

Fiscal Notes 101: Introduction to Regulatory Impact Analysis

OSBM
January 2020



What is a regulatory impact analysis or fiscal note?



A **tool** to identify, quantify, and communicate the anticipated effects of rule changes



A structured **evaluation of tradeoffs** - weighs the benefits of regulatory changes against their costs



Goals:

- Improve **rule design**
- Inform **decision-making**
- Increase **transparency** about rule changes and expected outcomes for regulated entities and interested parties



What is a regulatory impact analysis or fiscal note?

Addresses key questions for decisionmakers and the public:

- Why is a rule change necessary?
- How do the proposed changes address the issue?
- What are the expected outcomes?
- Who will be affected?
- Are the benefits likely to exceed the costs? By how much?
- How confident can we be? What are the biggest uncertainties?
- Are we getting the biggest bang for our buck compared to other approaches?

Examples

Approved regulatory impact analyses are published on
OSBM's website

<http://www.osbm.nc.gov/management/regulatory>



When does G.S. 150B 21.4 require an impact analysis?

Rule packages with **state government** impact, OR
Rule packages with **local government** impact, OR
Rule packages with **substantial** economic impact:
costs + benefits > \$1M in any year

A **rule package** is the group of permanent individual rules that the agency is requesting to publish together and that constitutes the new policy the agency is proposing to implement

\$Costs	\$ Benefits	\$Impact
-\$1M	\$0	=\$1M
-\$0.5M	+\$0.5M	=\$1M
\$0	+\$1M	=\$1M



Special Cases: Periodic Rule Readoptions

An analysis is required for readoptions (G.S. 150B-21.3A) if **all** criteria apply:

- Rule readopted **with substantive change** that requires publication in Register (G.S. 150B-21.2(c))
- Change results in **state, local, or substantial impact**
- **At least one rule** in the package the agency is proposing to adopt together **creates a net cost on any part of the regulated community**
 - ^ Different than “standard” rulemaking – if all rules reduce burden on regulated community, no analysis required

Baseline is current rule, unless expired

All other requirements for analysis apply



Special Cases: Federally Required Rules

Send to OSBM before Publication:

- **Certificate of federal requirement**
 - Federal law/regulation that requires rule or places conditions on the receipt of federal funds
 - Reason if all or part of rule is not required by or exceeds federal law
 - This information can be incorporated into the analysis
- **Scaled down fiscal note** if identical to federal regulation the agency is required to adopt
 - Rule change is not considered substantial in this situation[G.S. 150B-21.4(b1)].
 - Baseline: federal rule if funding depends on adoption

Up Next...

- What goes into the fiscal note document
- The analysis process



Cover page information

Impact Analysis Title with Name of Rule Package

Agency: Department or Commission
Division
Section

Rule Citation(s): 15A NCAC 13A .0101, .0102, .0103, .0104

Agency Contact: Name, Title
Email
Phone

Rulemaking Authority: N.C.G.S. citation(s) to authorizing legislation

Impact Summary: State Government: Yes/No
Local Government: Yes/No
Private Entities: Yes/No
Substantial Impact: Yes/No



The 7-step process

1. Define Problem
2. Identify Solution, Alternatives
3. Identify Impacts
4. Quantify and Monetize Costs and Benefits
5. Calculate Net Impact (Net Present Value)
6. Conduct Sensitivity Analysis
7. Evaluate Results, Make Decisions



Analysis process: Define the problem

What is the **rationale for the rule change**?

- Why is the rule change needed?
- What improvements does the agency hope to achieve?
Or what negative outcomes to avoid?
- Why should we care?

What is the cause of the problem?

What is the size and scope of the problem?

“To make changes required by Session Law XXXX...”

“To readopt rules in accordance with G.S. 21.3A....”

“To update rules...”

Above statements are important background but they do not define the problem and rationale for the changes!



Analysis process: Identify solutions, alternatives

Describe the **proposed rule changes**

- What are the new requirements or processes?
- Explain how the rule addresses the underlying cause(s) of the problem

Consider rule **alternatives**

- Are there approaches that are more/less effective than others? Higher/lower cost than others?
- Consider alternatives to regulation or modified implementation
- Which option provides the right balance? May be an iterative process as you work through the analysis

Substantial impact rule packages

- Must discuss at least two alternatives and why they were dismissed



Analysis process: Identify impacts

Impact = **costs and benefits** resulting from rule change

Impact > budgetary/financial costs or savings

Impact relates to the purpose and necessity of the rule

Common Impacts: **All Subject Areas**

Changes (+ or -) in...

