

Washington University in St. Louis

## Washington University Open Scholarship

---

Murray Weidenbaum Publications

Weidenbaum Center on the Economy,  
Government, and Public Policy

---

Formal Publication 35

11-1-1980

### Costs of Regulation and Benefits of Reform

Murray L. Weidenbaum

*Washington University in St Louis*

Follow this and additional works at: [https://openscholarship.wustl.edu/mlw\\_papers](https://openscholarship.wustl.edu/mlw_papers)



Part of the [Economics Commons](#), and the [Public Policy Commons](#)

---

#### Recommended Citation

Weidenbaum, Murray L., "Costs of Regulation and Benefits of Reform", Formal Publication 35, 1980, doi:10.7936/K7NS0S11.

Murray Weidenbaum Publications, [https://openscholarship.wustl.edu/mlw\\_papers/54](https://openscholarship.wustl.edu/mlw_papers/54).

Weidenbaum Center on the Economy, Government, and Public Policy — Washington University in St. Louis  
Campus Box 1027, St. Louis, MO 63130.

Previous titles in this series currently in print:

13. **Corporate Planning Versus Government Planning,**  
Murray L. Weidenbaum and Linda Rockwood
16. **How Britain Went Wrong,** Robert Bacon and Walter Eltis
17. **Vertical Control by Labor Unions,** Frederick R. Warren-Boulton
23. **Cutting the Size of Big Government,** Murray L. Weidenbaum
26. **Workers and the Hours Decision,** Edward Kalachek
28. **Control of the Bureaucracy: A Mismatch of Incentives and Capabilities,**  
Morris P. Fiorina
29. **Some Economic Aspects of Ethical-Behavioural Codes,**  
Roland N. McKean
30. **The Future of Business: Shock or Stability?** Murray L. Weidenbaum
31. **Directory of Federal Regulatory Agencies,** Ronald J. Penoyer
32. **The Congressional Budget Process: Some Views from the Inside,**  
proceedings of a conference
33. **Consumer Safety,** Barry R. Weingast
34. **Public Policy: No Longer a Spectator Sport for Business,**  
Murray L. Weidenbaum

Additional copies are available from:

Center for the Study of American Business  
Washington University  
Campus Box 1208  
St. Louis, Missouri 63130



## Costs of Regulation and Benefits of Reform

by Murray L. Weidenbaum



Center for the  
Study of  
American Business  
Washington University - St. Louis

## **Costs of Regulation and Benefits of Reform**

by Murray L. Weidenbaum

This booklet is one in a series designed to enhance the understanding of the private enterprise system and the key forces affecting it. The series will provide a forum for considering vital current issues in public policy and for communicating these views to a wide audience in the business, government, and academic communities. Publications will include papers and speeches, conference proceedings, and other research results of the Center for the Study of American Business.

Progress toward deregulation of the airlines and the elimination of many silly job safety regulations have created the notion that government regulation is entering a declining phase in the United States. The facts, however, support the reverse view. The pace of regulation of business is continuing on an upward trajectory. The number of agencies, regulatory programs, and authorizing statutes—and the budgets to carry them out—are all continuing to grow.

Moreover, a very substantial further expansion of regulation is in the government pipeline. Many of the laws passed in recent years are in the early growth stages of development. As the U.S. Council on Environmental Quality pointed out in its recent annual report (1978), current estimates of the burden of regulation “do not yet include many costs associated with the hazardous waste section of the Resource Conservation and Recovery Act of 1976, the Toxic Substances Control Act of 1976, and 1977 Amendments to the Federal Water Pollution Control Act, and the 1977 Amendments to the Clear Air Act.” For most of this legislation, the Council pointed out that the Environmental Protection Agency (EPA) is still in the process of developing its final regulations, the effects of which will not be felt until business and government begin to implement them.<sup>1</sup>

Similar patterns prevail in other areas. The Occupational Safety and Health Administration (OSHA) has recently promulgated a generic carcinogenic standard which, when implemented, is likely to generate compliance costs greater than the total existing array of OSHA standards.<sup>2</sup> The National Highway Traffic Safety

---

Mr. Weidenbaum is Director of the Center for the Study of American Business at Washington University in St. Louis. An earlier version of this report was prepared for the Key Issues Lecture Series at New York University, October 1979.



Administration is pursuing mileage goals at a pace which will test the outer limits of the survival capacity of the relatively few American companies that still produce motor vehicles.<sup>3</sup> In light of these expansions of regulatory activity, surely some perspective is useful.

