OMB guidelines define appropriate regulatory activity as agency efforts to correct economic distortions engendered by market incentives and behavior, it is axiomatic that such regulations would change resource allocation in ways ostensibly yielding an increase in the present value of aggregate output (or the aggregate consumption stream) over some set of future time periods. That regulation is needed to effect this shift in resource allocation demonstrates that the regulation increases resource use during the current (and perhaps some set of future) time period; that is why market forces fail to yield the resource use deemed more efficient by the regulators.

In other words, it must be the case in the OMB analytic framework that a given regulation increases resource consumption in, crudely, the short run, thus reducing the value of the aggregate consumption basket in the short run, in an effort to increase the value of the aggregate consumption basket — that is, the present value of the aggregate consumption stream — over the long run. The regulation, therefore, from an analytic standpoint engenders an investment of resources, however indirectly, the purpose of which is an increase in the present value of the consumption stream over time.⁸ The calculation of that present value obviously requires a choice among alternative discount

⁷ See the draft guidelines at 75-76.

⁸ The issue of intergenerational equity — the consumption stream tradeoff across time periods — is discussed in section VII.

rates, a consideration that makes relevant the admonition from section I above that “any given regulatory initiative may not introduce its own set of distortions the net effect of which is an increase in the inefficiency of resource allocation.” Any such outcome would be inconsistent with the explicit efficiency goals of the draft guidelines as explicated by OMB.

As just shown, resource consumption during the current time period driven by regulatory requirements, again, by definition, is an investment, and it must be evaluated in comparison with the social return to alternative investments. Accordingly, it is the opportunity cost of capital that is the appropriate discount rate to be applied to the analysis of regulatory initiatives, because the investment of resources toward achievement of regulatory goals imposes an opportunity cost in the form of other forgone investments.

Therefore, the appropriate discount rate is the opportunity cost of capital for the economy as a whole. For the period 1928-2020, the average annual before-tax return to investment in the Standard and Poor 500, in real (inflation-adjusted) terms was 8.5 percent.⁹ For the period 1960-2020, the figure was 7.61 percent. Such long-run historical figures are not consistent with the assertion in the draft OMB guideline “that the real (inflation-adjusted) rate of return on long-term U.S. government debt provides a fair approximation of the social rate of time preference,” which OMB estimates at 1.7 percent in real terms as an average over the most recent thirty-year period.¹⁰

The use of a discount rate of 1.7 percent rather than the 7 percent specified in the 2003 OMB circular A-4 would introduce a substantial distortion in the allocation of capital between private investment and that driven by regulatory requirements. In effect, regulatory investments yielding a prospective economic return of as little as 1.7 percent would displace private sector investments with prospective (expected) returns substantially higher.

The OMB discussion of appropriate discount rates fails to recognize this distortion because the OMB discussion fails to distinguish between two very different kinds of risks confronting investors choosing between investments in private-sector projects and investments in government bonds. For prospective investments in private projects, the potential investor confronts the risk that the project will fail to yield a rate of return competitive with those offered by alternative possible investments taken as a class.

For government resource consumption, whether direct through spending or indirect through regulation, the analogous risk is that the regulation in question will fail to reduce economic distortions sufficiently so as to justify that particular use of resources in terms of the opportunity cost of capital. But that is not the relevant risk confronting the potential investor in government bonds, which is instead the risk that the government will fail to service the debt as promised in real terms. (The government might create an inflation unanticipated by the purchasers of the bonds, so that even if the debt is serviced as promised in nominal terms, it will not be serviced as promised in real terms.)

For policymakers in their role as representatives of the taxpayers or the citizenry writ large,

⁹ The data on annual returns for several investment alternatives are reported by the Stern School of Management, New York University, at <http://www.stern.nyu.edu/~adamodar/pc/datasets/histretSP.xls>.

¹⁰ See the draft guidelines at 76.

the relevant question is whether the allocational improvements to be obtained through a given regulatory instrument will be sufficient to yield a rate of return to the economy in the aggregate at least equal to the opportunity cost of capital. The relevant question is not whether the government will service the debt as promised in real terms. That is why the OMB assertion that the interest rate on government bonds represents “a fair approximation of the social rate of time preference” is false. Again, the draft OMB directive that the interest rate on government bonds be used to discount the streams of benefits and costs of regulatory initiatives would create a large distortion toward justifying regulatory resource consumption, and therefore is inconsistent with the overall OMB justification of regulation in terms of the reduction of economic distortions inherent in market behavior. For this reason alone, the draft guidelines should not be finalized as written.

III. Further Observations on Discount Rates and the Interests of Future Generations

The “consumption rate of interest” is not the correct conceptual discount rate for regulatory analysis because, as discussed above, the regulatory reallocation of resources in pursuit of increased economic efficiency is an investment, the opportunity cost of which is the marginal social return to investment. Even if we assume that the “consumption rate of interest” conceptually is the correct parameter for discounting purposes, the relevant metric is the real market rate of interest on intertemporal consumption shifts, one crude measure of which is the market rate of interest on unsecured consumer loans. Even given the recent years of low interest rates maintained by the Federal Reserve, that market rate appears to be over 7 percent in real terms.¹¹ For secured loans (new autos), the real interest rate appears to be at least 3 percent,¹² but that is not the correct parameter for regulatory analysis because there is no collateral insuring against the possibility that government policies will prove uneconomic, that is, yield an aggregate economic return lower than the opportunity cost of capital. Note also that the use of a (low) “consumption rate of interest” for the evaluation of regulatory policy would introduce an important bias in the allocation of resources between government and private-sector resource use.

