CONGRESSIONAL BUDGET OFFICE
U.S. Congress
Washington, DC 20515

Douglas W. Elmendorf, Director

October 31, 2011

Honorable James Lankford
Chairman
Subcommittee on Technology, Information Policy,
Intergovernmental Relations and Procurement Reform
Committee on Oversight and Government Reform
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

This letter responds to your request for CBO's input regarding H.R. 373, the Unfunded Mandates Information and Transparency Act of 2011, as ordered reported by the Subcommittee on Technology, Information Policy, Intergovernmental Relations and Procurement Reform on September 21, 2011. Because that bill would directly affect CBO's work, I appreciate the opportunity that CBO had to express its concerns about the legislation prior to the subcommittee mark-up, and the continuing consultation since then between the committee staff and the CBO staff responsible for the agency's mandates work.

The two main questions that have arisen concern the scope of the mandate costs that are to be encompassed by CBO's estimates and the definition of a federal mandate as it applies to federal grant programs and other voluntary federal programs. In sum:

- The impact of including a directive in the Unfunded Mandates Reform Act (UMRA) for CBO to include "indirect costs" as a part of its analysis of mandate costs would depend on the meaning of that term. If the intent is for CBO's estimates to include costs, such as lost income, that would be incurred as a result of the mandate—regardless of whether those costs are borne by the mandated entity or passed on to other entities such as consumers or workers—CBO's mandate cost estimates already include those amounts. If the intent is for CBO to include an analysis of the distributional or macroeconomic effects of mandates, such estimates are not feasible as a routine part of analyzing reported legislation for mandates.

- Changing UMRA's definition of federal mandate to include conditions for receiving federal grants and for participating in other types of voluntary federal programs would significantly increase the number of bills defined as containing mandates, make cost estimates more difficult and time-consuming to complete, and considerably slow the process of providing mandate statements to the Congress. Fewer delays and a more efficient use of CBO's resources would result if, instead, committee chairmen or ranking members were to request CBO analyses of those legislative provisions that most concerned them.

Indirect Costs

For each bill reported by an authorizing committee, UMRA directs CBO to provide "the total amount of direct cost" of complying with the intergovernmental or private-sector mandates in that bill; direct costs are defined as the "aggregate estimated amounts" that public and private entities would incur as a result of complying with a mandate. That total is used to determine whether mandate costs in a bill exceed the relevant annual thresholds established in UMRA. (For 2011, those inflation-adjusted thresholds are $71 million and $142 million for intergovernmental and private sector mandates, respectively.)

You asked whether CBO takes "indirect costs" into account when estimating those aggregate costs. The answer is "yes," if that term applies to costs such as lost income or to costs that are passed on to consumers or workers; CBO's mandate cost estimates already include those amounts. Although UMRA uses the term "direct costs" to describe those aggregate estimated amounts—possibly leaving the impression that the costs currently included in mandate estimates are narrowly defined—the law requires CBO to include not only additional expenditures but also lost tax revenues for state, local, and tribal governments. In addition, CBO includes forgone business profits when estimating the costs of private-sector mandates.[1] In other words, CBO already takes into account a broad range of potential costs that would result from imposing new mandates. (In fact, UMRA makes no mention of indirect costs, and CBO does not make such a distinction.)

As approved by the subcommittee, H.R. 373 would require CBO to include in its estimates the "indirect costs" from complying with a mandate, defined as costs "other than direct costs… [including] lost income and secondary monetary costs." In fact, CBO already includes lost income as part of the compliance cost it identifies for mandated entities. Hence, adding "lost income" as an indirect cost to be estimated would not change how CBO prepares mandate cost estimates. We are uncertain as to the meaning of

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1. For example, CBO's estimate for H.R. 1254, the Synthetic Drug Control Act of 2011, included the forgone income from lost sales in the estimated cost of a ban on certain synthetic chemicals. (See http://www.cbo.gov/ftpdocs/124xx/doc12486/hr1254.pdf.) Also, CBO's estimate for H.R. 3678, the Internet Tax Freedom Act Amendments Act of 2007, identified the amount of lost revenues as the mandate cost of extending a moratorium on certain state and local taxation of online services and electronic commerce. (See http://www.cbo.gov/ftpdocs/87xx/doc8701/hr3678.pdf.)

the term “secondary monetary costs”; because CBO already estimates costs as broadly defined, it is unclear to us what costs that term would encompass that are not already included in CBO’s estimates.

One way to clarify the Congress’s intent would be to modify the definition of “direct costs” to indicate that, in the case of private-sector mandates, those costs include amounts that companies would forgo in profits to comply with the mandate. (The definition of direct costs for intergovernmental mandates already includes amounts that state, local, and tribal governments would be prohibited from raising in revenues to comply with federal mandates). Another possibility would be to just use the term “costs” (rather than “direct costs”), so as not to suggest that there are some costs that should not be included.