### THE NEW WAVE OF GOVERNMENT REGULATION

It is hard to overestimate the current rapid expansion of government involvement in business in the United States. Certainly the majority of public policy changes affecting business-government relations in recent years has been in the direction of greater governmental intervention—environmental controls, job safety inspections, equal employment opportunity enforcement, consumer product safety regulations, energy restrictions, and so forth. Indeed, when we attempt to look at the emerging business-government relationship from the business executive's viewpoint, we see a very considerable public presence in what historically have been private affairs.

No one who operates a business today, neither the head of a large company nor the corner grocer, can do so without considering a multitude of government restrictions and regulations. His or her costs and profits can be affected as much by a bill passed in Washington as by an executive action in the front office or a customer's decision at the checkout counter. Management decisions fundamental to the business enterprise are increasingly subject to governmental influence, review or control.

In fact, the term "regulated industry" has become archaic. Every industry in the United States is feeling the rising power of government regulation in each major aspect of its day-to-day operations. If we could accurately measure the pervasiveness of government intervention, we would not find the economists' favorites—electric utilities and railroads—at the top of the list. More likely, we would encounter such giants of the manufacturing sector as automobile, aerospace, and chemical companies, with the oil industry and health services not too far behind.

Because of the rapid proliferation of government regulatory activity in recent years, it should be useful to attempt to measure this

phenomenon. Let us try to do so by focusing on the resources that are required to carry out these efforts. That measurement should provide an upper limit to the amount of savings that could result from regulatory reform.

### THE COSTS OF GOVERNMENT REGULATION

The costs that result from government regulation of business can be analyzed by grouping them into three categories:

1. *The cost of administering the regulatory agencies:* This is the smallest portion and the easiest to measure. The data are also useful indicators of changing trends and relationships in the entire regulatory network.
2. *The indirect cost of compliance by the private sector:* This element is much larger and more difficult to measure. However, as we will see, there is a substantial literature on individual programs which can be drawn upon to develop useful aggregate estimates.
3. *The induced effects of regulation:* This is the most diffuse and elusive aspect of measuring the impacts of regulation. Yet there are important indicators which show that regulation has extremely substantial, long-term effects on innovation, capital formation, and the structure of industry.

#### The Direct Costs of Regulation

The expansion of regulation in the United States can be seen most readily in the steady increase in the number of major regulatory agencies established by the Congress—from fourteen prior to 1930, to a little over two dozen in 1950, to a present total of 57. As shown in Figure 1, the most rapid expansion occurred not in the New Deal period of the 1930s, but rather during the 1970s.<sup>4</sup>

The initial and direct effects of government regulation can be measured by the budgets of the regulatory agencies themselves, which are presented in Table 1. The figure includes such government administrative costs as salaries of inspectors, office supplies, and the government's own paperwork flow. These are the expenses of writing, managing, publishing, and policing regulations.<sup>5</sup> The great