One common argument observed in the climate policy context is that future generations prefer to avoid the damages that they ostensibly will bear because of the climate effects of resource allocation decisions made by the current generation, and because future generations cannot vote during the current time period, it is equitable to force the current generation to bear the costs of anthropogenic climate change that otherwise would be inflicted upon future generations.

However seemingly straightforward, that argument is not correct. Future generations prefer to receive a bequest of an aggregate capital stock both natural and manmade more- rather than less valuable, an objective very different from a maximization of the value of one dimension — climate phenomena. This requires efficient resource allocation by the current generation, and therefore the application of the correct discount rate. Consider a *homo sapiens* baby borne in a cave some 50,000 years ago. Despite the fact that at birth that child would have enjoyed environmental quality effectively unaffected by mankind, and *a fortiori* climate phenomena determined by natural processes only, the baby at birth would have had a life expectancy of only about ten years.¹³

Accordingly, it is obvious that given the opportunity to choose, that child would opt for

¹¹ See the data reported by the Federal Reserve Bank of St. Louis at <https://fred.stlouisfed.org/series/TERMCBPER24NS>.

¹² See <https://fred.stlouisfed.org/series/RIFLPBCIANM60NM>.

¹³ This life expectancy observation was provided by Professor Gail Kennedy, Department of Anthropology, University of California, Los Angeles, during a telephone interview conducted February 16, 2011.

less environmental quality and (perhaps) greater climate risk in exchange for a longer life expectancy engendered by a more valuable aggregate capital stock yielding improved shelter, expanded food supplies, a cleaner water supply, better medical care, *ad infinitum*. A bequest of greater wealth is the central objective of any generation, a reality shunted aside by the common focus upon only the climate dimension of the aggregate capital stock to be inherited by future generations.

IV. Fallacy 2: Majoritarian and Agency Internalization of Externalities and Provision of Collective Goods

The implicit but obvious assumption in the draft guidelines is that given the proper application of benefit/cost analytic principles, the promulgation of regulatory requirements will yield an improvement in resource allocation, in particular in the form of internalization of externalities and the expanded provision of collective goods, for which private incentives lead to resource misallocation.¹⁴

The OMB treatment of private and public incentives is wholly inconsistent, in that the draft guidelines delve in great detail into the purported problems attendant upon private incentives while ignoring the blatant problems inherent in government policymaking driven by the incentives created by majoritarian decision processes and bureaucratic efforts to maximize budgets.

Consider for example the provision of collective goods. The standard textbook analysis of collective goods exhibiting both non-rivalry in consumption and non-excludability of nonpayers predicts that market forces will underprovide such collective goods due to high transaction costs among large numbers of citizens and because of the obvious incentives of individual beneficiaries of the provision of such goods to obtain free rides on the provision of such goods by others.¹⁵ The OMB draft guidelines simply assume that government action will improve resource allocation by increasing the output of collective goods toward the efficient level, but that assumption ignores the incentives of government.

Consider a government operating under a majoritarian decision rule, and making choices between the output of a collective good (e.g., defense) and a private good (e.g., transfer payments). At a simplified level, the median voter (the marginal member of the majority) can vote to reduce the output of the collective good from the efficient level by \$1 per voter, and then to transfer \$2 to each member of the majority, and does so until \$2 of transfers have the same marginal value as \$1 of the collective good to the median voter.¹⁶ Accordingly, government itself has incentives to underprovide collective goods, and more complex models of majoritarian decisionmaking yield the same underprovision predictions as this highly simplified case.¹⁷ One response in a bargaining model of legislative budget choice might be to combine an increase in the provision of the

¹⁴ In many cases the internalization of externalities is the opposite side of the same coin as the provision of collective goods, as the reduction of negative externalities itself is a collective good.

¹⁵ “Underprovision” means an output level at which marginal social benefits exceed marginal costs. For one critique of the standard underprovision axiom, see Cotton M. Lindsay and William R. Dougan, “Efficiency in the Provision of Pure Public Goods by Private Citizens,” *Public Choice*, Vol. 156 (2013), pp. 31-43, at <https://link.springer.com/article/10.1007/s11127-012-9942-z>.

¹⁶ The majority is assumed here as 50 percent of the voters plus one. This is the equilibrium size of the majority because any majority coalition has incentives to transfer income from as many as possible and then to divide the total transfer among as few as possible.

¹⁷ See James M. Buchanan, *The Demand and Supply of Public Goods*, Chicago: Rand McNally, 1968.

collective good with an expansion in the provision of the transfers, so as to transform the collective good into a quasi-private one.¹⁸ An example is the siting of military bases and military contractors in all or most congressional districts; but the upshot is virtually certain to be an expansion of the government budget for the provision of the collective good above the “efficient” level, and therefore an increase also in the excess burden of the tax system. OMB simply ignores this issue.