- Time, money, or other resource investments for rule compliance and implementation
 - New workload or time savings
 - New expenditures or cost savings
 - Change in revenue
 - Operational efficiencies
 - Turnaround time



Analysis process: Identify impacts

Impact = **costs and benefits** resulting from rule change

Impact > budgetary/financial costs or savings

Impact relates to the purpose and necessity of the rule

Common Impacts: **Environmental Rules**

Changes (+ or -) in...

- Risk of disease, injury, or premature death
- Healthcare expenditures
- Commercial, recreational, consumptive, and aesthetic value of natural resources
- Ecosystem services value
- Treatment and remediation needs



Analysis process: Identify impacts

Impact = **costs and benefits** resulting from rule change

Impact > budgetary/financial costs or savings

Impact relates to the purpose and necessity of the rule

Common Impacts: **Health Rules**

Changes (+ or -) in...

- Risk of disease, injury, or premature death
- Healthcare expenditures
- Lifetime earnings
- Government services utilization and associated costs
- Criminal justice involvement and associated costs



Analysis process: Identify impacts

Impact = **costs and benefits** resulting from rule change

Impact > budgetary/financial costs or savings

Impact relates to the purpose and necessity of the rule

Common Impacts: **Education Rules**

Changes (+ or -) in...

- Student learning and skill proficiency
 - Indicators such as graduation rate, test scores, other proxies
- Lifetime earnings
- Healthcare expenditures, risk of disease
- Government services utilization and associated costs
- Criminal justice involvement and associated costs



Analysis process: Identify impacts

Impact = **costs and benefits** resulting from rule change

Impact > budgetary/financial costs or savings

Impact relates to the purpose and necessity of the rule

Common Impacts: **Occupational Licensing Rules**

Changes (+ or -) in...

- Public health and safety, consumer information
- Access to services
- Consumer price of occupational services
- Occupational earnings



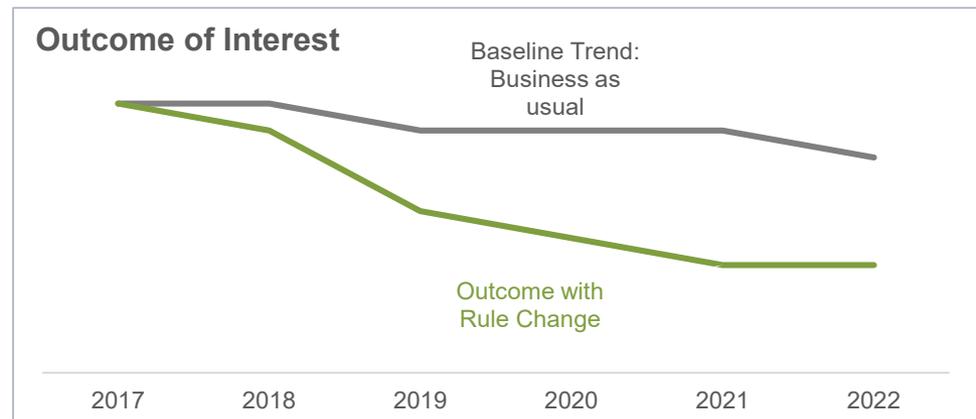
Analysis process: Identify impacts

Change in behaviors -> Change in outcomes, impact

How will the future be different **compared to the status quo baseline?**

Baseline

- **Includes** current economic and demographic trends, current rules and standalone statutes



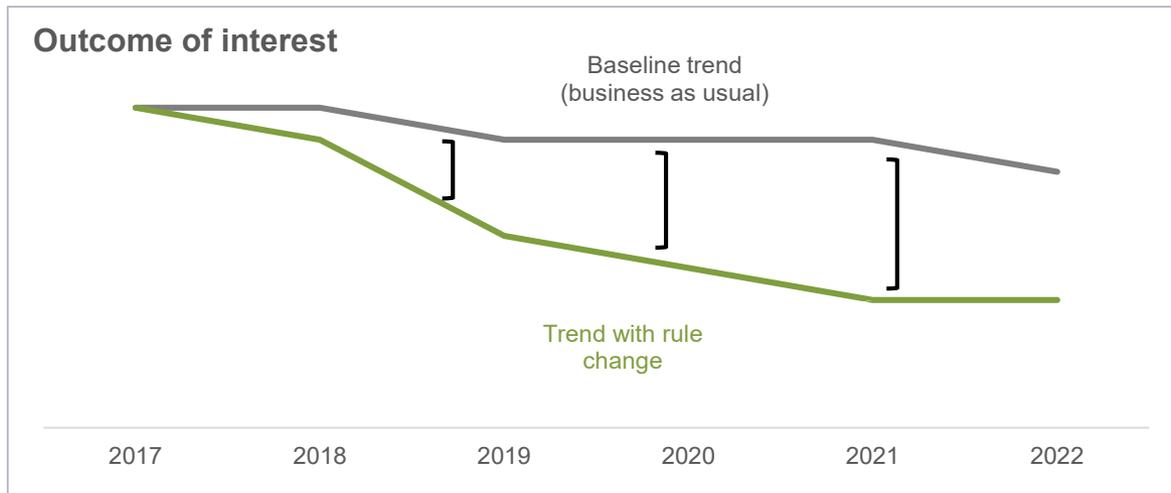
- **Excludes** existing policy not yet in rule, statutes that require rules for implementation, and “already compliant” argument



