

Outline of Preamble

Agencies may find regulatory experimentation to be a useful way of reducing the risks associated with permanent rulemaking. Although there is no formal definition of “regulatory experimentation” in statute or regulations, Zack Gubler defines it as: “any regulatory action designed with the express purpose, from the outset, of generating information that would reasonably be expected to inform a more permanent decision down the road.” There are many factors that agencies must consider in deciding whether to engage in a regulatory experiment and how to structure the experiment. Furthermore, agencies must consider the legal requirements associated with rulemaking, including the requirements of the Administrative Procedure Act, and various executive orders and statutes that pertain to rulemaking.

The preamble to the recommendation will note that regulatory experimentation must be authorized by statute. Whether and when any given authority suffices are questions that resist legal generalization and are highly circumstantial, and this recommendation will not attempt to answer them. Agency counsel will need to address them in the context of reviewing particular programs.

Additionally, the preamble will address the following topics:

- What is a regulatory experiment?
- How does a permanent experimental rule differ from everyday retrospective review of existing rules (with appropriate citations to 2014-5)?
- What legal issues must agencies confront when conducting a regulatory experiment (i.e., arbitrary-and-capricious review, notice-and-comment, Executive Order 12,866, etc.)?
- What are the benefits and drawbacks of regulatory experimentation?

Furthermore, the preamble will explain that this recommendation is merely intended to show agencies what to consider when deciding on whether to use a regulatory experiment and to highlight some key considerations in structuring the same – not to advocate for or against agencies adopting regulatory experimentation in general or in any given instance.

Draft Recommendations

Note: The recommendations here contain more background detail than is normally the case in an ACUS recommendation (e.g. defining terms such as “randomized control trials.”) Such background details will be moved to the preamble in the next version.

The Decision Whether to Run a Regulatory Experiment

1. In deciding whether to engage in a regulatory experiment, agencies should focus resources on rules: a) that have significant potential benefits relative to the status quo; b) that have a low probability of resulting in these benefits; and c) for which failure is not likely to result in catastrophic losses. It is these types of high-risk, high-reward rules where regulatory experimentation is likely to generate the greatest value.

2. In deciding whether to engage in a regulatory experiment, agencies should consider conducting a break-even analysis. A break-even analysis allows the agency to estimate, given the costs of the experiment, the magnitude of the net benefits the rule must generate to justify the experiment. In conducting a break-even analysis for regulatory experimentation, agencies must estimate the costs of the experiment; the probability that the rule fails under experimentation (i.e. that the net benefits of the rule do not end up justifying adoption of the rule on a permanent basis); and the net benefits of the rule if the experiment fails. With that information, the agency can then calculate the net benefits the rule would need to generate in the best-case scenario to justify the experiment.

Structuring Regulatory Experiments

3. In structuring regulatory experiments, agencies should consider three key design choices.
 - a. First, they should consider the choice between, on the one hand, a randomized trial and a non-randomized trial.¹ If an agency determines that it has the discretion to choose, it should consider the costs and benefits of each approach:
 - i. RCT: In an RCT, the agency applies the rule to some firms (the treatment group) and not to others (the control group). The assignment of firms to the treatment and control group is done randomly. From an analytical standpoint, an RCT is superior to any other experimental structure. The costs of such an approach are the potentially market-distorting effects of applying a rule to some firms and not others; the public perception of lack of fairness in allowing some firms to not be subject to a rule; and the direct costs of the experiment itself, including the time devoted to ensuring that all technical and ethical requirements are complied with, and designing and conducting the experiment.
 - ii. Quasi-experimental approaches: Quasi-experimental approaches are used when firms are assigned to the treatment and control group based on some non-random criteria. For example, an agency may choose to apply a rule to all firms within its regulatory scope for a limited duration, thus creating a “control group” which consists of the same firms before the rule went into effect. Alternatively, an agency may decide to apply the rule to firms that meet a certain threshold (e.g. a certain number of employees), thus creating a “control group” which consists of firms that do not meet that threshold. Agencies should consider a variety of statistical methods for analyzing such “threshold” scenarios so as to isolate the effect of the experimental rule from potential confounding variables. These approaches often entail less of a fairness concern than RCTs, and perhaps raise fewer

¹ In deciding between these two general approaches, agencies must first determine whether statutory language limits its ability to choose. For example, if a statute permits an agency to regulate only firms that meet a minimum number of employees, that agency could not employ a Randomized Control Trial (RCT) to all firms within its regulatory scope.

political objections, but introduce numerous statistical challenges and are analytically less reliable than RCTs.

- b. Second, agencies should consider the choice between a temporary rule that automatically expires pursuant to a sunset provision and a permanent rule that does not. In choosing whether to structure the experiment as a sunset or permanent rule, agencies must first determine whether statutory language limits its ability to choose. Assuming the agency has discretion, it should choose the structure that is consistent with the probability that the experiment will be a success. If it is sufficiently likely that the experimental results will justify adopting, on a permanent basis, the rule that is the subject of the experiment, the agency should structure it as a permanent rule when it adopts the experiment. Otherwise, it should be structured as a sunset rule, which expires automatically once the experiment is completed.
- c. Agencies should give considerable thought to how to ensure that correct lessons are drawn from the experiment. To the extent possible in light of resource constraints, agencies should consider the following methods of assessing their regulatory experiments:
 - i. Commissioned studies: Experts within the agency, including statisticians, economists, and other data experts, analyze the data from the regulatory experiment.
 - ii. Public calls for papers: Agencies announce a request for outside consultants to analyze the data.
 - iii. Expert panels and open forums: Agencies assemble experts internally or from the outside to analyze and discuss the data. If outside experts are brought in to provide advice to agencies regarding the experiment, agencies may need to meet the requirements of the Federal Advisory Committee Act.

In deciding which of these options to choose, agencies should consider a number of factors, including the scope of the issues and the issues' need for expert analysis; the agency's internal expertise; and the availability of, and the agency's awareness of, outside experts.

Legal and Other Considerations

4. Executive agencies should give special consideration to whether a regulatory experiment requires review by OIRA. Agencies should strive to determine whether the regulatory experiment meets Executive Order 12866's definition of a "significant regulatory action" by, for example, estimating the anticipated economic impact of the experiment. The agency should also work closely with OIRA to determine whether review makes sense for a given regulatory experiment.

5. Agencies should consider how stakeholders are likely to react to a regulatory experiment. The preferences of stakeholders are likely to be more complicated when it comes to a regulatory experiment than in the non-experimental context. This is because opposition to a regulatory experiment can come not only from stakeholders who oppose the rule that is the subject of the experiment but also from those who favor the rule but simply do not think it should be adopted on an experimental basis. In both cases, agencies can likely encourage stakeholder support by marshaling theoretical work from the relevant community of experts suggesting that, even though the theory alone would not necessarily justify adopting the rule on a permanent basis, it would justify making it the subject of an experiment.