The same is true for the implications of budget maximization incentives on the part of agencies.¹⁹ Agencies in the standard case negotiate with Congress for a lump-sum budget in exchange for a lump-sum basket of promised output. Congress is confronted with the problem of determining the minimum cost of that lump-sum basket and of some approximation of marginal benefits and costs in terms of whatever criteria are driven by political incentives.²⁰ Accordingly, agencies seeking larger budgets have incentives to exaggerate the importance of the problems that they seek to address through regulation, and to increase the range and complexity of their activities, thus increasing the difficulty of the information problem confronting Congress.²¹

A good example is the use of the “social cost of carbon” (SCC) as driven by analysis of climate phenomena with models that cannot predict the actual record on temperatures and other climate parameters, rather than the application of those actual data.²² The SCC is wholly artificial, driven by modeling projections of large and adverse climate impacts resulting from increasing atmospheric concentrations of greenhouse gases (GHG), despite the reality that there is no actual evidence of such serious adverse effects.²³ That the modeling projections can be manipulated also is an obvious reality; one trivial example of the available manipulation tools in the climate context is the application of extreme emissions scenarios combined with assumptions about the sensitivity of the climate system that are not consistent with the findings reported in the peer-reviewed literature.²⁴

Because the SCC framework exaggerates the economic costs of GHG emissions, it exaggerates also the benefits of reductions in those emissions. *Regulations yielding a purported given reduction in GHG emissions can be asserted to yield large net economic benefits even if it yields changes in future climate phenomena effectively equal to zero or unmeasurable.* Consider the “net-zero” emissions policies of the Biden administration: a “net zero emissions economy by

¹⁸ See Mancur Olson, *The Logic of Collective Action: Public Goods and the Theory of Groups*, Cambridge: Harvard University Press, 1971.

¹⁹ See William A. Niskanen, “Bureaucrats and Politicians,” *Journal of Law & Economics*, Vol. 18, No. 3 (December 1975), pp. 617-643, at <https://www.jstor.org/stable/725050>. See also Cotton M. Lindsay, “A Theory of Government Enterprise,” *Journal of Political Economy*, Vol. 84, No. 5 (October 1976), at <https://www.journals.uchicago.edu/doi/10.1086/260496>.

²⁰ Congress has powerful incentives to determine that minimum cost because resources not spent on one set of constituencies can be spent on another. I shunt aside here the issue of whether and how the availability of deficit finance affects this dynamic.

²¹ This complexity objective means that the budget in effect becomes a function of itself: Greater complexity increases the difficulty of the monitoring problem for Congress, thus allowing the agency to obtain a larger budget.

²² The substitution of model projections in place of actual data in policy analysis is a serious and growing problem, yielding serious biases in terms of analyses, estimates, policy initiatives, and measures of policy outcomes. See Kenneth P. Green, *The Plague of Models*, Fullerene Publishing, 2023, at <https://fullerenepublishing.ca/product/the-plague-of-models/>.

²³ See Steven E. Koonin, *Unsettled: What Climate Science Tells Us, What It Doesn't, and Why It Matters*, Dallas: BenBella Books, 2021. See also Benjamin Zycher at <https://www.budget.senate.gov/imo/media/doc/Dr.%20Benjamin%20Zycher%20-%20Testimony%20-%20Senate%20Budget%20Committee.pdf>.

²⁴ For voluminous discussions, see the various posts and papers at <https://judithcurry.com/>.

no later than 2050.”²⁵ If we apply the climate model used by the Environmental Protection Agency and most other federal agencies, under assumptions that exaggerate the effects of reduced GHG emissions, the temperature reduction yielded by the net-zero policy would be 0.137°C by 2100.²⁶ Because the standard deviation of the surface temperature record is 0.11°C, that effect would be barely detectable.²⁷

But the SCC framework shunts these realities aside. A good example is the earlier “efficiency” rule for medium- and heavy trucks promulgated by the Obama administration. The regulatory impact analysis for that rule reported the EPA estimate that it would reduce global temperatures by 2100 by 0.0026-0.0065°C, that is, by effectively zero. But because EPA simply multiplied the assumed reduction in GHG emissions by an assumed SCC, EPA concluded that the rule would yield over \$100 billion in net economic benefits. This framework is preposterous.²⁸

Thus have models replaced data in the climate policy context, and there is no obvious constraint preventing such analytic gameplaying in other contexts by the regulatory agencies supposedly required to adhere to the previous and newly proposed OMB analytic standards. Indeed: The substitution of models in place of actual data has infected regulatory policy in vast swaths of other environmental analysis, public health and pandemic matters, and much more.²⁹ Such politicized “analysis” will prove ubiquitous among the federal agencies because their budget maximization incentives are powerful, because regulation is and always must be shaped by political pressures, and because the regulatory bureaucracies are powerful interest groups both ideologically and in terms of their budgetary imperatives. Accordingly, this perverse process can be predicted with virtual certainty to continue and expand, but the OMB draft guidelines offer no constraints on such analytic approaches as the substitution of model projections in place of data, or a more general metastasis of regulatory constraints to be imposed upon the economy.³⁰

V. Fallacy 3: “Imperfect” or Asymmetric Information As a “Market Failure”

Consider the use of iron ore in the production of steel. Iron ore is not a free good; the production of it requires the use of scarce resources. Accordingly, market forces will limit the production of iron ore to that justified by the market value of steel or other goods for which iron ore is an input; the demand for iron ore is “derived” from the demand for steel.

There is no analytic difference between iron ore and information, the latter of which is an input in the production of a vast array of goods and services and for the “search” activities needed to discover available options among goods and services available. It is difficult to conceive of an exception to these observations.