Analysis process: Quantify, monetize costs and benefits

First quantify the **size of the rules' impact**

- *How much* will the world change as a result of the rule?
- *How big* is the difference between the expected outcomes and the baseline outcomes?



Then monetize the **value** of that impact **over time**

- Methods and data will be impact-specific



Analysis process: Quantify, monetize costs and benefits

Sources used to identify, quantify, monetize impacts:

- Administrative and program data
- Subject area research literature (type and size of impact)
- Economic literature (social value of nonmarket impacts)
- Market data, prices
- State and national demographic data, employment cost data, industry data, cost indices
- Surveys of regulated entities, interested parties
- Experiences in other states
- Professional experience
- Federal regulatory impact analyses, scaled to NC

Research + Data + Context + Experience = Evidence

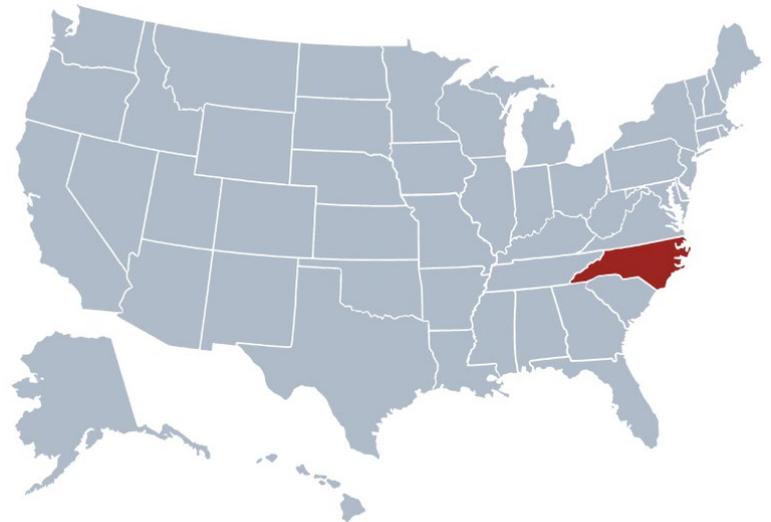


Analysis process: Quantify, monetize costs and benefits

Impacts should be analyzed from **multiple perspectives**

- State government
- Local government
- Relevant private sector entities (regulated entities, consumers, nearby residents, students, etc)
- General population

Scope of the analysis is NC –
exclude impacts on entities
outside the state borders





Analysis process: Quantify, monetize costs and benefits

It is not always possible to fully monetize rule impacts

- Benefits like better health or environmental quality can be especially difficult to capture due to research and data limitations

Quantify to the greatest extent possible

Provide context for unquantified impacts with best available information

- Identify expected impacts, and evidence
- Characterize the likely magnitude or frequency of the costs and benefits, if possible
- State assumptions, discuss relevant unknowns, limitations
- Conduct sensitivity analysis, if applicable



Analysis process: Quantify, monetize costs and benefits

Include **opportunity costs/savings** such as staff time

- Opportunity cost is the value of the activity or resource investment given up because of doing something new
- The use of any resource, including a person's time, has an opportunity cost because resources are limited and we are forced to make trade-offs
- Opportunity costs are not always budgetary costs

Choose a **time horizon** appropriate for future impacts

- Far enough to capture all expected outcomes
- At least one full cycle or cohort

Account for **transfers** between groups

- Example: Fee is a cost to regulated entity and benefit to state



Analysis process: Calculate net impact

Costs and benefits may continue into the future and may change over time

Discounting is a way of adjusting costs and benefits occurring at different times into a common period so that they can be compared