It is possible that some think of the term “indirect costs” as including the secondary or distributional effects that would result from a mandate. It is true that legislation that would result in additional costs for mandated entities may prompt those entities to pass costs along to workers, other sectors in the economy, or consumers. In fact, as described above, CBO estimates the total costs of complying with federal mandates, *including amounts that may be passed on to other entities such as consumers and workers*. CBO does not, however, project how the burden of those costs would ultimately be distributed. We have provided such information on occasion in the past at the request of the Congress, but those distributional analyses can take a significant amount of time so it would not be possible to prepare such analyses for most legislation.[2] Providing distributional analyses for every bill with mandates or with changes in conditions of assistance would be impossible given the time constraints that the legislative process imposes. (CBO currently prepares several hundred mandate statements every year.)

It is also possible that some people may use the term indirect costs to mean the macroeconomic effects of a particular piece of legislation. However, such analyses are difficult, complicated, and time-consuming; CBO’s mandate estimates do not—and could not in any practical way—include the effects of each bill on gross domestic product, employment, or inflation. (Under the longstanding procedures governing the Congressional budget process, CBO’s estimates of the federal budgetary impact of legislation do not encompass such effects.) To the extent practicable, however, when preparing mandate statements, CBO takes into account anticipated behavioral responses by mandated entities that would result from enacting legislation.

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2. For example, see the CBO study entitled *The Economic Effects of Legislation to Reduce Greenhouse-Gas Emissions,* September 2009. http://www.cbo.gov/ftpdocs/105xx/doc10573/09-17-Greenhouse-Gas.pdf

Changes in Conditions Governing Grants and Other Voluntary Federal Programs

Other provisions of H.R. 373 would change the definition of a federal mandate to include conditions of federal assistance (that is, federal grants) and duties surrounding participation in voluntary federal programs. The bill would require committee reports to include a comparison of the funding authorized in a bill with the costs of those newly defined mandates.

Providing this kind of information about conditions of federal assistance for committee reports would present significant challenges:

- By redefining a federal mandate to include the conditions associated with all voluntary federal programs and grants, H.R. 373 would greatly increase the number of bills containing mandates and the number of provisions in each bill that might be considered mandates under UMRA. (CBO already reviews for mandates legislation that would affect a number of large grant programs because UMRA includes special rules for determining whether legislation regarding those programs contains mandates.)[3] CBO expects that this new definition of mandate would increase the number of grant programs that might involve mandates to about 200. In addition, the new definition would sweep in a host of other programs that are voluntary in nature, and new requirements in those programs would then be mandates.

- Providing a comparison of the funding authorized in proposed legislation with the estimated costs of implementing new conditions, without limiting such comparisons to costs exceeding the thresholds established in UMRA, would require CBO to provide estimates of the costs of conditions at a level of detail not currently required for other types of mandates. Such comparisons could be time-consuming, depending on the number of changes made to grant programs and the complexity of the new requirements.

As a result, mandate cost estimates would be more difficult and would take longer to complete, and the process of providing mandate statements to the Congress would be slowed.

Nevertheless, it is clear that adding new conditions to existing large grant programs without providing additional funding for those programs can have important implications for state, local, and tribal budgets, and CBO's goal is to provide instructive and timely

3. UMRA defines large entitlement programs as a "then-existing federal program under which $500 million or more is provided annually to state, local, or tribal governments under entitlement authority." Those programs as listed in the conference report for Public Law 104-4 include: Medicaid; Temporary Assistance for Needy Families; child nutrition programs; Food Stamps; the Social Services Block Grant; Vocational Rehabilitation State Grants; grants for foster care, adoption assistance, and independent living; family support payments for the Job Opportunities and Basic Skills program; and Child Support Enforcement.

information to the Congress about pending legislation. Section 102 of UMRA (2 U.S.C. 602(h)) provides a possible solution: It directs CBO to provide, to the extent possible and at the request of the chairman or ranking member of a committee, additional studies on federal mandates. Instead of changing the definition of mandates to encompass all conditions of assistance, allowing chairmen and ranking members to request additional information about proposed grant conditions in particular cases would focus CBO's limited resources on the issues of greatest concern to the Congress.

I hope this information is helpful. If you have further questions, please don't hesitate to contact me, Patrice Gordon (for private-sector mandates), or Leo Lex (for intergovernmental mandates).

Sincerely,

Douglas W. Elmendorf

Douglas W. Elmendorf
Director

Identical letter sent to the Honorable Gerald E. Connolly.