As with iron ore, the production of information requires the investment of scarce resources.

²⁵ See <https://www.whitehouse.gov/briefing-room/statements-releases/2023/04/20/fact-sheet-president-biden-to-catalyze-global-climate-action-through-the-major-economies-forum-on-energy-and-climate/#:~:text=Putting%20the%20Power%20Sector%20on%20a%20Path%20to%20Net%20Zero%20Emissions&text=President%20Biden%20has%20set%20an,by%20no%20later%20than%202050.>

²⁶ Author computations using MAGICC 7.0, available at <https://magicc.org/>.

²⁷ See <https://agupubs.onlinelibrary.wiley.com/doi/pdf/10.1029/1999JD900835>.

²⁸ See Benjamin Zycher at <https://scholarship.law.tamu.edu/cgi/viewcontent.cgi?article=1154&context=lawreview>.

²⁹ See Green, *op. cit.* fn. 19 *supra*.

³⁰ One good example is the “guidance” for federal agencies on greenhouse gas emissions and climate change under the National Environmental Policy Act. See Benjamin Zycher at <https://www.aei.org/wp-content/uploads/2023/03/Zycher-comment-CEQ-NEPA-GHG-Climate-Guidance-RIN-0331-AA06-3-10-2023.pdf>.

Accordingly, information is not free, as has been recognized by economists and many others for centuries at a minimum, and the collective nature of information — consumption of a piece of information by one individual does not reduce the amount available, unlike the case for, say apples — does not change that crucial underlying reality.

Accordingly, complete or “perfect” information is an illusion. Individuals have incentives to invest resources in the acquisition of information until the expected marginal benefit of doing so equals the marginal cost. That statement is a truism, but it carries with it important testable implications nonetheless, the central one of interest here is that the acquisition of “complete” information is almost certain to be inefficient.³¹

Accordingly, the description in the draft guidelines of imperfect information as a “market failure” is preposterous. Less steel is produced than otherwise would be the case because iron ore is not free; that does not mean that the “imperfect” (incomplete) production of iron ore is a “market failure.” Similarly, because resources are limited always and everywhere, not all information is produced — even at a conceptual level, that is close to an impossibility — and all individuals must pursue their myriad activities in a state of substantial ignorance. There is nothing inefficient about this state of affairs, and it does not represent a “market failure.”

Nor do information asymmetries — lower information costs in a given context for one set of parties than for others — change this central truth. Just as cheaper iron ore would be welcome from the viewpoint of the consumers of steel, cheaper information would be welcome from the viewpoint of those confronted with information costs higher than those faced by others. That information costs are what they are is a reality; it is not a source of “inefficiency.”

The standard argument is that information asymmetries reduce the number of transactions that otherwise would make all parties better off; if a prospective buyer of a used auto cannot determine the quality of the vehicle cheaply, and if he does not know or trust the seller, then a transaction that would be efficient fails to be consummated. That is true enough; but it is not an inefficient outcome and certainly is not a “market failure.” As in our iron ore example, some steel is not produced because iron ore is not free. The cost of acquiring information is what it is, and some transactions are lost because of it. At most, the presence of asymmetric information might yield a wealth transfer between parties to a transaction — the price might be higher or lower than would be the case in the absence of an information asymmetry — but that is not an inefficient outcome and certainly is not a “market failure.” Economics does not offer a theory of why one distribution of wealth is to be preferred — is more “efficient” — than another, and a regulatory analytic framework for government agencies that ostensibly pursues improvements in the efficiency of resource allocation has no business promulgating one.

There is the further matter that the OMB draft guidelines are curiously silent about why government regulators can be predicted to have access to better information, or to know what information ought to be provided in greater quantities, or to know how to induce market participants to reveal more information than they would choose otherwise. The discussion of information costs in the draft OMB guidelines is deeply confused, and should not be incorporated into a final set of analytic guidelines.

VI. Fallacy 4: “Market Power” and “Behavioral Biases” As “Market Failures”

³¹ See, e.g., George J. Stigler, *The Theory of Price*, third edition, London: MacMillan, 1966, at 1-4.

The definition of “market power” in the draft guidelines is more-or-less a standard one.³²

A firm or group of firms has market power as a seller (“monopoly power” or “oligopoly power”) when it can influence or determine the price at which it sells its goods and services; analogously, a firm or group of firms has market power as a purchaser (“monopsony power” or “oligopsony power”) when it can influence or determine the wages or other prices paid for goods and services it buys.

However commonplace, this definition is useless for purposes of shaping the analysis of regulatory policies. How is “market power” to be measured? What is the appropriate tradeoff between market power and the exploitation of scale economies? What degree of market power under a given measurement metric is “too much?” How are market forces that reduce market power in a dynamic context — entry by new competitors or new technologies is the classic process — to be evaluated?

More to the point, the OMB discussion of why “market power” exists is poor.³³

market power may arise from a variety of sources, including but not limited to barriers to entry for competitors, economies of scale, control of inherently scarce resources, intellectual property protections, privileged access to infrastructure, control over commercial platforms or networks, unlawful exclusionary conduct, and monopoly access to detailed consumer data.