- Discounting accounts for the time value of money

Net Present Value (NPV) represents the value of the expected effect of the rules to North Carolina as a whole

- The sum of the net impact (benefits minus costs) over time, discounted to a present-day dollar value equivalent
- Bigger NPV = NC better off



Analysis process: Calculate net impact

Example:

Cost **-\$10** next year (Yr1)

Benefit **+\$100** in two years (Yr2)

Discount rate 7% (0.07)

	Yr 0 (today)	Yr 1	Yr 2
Costs		(-10)	
Benefits			+100
Discounted to common period		(-9)	+87
NPV	\$78		

Discounted **cost** in Yr0 (today)= $-\$10 / (1+0.07)^1$ - \$9

Discounted **benefit** in Yr0 (today)= $+\$100 / (1+0.07)^2$ + \$87

therefore...

Net Present Value in common Yr0 terms= $\$87 - \9 +\$78



Analysis process: Calculate net impact

For complex analyses, consider a summary table of impacts by affected entity and year, including unquantified impacts

	Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6
BENEFITS						
State Gov't						
Benefit A	-	274,600	452,300	472,700	494,300	516,200
Local Gov't						
Benefit C	-	30,200	49,800	52,000	54,400	56,800
Private						
Benefit D	-	199,300	321,100	330,500	339,700	348,500
Benefit E	-	200	200	200	200	200
Total Benefits	-	504,300	823,400	855,400	888,600	921,700
COSTS						
State Gov't						
Cost A	186,400	250,300	262,300	274,100	286,600	299,400
Cost B	10,600	-	-	-	-	-
Local Gov't						
Cost C	-	16,100	16,800	17,600	18,400	19,200
Private						
Cost D	-	105,900	108,600	111,800	114,900	117,900
Total Costs	197,000	372,300	387,700	403,500	419,900	436,500
Net Impact	(197,000)	132,000	435,700	451,900	468,700	485,200
NPV (in Yr1 dollars)	1,379,317					



Analysis process: Conduct sensitivity analysis

All rule packages: Describe key **uncertainties**, **assumptions**, research or data **limitations**

Substantial impact rule packages: conduct **sensitivity analysis**

- Show the effect of varying key inputs within a plausible range
- How do different assumptions (typically both higher and lower estimates) change the NPV of benefits, costs, or both?



Analysis process: Evaluate results

Recap - completed analysis should convey to stakeholders:

- Why is a rule change necessary? What problems do the rules address?
- How do the proposed changes address the issue?
- What are the expected outcomes (costs and benefits)?
- Who will be affected?

Decisionmakers can make judgements about:

- Relative magnitude and distribution of costs and benefits
- Likelihood of benefits exceeding costs
- Cost effectiveness compared to other approaches
- Degree of confidence in expected outcomes

Questions About the Analysis Process?

Up Next...

- OSBM's Role
- Tips for approval



OSBM's Role

Reviews rule analysis for **adherence to G.S. 150B** (everyone) **and E.O. 70 requirements** (cabinet agencies) before publication of state, local, or substantial impact rules

Determines if the analysis **comprehensively identifies and assesses** the impacts on all affected entities

Certifies that **sufficient state funds** are available to implement the rule (G.S. 150B-21.4(a))

- Rule changes **may not require** an expenditure of more money than is budgeted



OSBM's Role

Establishes if the agency adhered to economic **principles in G.S. 150B-19.1** for substantial impact rules