**TABLE 1**  
**Expenditures on Federal Regulatory Activities**  
(Fiscal Years, Millions of Dollars)

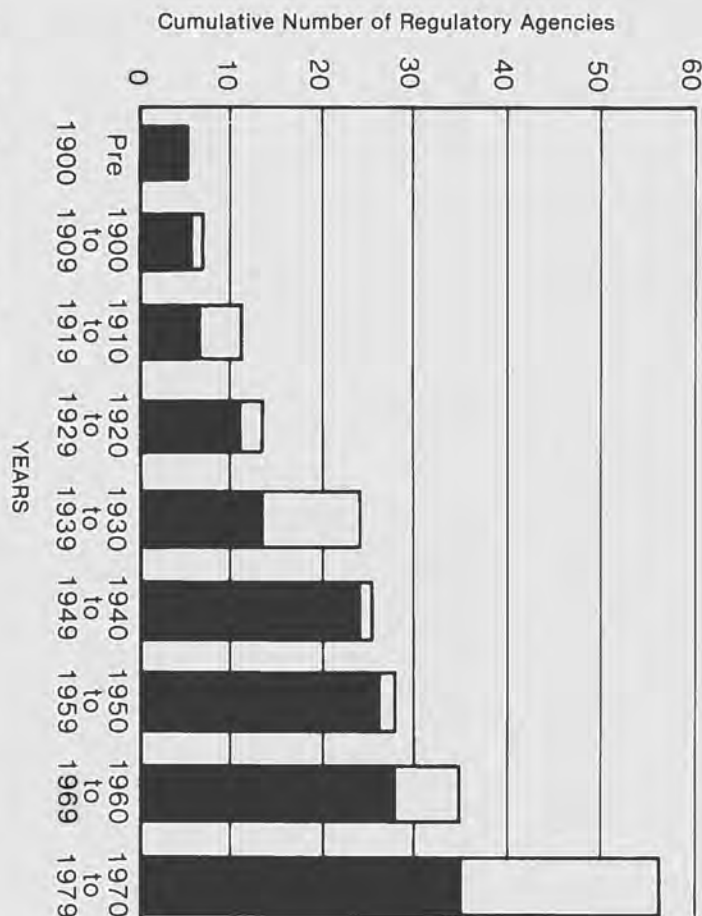
Area of Regulation	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	(Estimated) 1980	1981	% Change 1970 to 1979	% of 1981 Budget
<b>Social Regulation</b>														
Consumer Safety and Health .....	\$ 392	\$ 593	\$ 948	\$1059	\$1251	\$1347	\$1464	\$1772	\$2261	\$2474	\$2606	\$2857	+ 531%	41%
Job Safety and Other Working Conditions .....	62	104	124	227	310	379	447	492	544	642	742	800	+ 935%	12%
Environment and Energy .....	85	146	493	585	759	967	1026	1047	1296	1517	1688	2217	+ 1685%	32%
Total Social Regulation .....	539	843	1565	1871	2320	2693	2937	3311	4101	4633	5036	5874	+ 760%	85%
<b>Economic Regulation</b>														
Finance and Banking .....	106	123	134	142	158	186	211	240	273	296	294	352	+ 179%	5%
Industry-Specific Regulation .....	125	151	166	140	203	220	251	286	297	318	377	384	+ 154%	5%
General Business .....	96	105	120	133	153	169	199	225	245	271	316	327	+ 182%	5%
Total Economic Regulation .....	327	379	420	415	514	575	661	751	815	885	987	1063	+ 171%	15%
<b>Grand Total .....</b>	<b>\$ 866</b>	<b>\$1222</b>	<b>\$1985</b>	<b>\$2286</b>	<b>\$2834</b>	<b>\$3268</b>	<b>\$3598</b>	<b>\$4062</b>	<b>\$4916</b>	<b>\$5518</b>	<b>\$6023</b>	<b>\$6937</b>	<b>+ 537%</b>	<b>100%</b>
Annual Nominal Increase .....		41%	62%	15%	24%	15%	10%	13%	21%	12%	9%	15%		
Annual GNP Deflator .....		5.1%	4.1%	5.8%	9.7%	9.6%	5.3%	5.5%	7.3%	8.9%	8.9%	8.8%		
GNP Deflator Index <sup>1</sup> .....	100	105.1	109.4	115.7	127.0	139.2	146.5	154.6	165.9	180.7	196.7	214.0		
Total in 1970 \$ .....	\$ 866	\$1163	\$1814	\$1976	\$2231	\$2348	\$2456	\$2627	\$2963	\$3054	\$3062	\$3242		
Annual Real % Increase .....		34%	56%	9%	13%	5%	5%	7%	13%	3%	0%	6%		

NOTE: <sup>1</sup>GNP Deflator figures for years 1971-1977 are taken from *Statistical Abstract of the United States, 1978*. Figures for 1978-1981 are taken from the *Budget of the United States Government, Fiscal Year 1981*.

Source: Center for the Study of American Business

bulk of the regulatory budgets (approximately eighty-five percent) is devoted to the newer areas of social regulation, such as job safety, energy and the environment, and consumer safety and health. Note that the traditional regulating commissions may still dominate the professional literature, but they cast a much smaller shadow on the federal budget.

**FIGURE 1**  
**Historical Perspective of Federal Agency Growth**



Source: Center for the Study of American Business  
Note: Agencies do not total 57 since some agencies have split regulatory functions between two or more spin-off agencies. The date that the parent organization was established was used to create the chart.

These governmental outlays indicate the costs of regulation which are borne by the taxpayer. Estimates for the fiscal year 1980 show a total of \$6.0 billion in federal expenditures to operate the 57 agencies which regulate business. That dollar figure represents nearly a six-fold increase from the 1970 level of \$866 million. There has been, and continues to be, a steady growth in the pace of regulatory activities. In fact, budget estimates for the regulatory agencies for fiscal 1981 show an increase of nearly \$1 billion, to a total of \$6.9 billion in administrative costs—a 15 percent increase over 1980 figures.

In short, the cost of operating federal regulatory agencies is rising more rapidly than the federal budget as a whole, the population of the country, or the gross national product. The costs to the taxpayer are obviously not trivial, but the key effects of government regulation must be seen in terms of the compliance by the private sector.