Precisely what constitutes “barriers to entry for competitors?” OMB does not tell us, perhaps because much policy discussion of such “barriers” shunts aside the relevant issues under an apparent assumption that the answer is obvious. It is not. An “entry barrier” must be a cost confronting a potential entrant that was not confronted by the existing firm enjoying some degree of market power, but the nature of such a cost asymmetry is very far from clear, unless it is the result of government regulatory (or other) policies themselves, a dimension of the “market power” problem that the draft guidelines recognize only in passing.³⁴

Note that the cost advantage enjoyed by the existing firm ought to be manifested by the ownership or employment of factors of production the wages of which under competitive processes would reflect the cost advantage creating the “barrier to entry.” Accordingly, the opportunity cost of owning or employing such productive factors ought to eliminate the barrier to entry — the cost advantage — unless the specific productive factor is specialized to the firm for some reason.

The larger problem ignored by OMB is the question of why such “barriers,” however defined, exist. The implicit premise in the (cursory) OMB discussion is the absence of conditions that loosely would characterize a perfectly competitive market. But the competitive process itself is costly in terms of resource allocation; the “efficient” degree of competitiveness is unlikely in

³² See the draft guidelines at 17.

³³ *Ibid.*

³⁴ On barriers to entry, see Harold Demsetz, “Barriers to Entry,” *American Economic Review*, Vol. 72, No. 1 (March 1982), pp. 47-57, at <https://www.jstor.org/stable/1808574#:~:text=Information%20costs%20are%20the%20more,both%20consumer%20and%20seller%20viewpoints.>

most contexts to be something approximating “perfect” competition. Accordingly, some “market power” is efficient, a subtlety that the OMB discussion ignores.

OMB fails to delve into the tradeoff between the achievement of scale economies — reduced costs — and a reduction of “market power,” a gap in the draft guidelines that allows for expansive regulatory activity driven by the whims of the regulators. The “control of inherently scarce resources” as a source of “market power” is a tautology: monopolization of an input yields monopoly power. To what degree would the substitutability of other inputs affect the perceived need to regulate in the face of “market power” in the OMB framework? OMB fails to tell us. More broadly, all resources are “scarce”; that is why their market prices are greater than zero. How “scarce” does a resource have to be in order to create “market power” sufficiently important to justify regulatory intervention? OMB fails to tell us.

“Intellectual property protections” certainly are a source of (temporary) market power — as they are designed to be — but it is not clear what point OMB is trying to make by including this parameter in its list of sources of market power. The cursory OMB reference to “privileged access to infrastructure” is wholly ambiguous; precisely who is offering such privilege? If, as suggested in passing twice in the OMB discussion, the “privileged access” is the result of proximity to “natural infrastructure,” then such proximity ought to be reflected in land prices, thus eliminating any cost advantages attendant upon a purported privileged access to infrastructure.” Any “control over commercial platforms or networks,” whatever “control” means in this context, would carry an opportunity cost, again eliminating any cost advantage; and in the context of “market power,” OMB fails to tell us (or the regulatory agencies) how such control was achieved. Was there not some efficiency dynamic at work?

The remaining OMB discussion of the sources of market power is useless in terms of explaining the efficiency or inefficiency dimensions of the observations in a way leading regulatory agencies toward efficient regulatory efforts. Few economic sectors are perfectly competitive, and few firms have no control over the prices that they charge. It cannot be the case that OMB believes that the entire economy should be regulated so as to reduce the effects of “market power,” but nowhere in the draft guidelines is there a useful discussion that outlines the relevant distinctions and considerations.

Nor does OMB discuss the “market power” of government generally, and the federal government in particular. The central purpose of a compound republic — federalism — is the imposition of competitive constraints upon government, and there is an obvious tradeoff between such competition and the achievement of scale economies in the provision of government services. The exercise of market power by regulatory agencies already has been discussed above in the context of efforts by agencies to maximize their budgets, but the same consideration affects the nature and stringency of the regulatory initiatives — the regulatory “prices” — that agencies can impose upon the private sector. OMB ignores this issue.³⁵

The OMB discussion of “behavioral biases” is no better.³⁶

³⁵ This problem is crucial in terms of the division of regulatory responsibilities between the states and the federal government. It is important as well in a number of other contexts, an example of which is federal to state/local revenue sharing, essentially a cartel arrangement in which the federal government impose taxes upon the nation write large higher than those that states would be able to impose if they were forced to compete more fully for location and investment decisions.

³⁶ See the draft guidelines at 18-19.

Behavioral biases can be categorized in two groups: limitations on information processing and decision-making biases. Because of limited capacity to process information, even when adequate information is available, people can make systematic mistakes; limited attention, focus, and time can lead to the use of heuristics (rules of thumb).

People also exhibit various decision-making biases, such as those stemming from framing effects, anchoring effects, loss aversion, present bias, unrealistic optimism, and a preference for the status quo. Another sort of decision-making bias stems from challenges in decision-making, such as imperfect self-control. When individuals exhibit imperfect self-control, they make a decision that increases short-term well-being by less than it decreases future well-being... [Regulatory analysis might] require[s] a departure from an assumption... that individuals optimize their own lifetime well-being subject to budget and other relevant constraints.

Like the costs of iron ore or the acquisition of information discussed above, “limitations on information processing” are a fact of life; the use of rules of thumb as a response is not a “market failure,” and OMB implicitly recognizes this reality in its observation about “limited attention, focus, and time.” After all, “attention, focus, and time” devoted to one set of individual considerations leaves less available for others. The “decision-making biases” referenced by OMB also are the result of information costs; they are not a source of “inefficiency.”