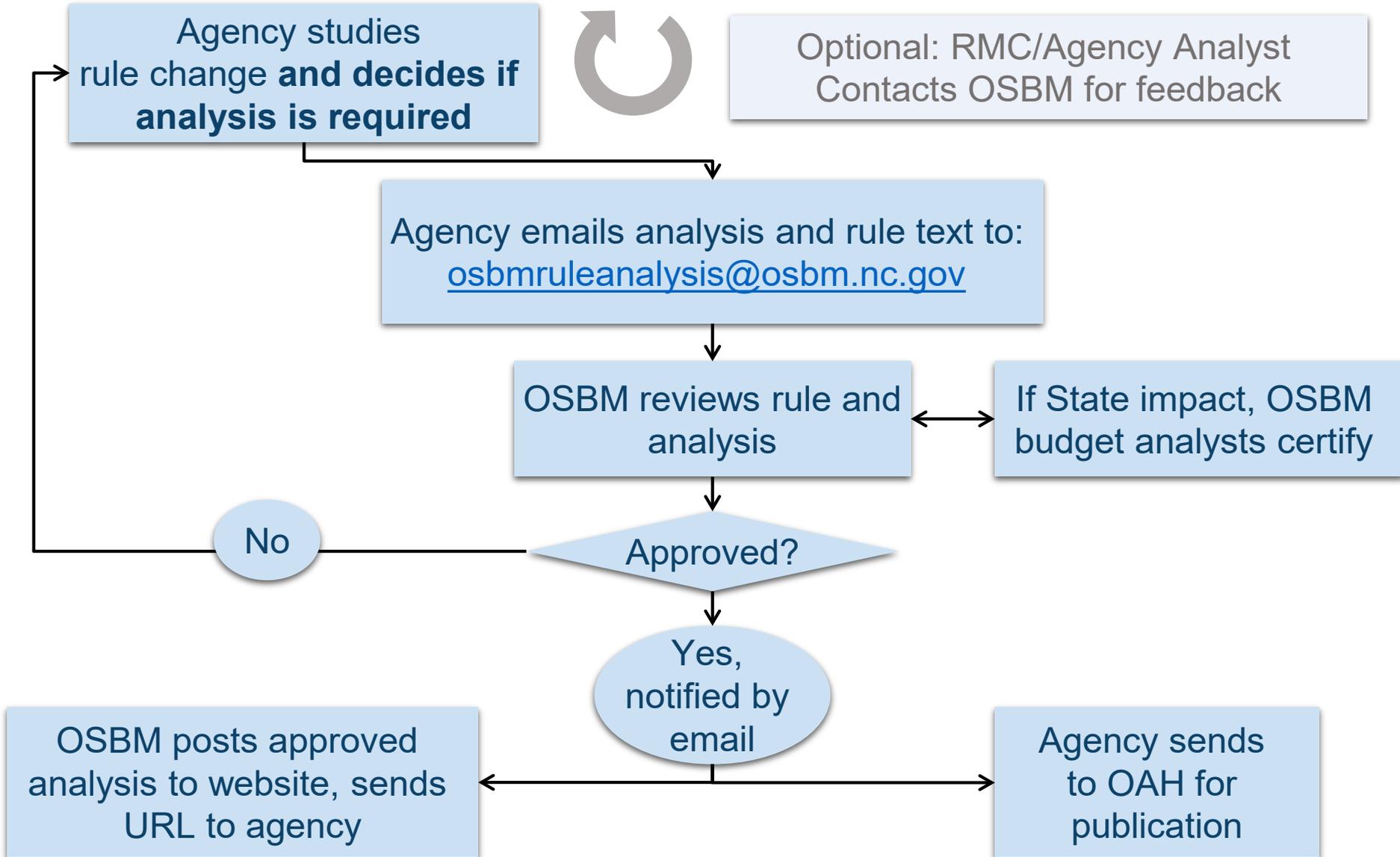
- 1) Be expressly authorized and serve the public interest
- 2) Seek to reduce burden on regulated entities**
- 3) Be clear, unambiguous, and necessary
- 4) Consider cumulative effect of rules
- 5) Consider sound, reasonably available information**
- 6) Achieve rule objective in cost-effective and timely manner**

Additional Principles for Cabinet in E.O. 70 Section 2

- Quantify costs and benefits to greatest extent possible
- Identify and assess alternatives
- Encourage public comment and ensure access to information
- Coordinate rule action with other agencies for overlap
- Update analysis for significant changes before adoption