#### **The Indirect Cost of Regulation**

At first blush, government imposition of socially desirable requirements on business through the regulatory process appears to be an inexpensive way of achieving national objectives. This practice apparently costs the government little—about one percent of the federal budget. But the public does not escape paying the cost. Every time, for example, that the EPA imposes a more costly (albeit less polluting) method of production on any firm, the cost of the firm's product to the consumer will tend to rise. Similar effects flow from other regulatory efforts, including those involving product safety, job health, and hiring and promotion policies.

These higher prices represent the "hidden tax" of regulation that is shifted from the government to the consumer. Moreover, to the extent that government-mandated requirements impose similar costs on all price categories of a given product (such as passenger automobiles), this hidden tax tends to be more regressive than the income tax or sales taxes. Of course, it is not inevitable that every regulatory activity will increase inflationary pressures. Where

regulation generates social benefits (such as a healthier and thus more productive work force) in excess of the social costs it imposes, inflationary pressures should be reduced.

At times the impact of regulation on the prices that consumers pay is direct and visible. The federal government has required the producers of automobiles to incorporate in their product a wide array of specified safety and environmental features. The Bureau of Labor Statistics each year estimates the added price of the typical passenger automobile resulting from the safety and ecological features which were incorporated that year in response to federal requirements. In Table 2, these items are summed and put on a consistent price basis. Through 1978, the cumulative cost increase per vehicle of these mandated features came to \$666, or \$7 billion for the vehicles sold that year.

Numerous other costs in the private sector result from the activities of regulatory agencies. In a few cases—notably EPA and OSHA—comprehensive annual surveys of the cost of compliance are available. An annual survey by the McGraw-Hill Department of Economics reports the capital outlays that are made to meet OSHA standards; its current estimates are in the neighborhood of \$3.5 billion a year.

The U.S. Council on Environmental Quality (CEQ) projects each year the incremental capital and operating costs that arise from environmental regulation. As can be seen in Table 3, the annual cost of incremental pollution abatement expenditures was \$26.9 billion in 1978, consisting of \$14.0 billion of current costs and \$12.9 billion for amortization of capital costs. CEQ estimates that these costs will rise to \$64.0 billion in 1987 (measured in constant 1978 dollars) and that, over the decade, approximately \$478 billion will be spent to comply with federal environmental legislation, above and beyond those substantial outlays that would have been made in the absence of such legislation.

Another very substantial direct cost is borne by business firms that must fill out the never-ending flow of questionnaires and other forms issued by the regulatory agencies. The Federal Paperwork



TABLE 2

## Increase in Retail Price of Automobiles Due to Federal Requirements

Year of Regulation	Government Mandated Equipment	Estimated Current Cost
1968	Seat and shoulder belts, standards for exhaust emissions	\$ 47.84
1968-69	Windshield defrosting systems, door latches, etc.	14.53
1969	Head restraints	27.48
1970	Reflective devices and further emission standards	14.77
1968-70	Ignition locking and buzzing systems, etc.	12.75
1971	Fuel evaporative systems	28.33
1972	Improved exhaust emissions and warranty changes; seat belt warning system	42.37
1972-73	Exterior protection	95.29
1973	Reduced flammability materials, etc.	8.72
1969-73	Improved side door strength	20.85
1974	Interlock system and improved exhaust emissions	133.50
1975	Additional safety features and catalytic converter	146.66
1976	Hydraulic brakes, improved bumpers, etc., (less savings from removal of interlock system)	41.54
1977	Leak resistant fuel system, etc.	21.25
1978	Redesign of emissions controls	9.99
	TOTAL	\$665.87

Source: Center for the Study of American Business

TABLE 3  
Estimated Incremental Pollution Abatement and Environmental Quality Expenditures, 1978-87  
(billions of 1978 dollars)