The comedy highlight of the OMB discussion is the classification of “imperfect self-control” as a behavioral bias that “increases short-term well-being by less than it decreases future well-being,” that is, the use by individuals of discount rates too high. Is it the position of OMB that the inexorable political pressures shaping regulatory outcomes will not be driven by the political dynamics of the next election? Precisely what public choice model of policy formulation does OMB have in mind in its implicit assumption that private individuals use discount rates too high, but government officials systematically do not?

At a more general level, what is the basis for the OMB premise that individuals exhibit systematic behavioral biases, but the staffs and officials of regulatory agencies will not? Is it the view of OMB that the staffs and officials “optimize their own lifetime well-being subject to budget and other relevant constraints,” or that they do not? Can either of those two possibilities be predicted to yield systematic regulatory outcomes that are efficient?

VII. Fallacy 5: “Environmental Justice.”

The “environmental justice” issue typically is defined in terms of differing levels of environmental quality experienced by various groups, the poor and minority groups in particular. The brief OMB formulation is as follows.³⁷

Under Executive Order 12898, “Federal Actions to Address Environmental Justice in Minority Populations and Low-Income Populations,” to “the extent practical and appropriate, Federal agencies” must “determine whether their programs, policies, and activities have disproportionately high and adverse

³⁷ See the draft guidelines at 88.

human health or environmental effects on minority populations and low-income populations.” Agencies are also tasked with, “[t]o the greatest extent practicable and permitted by law, ... addressing, as appropriate, disproportionately high and adverse human health or environmental effects of [their] programs, policies, and activities on minority populations and low-income populations.”

The basic problem with the “environmental justice” concept is straightforward: It is too narrow. Environmental quality is one component of “health” broadly defined, and it is clear from the scholarly literature that “health” is a “normal” good, that is, one the consumption of which rises with income or wealth. This is true for individuals and for economies as a whole.³⁸ Lower-income individuals and households, precisely because their incomes are lower, consume less environmental quality, lower-quality diets, *ad infinitum*.

Therefore, it is unsurprising that lower-income individuals and households tend to be located in areas with lower environmental quality; that is what they can afford. This is a reality regardless of the impacts of differences in environmental quality on “health,” that is, mortality and morbidity. Even if a lower level of environmental quality is merely unpleasant, that is a factor relevant to the ways in which individuals and households allocate their limited resources.

Accordingly, the “environmental justice” issue is little more than the observation, or complaint, that the poor consume less environmental quality than others, that is, that they choose to allocate their resources in ways different from those exhibited by individuals and households wealthier.

There is the further matter that OMB fails to define the relevant concepts, undoubtedly because they are wholly subjective, and thus not measurable in any “objective” sense, leaving the meaning of the following observation to the imaginations of the regulatory agencies.³⁹

Regulations can play a key role in promoting distributional fairness and advancing equity.

What are “distributional fairness” and “equity?” Obviously, the definitions are elusive, and in any event cannot be divorced from considerations of individual productivity.⁴⁰ There is the classic endowment problem — individuals enter life with very different endowments of human and financial capital — an obvious reality central to the “fairness” and “equity” questions, but not a parameter clearly malleable by regulatory policy. One central long-term policy initiative by government intended (in part) to deal with the endowment problem is public education, but the low relative quality of public schools in low-income and minority areas illustrates the difficulty of using public policies to change “distributional fairness” and “equity” outcomes in specific directions. Does OMB believe that the “distributional fairness” and “equity” outcomes would be

³⁸ On the income elasticity of the demand for health care spending, see <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC5890070/>. On the environmental Kuznets curve, see, e.g., <https://www.sciencedirect.com/topics/earth-and-planetary-sciences/environmental-kuznets-curve>.

³⁹ See the draft guidelines at 19.

⁴⁰ See Cotton M. Lindsay, “Measuring Human Capital Returns,” *Journal of Political Economy*, Vol. 79, No. 6 (Nov-Dec 1971) pp. 1195–1215.

systematically different for regulatory policy? If so, OMB fails to explain any such result would obtain.

Nor does OMB address the longstanding problem traditionally described as the equity/efficiency tradeoff.⁴¹ Efforts by government to effect changes in the distribution of income or wealth necessarily affect resource allocation in ways reducing aggregate productivity. Perhaps a given change in “distributional fairness” and “equity” is worth the attendant reduction in aggregate wealth; perhaps not. There is no “objective” measure of this tradeoff because we do not have an efficiency theory of the relative virtues of different distributional outcomes.

OMB attempts to circumvent this obvious problem by arguing that the declining marginal utility of income means that a transfer from those better off to those worse off improves aggregate wellbeing. This is an utter *non sequitur*. The universal observation of a declining marginal utility of income is for a given individual. It is not applicable across individuals; that is why standard economic analysis does not allow for interpersonal utility comparisons, for which there is no theoretical basis.

VIII. Conclusions

OMB justifies the implementation of regulatory policy as a tool with which to correct “market, institutional, or behavioral distortions,” an orientation vast in its implications, even without the immediate expansion that “these concepts do not capture all the underlying circumstances that spur regulatory action.” It is obvious from the OMB discussion that the “distortions” of interest are those that lead away from allocational outcomes that can be described as Pareto optimal (“efficient”) in a textbook sense. There is nothing original about this orientation; it is consistent with the analytic principles underlying the earlier version of Circular A-4, and with the broad sweep of analytic thinking underlying the analysis of “efficiency” in traditional welfare economics.