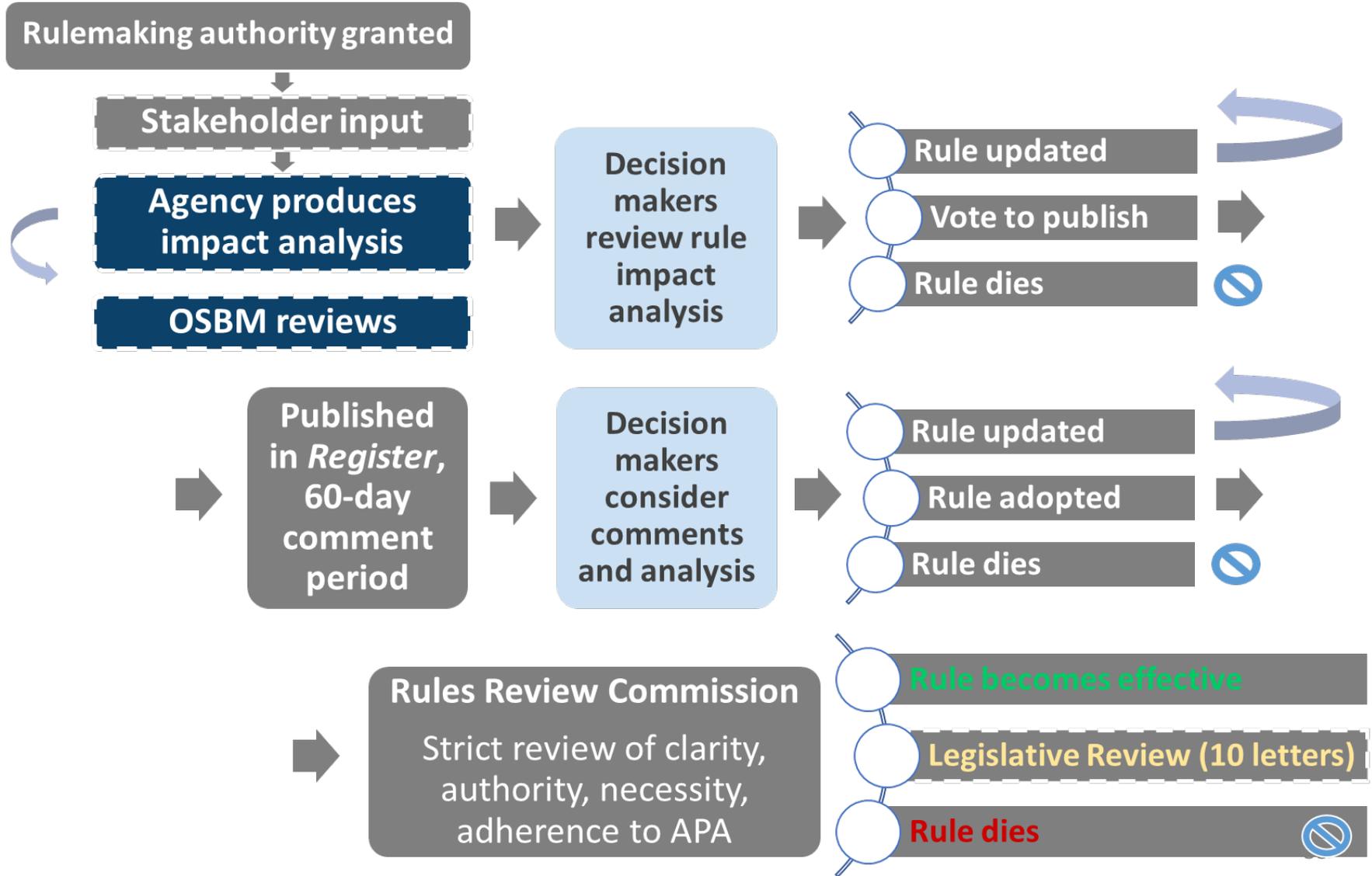


OSBM approval Process





Rulemaking process and next steps





Tips for approval

Timeline management

- No “standard” timeline for fiscal note completion – depends on complexity of the rule, magnitude of impact, strength of the analysis and need for revisions
- Allow enough time for revisions, accounting for internal agency and OSBM turnaround time
- For rules with substantial economic impact, complex or controversial changes, and large rule packages:
 - Recommend initial conversations about reason for rule change, proposed interventions, and analysis approach at earliest opportunity
 - Recommend submitting first complete fiscal note draft for comment at least 60 days in advance (partial drafts earlier)
- For all other rule packages: recommend submitting first complete draft for comment at least 30 days in advance
- **Involve OSBM early!** (even before rule text is finalized)



Tips for approval

Capture the change in future outcomes **attributable to the rule**, compared to status quo baseline

Assess the size of the expected impact – Utilize internal agency data, external research, program evaluations, modeling, etc

Quantify costs and benefits as much as possible

- Identify expected outcomes, and the evidence
- Remember to include opportunity costs
- Consider each group affected by the rule change
- Choose time horizon appropriate for future impacts

Make reasonable assumptions, clearly state limitations, and use sensitivity analysis to understand the impact of key inputs

Describe non-monetized impacts and provide context about likely magnitude



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The Administrative Procedure Act
(G.S. 150B)

OSBM Rule Analysis Website:

<http://www.osbm.nc.gov/management/regulatory>

- Training slides
- Approved fiscal notes by agency
- OSBM Budget Manual (Chapter 7)

Regulatory Impact Analyses