	1978			1987			Cumulative (1978-87)		
	Operation and Maintenance	Annual Capital Costs	Total Annual Costs	Operation and Maintenance	Annual Capital Costs	Total Annual Costs	Capital Investment	Operation and Maintenance	Total Costs
Air Pollution									
Public	0.9	0.3	1.2	2.0	0.8	2.8	4.6	13.7	5.5
Private									
Mobile	4.3	3.3	7.6	5.1	9.3	14.4	59.6	45.0	66.4
Industrial	2.3	2.7	5.0	3.7	5.2	8.9	28.6	44.1	38.6
Utilities	1.6	1.2	2.8	6.5	4.8	11.3	26.4	37.5	28.1
Subtotal	9.1	7.5	16.6	17.3	20.1	37.4	119.2	140.3	138.6
Water Pollution									
Public	1.5	3.0	4.5	2.1	5.0	7.1	17.2	16.6	46.7
Private									
Industrial	2.1	1.6	3.7	5.7	4.6	10.3	28.0	38.9	30.4
Utilities	1.2	0.8	2.0	1.8	1.2	3.0	3.9	16.0	10.1
Subtotal	4.8	5.4	10.2	9.6	10.8	20.4	68.5	71.5	87.2
Solid Waste									
Public	NA	NA	NA	0.5	0.3	0.8	NA	3.5	2.2
Private	NA	NA	NA	1.2	0.6	1.8	NA	8.8	4.7
Subtotal	NA	NA	NA	1.7	0.9	2.6	NA	12.3	6.9
Toxic Substances	0.1	NA	0.1	0.3	NA	0.3	NA	2.2	NA
Drinking Water	<.05	<.05	<.05	0.4	0.4	0.8	NA	2.9	2.7
Noise	<.05	<.05	<.05	0.6	1.0	1.6	4.8	2.5	4.1
Pesticides	<.05	<.05	<.05	0.1	<.05	0.1	NA	0.4	<.05
Land Reclamation	NA	NA	NA	0.8	NA	0.8	NA	6.0	NA
Total	14.0	12.9	26.9	30.8	33.2	64.0	192.5	238.1	239.5
									477.6

Source: U.S. Council on Environmental Quality

NA = Not Available

Commission estimated that this paperwork burden costs businesses from \$25 to \$32 billion each year.<sup>6</sup>

For many of the older regulatory agencies—such as the Interstate Commerce Commission (ICC) and the Civil Aeronautics Board (CAB)—independent scholars have estimated the costs for all or a portion of the regulations. Usually, each estimate has covered a different time period. The Center for the Study of American Business at Washington University culled from the literature what were considered to be the best estimates, usually taking the lower end if a range was offered, and put the results on a consistent price basis. Industry-specific regulations (such as those of the ICC, CAB, etc.) figure prominently, in part because of the wealth of data available on them. For many of the newer regulatory agencies, however, such as the Consumer Product Safety Commission and the Department of Energy, reasonable compliance costs have not been developed, and thus implicitly they were carried at zero, except for the paperwork burden. This procedure yields both a major underestimate and a clear opportunity for further research. The resulting estimate of the compliance costs came to \$63 billion in 1976 (see Table 4).

**TABLE 4**  
**Annual Cost of Federal Regulation**  
**By Area, Calendar 1976**  
**(millions of dollars)**

Area	Administrative Cost	Compliance Cost	Total
Consumer Safety and Health	\$1,516	\$ 5,094	\$ 6,610
Job Safety and Working Conditions	483	4,015	4,498
Energy and the Environment	612	7,760	8,372
Financial Regulation	104	1,118	1,222
Industry Specific	484	19,919	20,403
Paperwork	(a)	25,000	25,000
<b>TOTAL</b>	<b>\$3,199</b>	<b>\$62,906</b>	<b>\$66,105</b>

(a) Included in other categories

Source: Center for the Study of American Business

These estimated compliance costs were approximately twenty times larger than the budgets of the agencies issuing the regulations.<sup>7</sup>

Thus, on the average, each dollar that Congress appropriates for regulation results in an additional \$20 of costs imposed on the private sector of the economy. In a more recent report prepared for the Joint Economic Committee of the U.S. Congress, I attempted to prepare a rough update of these figures by using the multiplier of 20 to 1 that was obtained in the base period and applying it to the budget data for more recent years. The results showed the continued upward movement in the costs resulting from federal regulation of business.<sup>8</sup> Using that approach, the estimated aggregate cost of issuing and complying with federal regulations comes to about \$126 billion in the fiscal year 1980, or over \$500 for each man, woman, and child in the United States (see Table 5).

**TABLE 5**  
**Estimated Cost of Federal Regulation of Business**  
**(Fiscal years, in billions of dollars)**

	1977	1978	1979	(estimated) 1980
Administrative Costs	\$ 4.1	\$ 4.9	\$ 5.5	\$ 6.0
Compliance Costs	\$82.0	\$ 98.0	110.0	120.0
<b>TOTAL</b>	<b>\$86.1</b>	<b>\$102.9</b>	<b>\$115.5</b>	<b>\$126.0</b>

Source: Center for the Study of American Business



## The Induced Effects of Regulation

Some of the most powerful effects that flow from the exercise of the government's rule-making power are even more difficult to quantify. Those induced impacts of regulation include the following:

*The innovative product research and development that is not performed because corporate research and development budgets increasingly are being devoted to what is termed "defensive research."* A number of individual companies report that they devote large and growing shares of their scientific resources to meeting regulatory requirements or to avoiding violations of regulatory restrictions. For example, one hidden cost of government regulation is a reduced rate of introduction of new products. The longer it takes for a new product to be approved by a government agency—or the more costly the approval process—the less likely that the new product will be created. In any event, innovation will be delayed. The impacts are most conspicuous in the pharmaceutical area and are likewise becoming onerous in the chemical products sector, particularly as the toxic substance control regulations are promulgated.