This means that the motivating principle underlying the OMB regulatory guidelines — an improvement in allocational efficiency — carries a central implication, to wit, any given regulatory initiative may not introduce its own set of distortions the net effect of which is an increase in the inefficiency of resource allocation.

The central problem is that this central regulatory efficiency objective is inconsistent with much of the analysis and parameters promulgated in the draft OMB guidelines. The use of a discount rate of 1.7 percent rather than the 7 percent specified in the 2003 OMB circular A-4 would introduce a substantial distortion in the allocation of capital between private investment and that driven by regulatory requirements. OMB fails to recognize this because OMB fails to distinguish between two very different kinds of risks confronting investors choosing between investments in private-sector projects and investments in government bonds. For prospective investments in private projects, the potential investor confronts the risk that the project will fail to yield a rate of return competitive with those offered by alternative possible investments taken as a class. For government resource consumption, whether direct through spending or indirect through regulation, the analogous risk is that the regulation in question will fail to reduce economic distortions sufficiently so as to justify that particular use of resources in terms of the opportunity cost of

⁴¹ The classic discussion is Arthur M. Okun, *Equality and Efficiency: The Big Tradeoff*, 1975, at <https://www.brookings.edu/book/equality-and-efficiency-the-big-tradeoff/>.

capital. But that is not the relevant risk confronting the potential investor in government bonds, which is instead the risk that the government will fail to service the debt as promised in real terms. For this reason alone, the draft guidelines should not be finalized as written.

The “consumption rate of interest” is not the correct conceptual discount rate for regulatory analysis because, as discussed above, the regulatory reallocation of resources in pursuit of increased economic efficiency is an investment, the opportunity cost of which is the marginal social return to investment.

The common argument that a low discount rate is needed to further the goal of intergenerational equity is not correct. Future generations prefer to receive a bequest of an aggregate capital stock both natural and manmade more- rather than less valuable, an objective that requires efficient resource allocation by the current generation, and therefore the application of the correct discount rate.

The OMB treatment of private and public incentives is wholly inconsistent, in that the draft guidelines delve in great detail into the purported problems attendant upon private incentives while ignoring the blatant problems inherent in government policymaking driven by the incentives created by majoritarian decision processes and bureaucratic efforts to maximize budgets. The OMB draft guidelines simply assume that government action will improve resource allocation by increasing the output of collective goods toward the efficient level, but that assumption ignores the incentives of government also to underprovide collective goods in favor of transfers to members of the majority coalition.

Agencies seeking larger budgets have incentives to exaggerate the importance of the problems that they seek to address through regulation, and to increase the range and complexity of their activities, thus increasing the difficulty of the information problem confronting Congress. A good example is the use of the “social cost of carbon” (SCC) as driven by analysis of climate phenomena with models that cannot predict the actual record on temperatures and other climate parameters, rather than the application of those actual data. The SCC is wholly artificial, driven by modeling projections of large and adverse climate impacts resulting from increasing atmospheric concentrations of greenhouse gases (GHG), despite the reality that there is no actual evidence of such serious adverse effects. Because the SCC framework exaggerates the economic costs of GHG emissions, it exaggerates also the benefits of reductions in those emissions. Regulations yielding a purported given reduction in GHG emissions can be asserted to yield large net economic benefits even if it yields changes in future climate phenomena effectively equal to zero or unmeasurable.

Thus have models replaced data in vast swaths of environmental analysis, public health and pandemic matters, and much more, and there is no obvious constraint preventing such analytic gameplaying in other contexts by the regulatory agencies supposedly required to adhere to the previous and newly proposed OMB analytic standards. Such politicized “analysis” will prove ubiquitous among the federal agencies because their budget maximization incentives are powerful, because regulation is and always must be shaped by political pressures, and because the regulatory bureaucracies are powerful interest groups both ideologically and in terms of their budgetary imperatives. The OMB draft guidelines offer no constraints on such analytic approaches.

The description in the draft guidelines of imperfect information as a “market failure” is preposterous. Because resources are limited always and everywhere, not all information is produced — even at a conceptual level, that is close to an impossibility — and all individuals must

pursue their myriad activities in a state of substantial ignorance. There is nothing inefficient about this state of affairs, and it does not represent a “market failure.”

Nor do information asymmetries — lower information costs in a given context for one set of parties than for others — change this central truth. Cheaper information would be welcome from the viewpoint of those confronted with information costs higher than those faced by others. That information costs are what they are is a reality; it is not a source of “inefficiency.”

The cost of acquiring information is what it is, and some transactions are lost because of it. At most, the presence of asymmetric information might yield a wealth transfer between parties to a transaction — the price might be higher or lower than would be the case in the absence of an information asymmetry — but that is not an inefficient outcome and certainly is not a “market failure.” Economics does not offer a theory of why one distribution of wealth is to be preferred — is more “efficient” — than another, and a regulatory analytic framework for government agencies that ostensibly pursues improvements in the efficiency of resource allocation has no business promulgating one.

The definition of “market power” in the draft guidelines is more-or-less a standard one, but the application of that definition in the draft guidelines is deeply problematic. How is “market power” to be measured? What is the appropriate tradeoff between market power and the exploitation of scale economies? What degree of market power under a given measurement metric is “too much?” How are market forces that reduce market power in a dynamic context — entry by new competitors or new technologies is the classic process — to be evaluated?

Moreover, the OMB discussion of why “market power” exists is poor. Precisely what constitutes a “barrier to entry for competitors?” OMB does not tell us, perhaps because much policy discussion of such “barriers” shunts aside the relevant issues under an apparent assumption that the answer is obvious. It is not, and the larger problem ignored by OMB is the question of why such “barriers,” however defined, exist. The implicit premise in the (cursory) OMB discussion is the absence of conditions that loosely would characterize a perfectly competitive market. But the competitive process itself is costly in terms of resource allocation; the “efficient” degree of competitiveness is unlikely in most contexts to be something approximating “perfect” competition. Accordingly, some “market power” is efficient, a subtlety that the OMB discussion ignores.

OMB fails to examine carefully the tradeoff between the achievement of scale economies — reduced costs — and a reduction of “market power,” a gap in the draft guidelines that allows for expansive regulatory activity driven by the whims of the regulators. The “control of inherently scarce resources” as a source of “market power” is a tautology: monopolization of an input yields monopoly power. More broadly, all resources are “scarce”; that is why their market prices are greater than zero. How “scarce” does a resource have to be in order to create “market power” sufficiently important to justify regulatory intervention? OMB fails to tell us.

“Intellectual property protections” certainly are a source of (temporary) market power — as they are designed to be — but it is not clear what point OMB is trying to make by including this parameter in its list of sources of market power. The cursory OMB reference to “privileged access to infrastructure” is wholly ambiguous; precisely who is offering such privilege? If the “privileged access” is the result of proximity to “natural infrastructure,” then such proximity ought to be reflected in land prices, thus eliminating any cost advantages attendant upon a purported “privileged access to infrastructure.” Any “control over commercial platforms or networks,”

whatever “control” means in this context, would carry an opportunity cost, again eliminating any cost advantage; and in the context of “market power,” OMB fails to tell us (or the regulatory agencies) how such control was achieved. Was there not some efficiency dynamic at work?

Nor does OMB discuss the “market power” of government generally, and the federal government in particular. The central purpose of a compound republic — federalism — is the imposition of competitive constraints upon government, and there is an obvious tradeoff between such competition and the achievement of scale economies in the provision of government services. The exercise of market power by regulatory agencies already has been discussed above in the context of efforts by agencies to maximize their budgets, but the same consideration affects the nature and stringency of the regulatory initiatives — the regulatory “prices” — that agencies can impose upon the private sector. OMB ignores this issue.

The OMB discussion of “behavioral biases” is no better. “Limitations on information processing” are a fact of life; the use of rules of thumb as a response is not a “market failure,” and OMB implicitly recognizes this reality in its observation about “limited attention, focus, and time.” The “decision-making biases” referenced by OMB also are the result of information costs; they are not a source of “inefficiency.”

The comedy highlight of the OMB discussion is the classification of “imperfect self-control” as a behavioral bias that “increases short-term well-being by less than it decreases future well-being,” that is, the use by individuals of discount rates too high. Is it the position of OMB that the inexorable political pressures shaping regulatory outcomes will not be driven by the political dynamics of the next election? Precisely what public choice model of policy formulation does OMB have in mind in its implicit assumption that private individuals use discount rates too high, but government officials systematically do not? At a more general level, what is the basis for the OMB premise that individuals exhibit systematic behavioral biases, but the staffs and officials of regulatory agencies will not?

The “environmental justice” concept is too narrow. Environmental quality is one component of “health” broadly defined, and it is clear from the scholarly literature that “health” is a “normal” good, that is, one the consumption of which rises with income or wealth. This is true for individuals and for economies as a whole. Lower-income individuals and households, precisely because their incomes are lower, consume less environmental quality, lower-quality diets, *ad infinitum*. Therefore, it is unsurprising that lower-income individuals and households tend to be located in areas with lower environmental quality; that is what they can afford. This is a reality regardless of the impacts of differences in environmental quality on “health,” that is, mortality and morbidity. Even if a lower level of environmental quality is merely unpleasant, that is a factor relevant to the ways in which individuals and households allocate their limited resources. Accordingly, the “environmental justice” issue is little more than the observation, or complaint, that the poor consume less environmental quality than others, that is, that they choose to allocate their resources in ways different from those exhibited by individuals and households wealthier.

More broadly, OMB fails to define the “distributional fairness” and “equity” concepts, undoubtedly because they are wholly subjective, and thus not measurable in any “objective” sense, leaving the definitions to the imaginations of the regulatory agencies. Nor does OMB explain why we should expect regulatory policies to advance such goals however defined, and the same is true for the longstanding problem traditionally described as the equity/efficiency tradeoff. Efforts by government to effect changes in the distribution of income or wealth necessarily affect resource

allocation in ways reducing aggregate productivity. Perhaps a given change in “distributional fairness” and “equity” is worth the attendant reduction in aggregate wealth; perhaps not. There is no “objective” measure of this tradeoff because we do not have an efficiency theory of the relative virtues of different distributional outcomes. OMB attempts to circumvent this obvious problem by arguing that the declining marginal utility of income means that a transfer from those better off to those worse off improves aggregate wellbeing. This is an utter *non sequitur*.

The draft guidelines are fatally flawed — indeed, perverse — and should not be finalized in the current draft form.