*The new investments in plant and equipment that are not made because the funds must be diverted to meeting government-mandated social requirements.* The resultant loss of productivity has been measured for environmental and job safety by Edward Denison of the Department of Commerce at about one fourth of the potential average annual increase in productivity.<sup>9</sup>

Capital formation and productivity are also adversely affected by the uncertainty about the future of regulations governing the introduction of new processes and products. An example is furnished in the report of a task force of the U.S. Energy Resources Council which dealt with the possibility of developing a new synthetic fuel industry. In considering the National Environmental Policy Act of 1969, the task force stated that the major uncertainty was not whether a project would be allowed to proceed, but rather the length of time it would be delayed pending the issuance of an environmental impact statement that would stand up in court. In assessing the overall impact of government regulatory activity on the establishment

of a new energy industry, the task force concluded, "In summary, some of these requirements could easily hold up or permanently postpone any attempt to build and operate a synthetic fuels plant."<sup>10</sup> The recent cancellation of the SOHIO pipeline project (in 1979) provides evidence that the regulatory uncertainties are not limited in their adverse impacts to new (coal degasification) or even controversial (nuclear) technologies.

*The workers that are not hired because federal regulations have priced them out of labor markets.* One increase in the statutory minimum wage reduced teenage employment in the United States by over 200,000 below what it otherwise would have been.<sup>11</sup> In construction labor, where unemployment rates are substantially above the national average, government regulation also has acted to price some segments of the work force out of competitive labor markets. Under the Davis-Bacon Act, "prevailing" wages are paid on federal and federally supported construction projects. These government-mandated wage rates are often higher than those that actually prevail in the labor market where the work is done.<sup>12</sup>

*The concentration of industry that results as smaller enterprises find that the burdens of government regulation fall on them disproportionately hard.* Most of this impact is unintentional, in that the regulations typically do not distinguish among companies of different sizes. But forcing a small firm to fill out the same specialized forms—or to develop a new type of equipment—as a large company with highly-trained technical staffs places a significantly greater burden on that smaller enterprise. This general point is supported by data and examples for such different governmental regulatory activities as the Environmental Protection Agency, the Employee Retirement Income Security Act (ERISA), the National Labor Relations Board, the Occupational Safety and Health Administration, and the Securities Exchange Commission.<sup>13</sup>

*The immeasurable effects of government regulation on the basic entrepreneurial nature of the private enterprise system.* To the extent that management's attention is diverted from traditional product development, production, and marketing concerns to meeting

governmentally imposed social requirements, a significant bureaucratization of corporate activity results.

In employee pension fund management, for example, pension regulation has shifted much of the concern of fund managers from maximizing the return on the contributions to a more cautious approach of minimizing the likelihood that the managers will be criticized for their investment decisions. It thus has become safer—although not necessarily more desirable for the employees covered—for the pension managers to keep more detailed records of their deliberations, to hire more outside experts (so that the responsibility can be diluted), and to avoid innovative investments.

In short, federal regulatory activity is resulting in a significant bureaucratization of business activity. The ultimate costs of excessive government involvement in the economy are not always visible but surely are powerful—the factories that are not built, the jobs that are not created, the goods and services that are not produced, and the incomes that are not generated. These effects have formidable impact on our standard of living and our quality of life.

### THE IMPLICATIONS FOR ACADEMIC THINKING

It must be recognized that impetus for most of the expansion in government power over business is not being provided by the industries being regulated. Generally, businesses have shown a minimum of enthusiasm for EPA, OSHA, ERISA, the Equal Employment Opportunity Commission (EEOC), etc. If anything, the companies claim that the “benefits” to them of these regulations are negative. The pressures for the new style of regulation come, rather, from a variety of citizen groups concerned primarily with non-economic aspects of our national life—environmentalists, consumer groups, labor unions, and civil rights organizations. Professor Barry Weingast of Washington University has been developing a more comprehensive theory of the relationships among the regulators and the regulated, an approach that tries to take account of the changing balance among public and private interest groups.<sup>14</sup>

To talk or write about the regulated industry “capturing” its regulators is, to put it kindly, a rather quaint way of viewing the fundamental shift in business decision making now taking place: the shift of power from private managers to public officials. Yet, the core of the economists’ version of the “capture” theory still holds—public policy tends to be dominated by the organized and compact pressure groups which attain their benefits at the expense of the more diffused and larger body of consumers.<sup>15</sup> But the nature of those interest groups has changed in recent years. Rather than the railroad baron (a relatively easy target for attack), the villain of the piece has become a self-styled representative of “the public interest,” who has succeeded so frequently in identifying his or her personal prejudices with the national well-being. The business firm, in contrast, performing its traditional middleman function, more typically serves the unappreciated and involuntary role of proxy for the overall consumer interest.

It is not a question of begrudging a “few” more billion dollars for job safety, consumer health, etc. The truth is that the typical regulatory program is not reaching the worthy objectives it was established to attain. For instance, take the job safety program: despite the array of regulations, inspections, and proceedings—and, of course, the billions of dollars devoted each year to meeting the federal safety standards—we see no improvement in the statistics on days lost due to job health and safety hazards.

But that is no isolated example. Surely the railroad passenger—that vanishing breed of consumer—does not benefit from the mass of regulation maintained over rail companies by the Interstate Commerce Commission. Unfortunately, these are typical and not unusual cases. Virtually every study of regulatory experience—ranging from trucking to pharmaceuticals to pensions—indicates both needless expense and ineffective operations or, worse yet, counterproductive results.



## APPROACHES TO REGULATORY REFORM

Economists are prone to take measurements of economic phenomena. The numbers, of course, are not an end in themselves, but an input to decision makers. The measurement of the costs and related impacts that flow from government regulation is no esoteric matter. This information can be used in many ways. First of all, the cost data show the public and the government the economic importance that regulation has assumed, especially as measured by the large dollar amounts of resources that are required in order to meet federal mandates.

Second, this information helps to shift the public dialogue onto new and higher ground. The pertinent policy questions are no longer, "Are you for or against clean air or safe products?" or other such absolutes. Increasingly, the public discussions are formed in terms of less emotional and long-neglected questions such as, "How well is the regulatory process working?" and, "Are there better ways of achieving the public's desires?"

Finally, the availability of information on the costs of regulation is an important step in reforming the regulatory process. The pressure of the cost data inevitably leads to proposals for benefit/cost analyses, cost-effectiveness studies, risk-benefit evaluations, and similar analytical approaches to what in the past had been viewed too often as emotional issues. Hopefully, legislation reforming regulatory practices will mandate such analytical techniques and thus improve the cost—and benefit—data that are used in the regulatory process.

A new way of looking at the microeconomic effects of regulatory programs is needed. A parallel can be drawn to macroeconomic matters, where important and conflicting objectives are recognized and attempts at trade-offs are made (for example, as between economic growth and price stability). At the microeconomic level, it is likewise appropriate to reconcile the goals of specific government programs with national objectives. Environmental protection, product safety, and other regulatory efforts should be related to costs to the consumer, availability of new products, and employment. In part, this reconciliation can be made at the initial

stages of the government process, when the president proposes and the Congress enacts a new regulatory program.

### Benefit-Cost Analysis

One device for broadening the horizons of government policymakers and administrators is the economic impact statement. Policymakers could be required to consider the costs (and other adverse effects) of their actions as well as the benefits. This is not a novel idea. In November 1974, then-President Gerald Ford instructed the federal agencies under his jurisdiction to examine the effects of major regulatory actions on costs, productivity, employment, and other economic factors. President Carter has continued this effort, with some modifications.

This first step is subject to several shortcomings. Many of the key regulatory agencies—ranging from the Consumer Product Safety Commission to the Federal Trade Commission—are so-called "independent agencies," which are beyond the president's jurisdiction in these matters. Even in the case of the regulatory activities that come within presidential oversight, the agencies covered by the Executive Order are required only to examine the economic aspects of their actions; the weight they give to economic factors remains at their discretion—to the extent that Congressional statutes permit them to give any consideration to economic influences at all.

A broader approach is needed, one with a strong legislative mandate. In the fashion of the environmental impact statements (but without as much of the trivia), Congress should require each regulatory agency to assess the impact of its proposed actions on the society as a whole, and particularly on the economy. Much would depend on the "teeth" put into any required economic impact statement. Merely legislating the performance of some economic analysis by an unsympathetic regulator would serve little purpose beyond delaying the regulatory process and making it more costly. But limiting government regulation to those instances where the total benefits to society exceed the costs would be a major departure from current practice.



Government regulation should be carried to the point where the incremental costs equal the incremental benefits, and no further. Indeed, this is the basic criterion that is generally used to screen government investments in physical resources. Overregulation is not an emotional term. It is the economist's shorthand for regulation for which the costs exceed the benefits.

The critics of the analytical approach to evaluate government regulation tend to forget that benefit/cost analysis is a neutral concept. It gives as much weight to a dollar of benefits as to a dollar of costs. And, in a broader sense, the estimation of benefits and costs need not be necessarily viewed in dollar terms. The costs as well as the benefits may at times properly be measured in terms of human life. For example, OSHA regulations may have a very high opportunity cost when they divert professional safety staffs of the companies from their traditional duty of training workers in safer procedures. The "benefits" of following rules printed in the *Federal Register* may be far more illusory and surely fewer.

The implementation of benefit/cost analyses needs a great deal of attention. After all, a reluctant agency can merely go through the motions of studying the effects of its actions on the economy and then proceed as it originally intended. An agency not directly involved in regulation—such as the General Accounting Office or the Office of Management and Budget—should set government-wide standards, concepts, and methods of performing economic evaluations of regulations, including the estimation of benefits and costs. The determination of the interest rates to be used in discounting future costs and benefits, for example, should not be a matter left to the judgment of the agency which is attempting to justify its own action. Where a dollar sign cannot be placed on the benefits, reliance can be placed on cost/effectiveness analysis, which is a search for least-cost solutions.

As a minimum, the Congress should endorse the kind of common sense that was embodied in a federal court decision which stopped OSHA from issuing new benzene regulations. The court's language is instructive: "Although the agency does not have to

conduct an elaborate cost/benefit analysis...it does have to determine whether the benefits expected from the standards bear a reasonable relationship to the costs imposed by the standard."<sup>16</sup> (When OSHA appealed that decision to the Supreme Court, its benzene standards were rejected.)

The ability of the executive branch to change the basic regulatory system is limited. Each regulation is issued in accord with a law passed by Congress. Reform measures cannot simply be "proclaimed," they must be legislated. Many of the proposals to reform government regulation involve the "sunset" mechanism—the compulsory periodic review of each major regulatory program to determine whether it is worthwhile to continue it in the light of changing circumstances. This procedure would provide Congress with a formal opportunity to revise the underlying regulatory statutes or to determine that a given regulatory program is no longer needed and that the "sun" should be allowed to "set" on it. A benefit/cost analysis would provide a quantitative mechanism that would help in making those value judgments.

### **Budgeting as a Management Tool**

Greater attention should be given to the role of the Congressional budget process in managing regulation. In those cases where an agency's regulations generate more costs than benefits, the agency's budget for the coming year should be reduced, and perhaps vice versa. Because the appropriations for the regulatory agencies are small portions of the government's total budget, limited attention has been given to them in the budget process. In view of the large costs that they often impose on the society as a whole, greater attention is warranted in reviewing their appropriation requests via a regulatory budget.

### **Changing Attitudes Toward Regulation**

Fundamentally, regulatory reform is not a concern with technical measurements or administrative procedures. Rather, government decision makers need to take a very different view of the regulatory mechanism than they do now. Rather than relying on regulation to

control in detail every facet of private behavior, the regulatory device needs to be seen as a powerful tool to be used reluctantly and with great care and discretion. Consequently, it is attitudes that need to be changed. Experience with the job safety program provides a cogent example. Although the government's safety rules have resulted in billions of dollars in public and private outlays, the goal of a safer work environment has not been achieved.

A more satisfying answer to improving the effectiveness of government regulation of private activities requires a major change in the approach taken to regulation, and one not limited to the job safety program. Indeed, that program is used here merely as an illustration. If the objective of public policy is to reduce accidents, then public policy should focus directly on the reduction of accidents. Excessively detailed regulations are often merely a substitute—the normal bureaucratic substitute—for hard policy decisions.

Rather than placing emphasis on issuing citations to employers who fail to fill forms out correctly or who do not post the required notices, stress should be placed on the regulation of those employers with high and rising accident rates. Perhaps fines should be levied on those establishments with the worst safety records. As the accident rates decline toward some sensible standard, the fines could be reduced or eliminated. But the government should not be much concerned with the way a specific organization achieves a safer working environment. Some companies may find it more efficient to change work rules, others to buy new equipment, and still others to retrain workers. The making of this choice is precisely the kind of operational business decision making that government should avoid, but that now dominates many regulatory programs.

### **Alternatives to Regulation**

The promulgation by government of rules and regulations restricting or prescribing private activity is not, of course, the only means of accomplishing public objectives. Codes of behavior adhered to on a voluntary basis can be effective. Government itself has available to it various powers other than the regulatory mechanism.

Through its taxing authority, the government can provide strong signals to the market. Rather than promulgating detailed regulations governing allowable discharges into the nation's waterways, the government could levy substantial taxes on those discharges.

The use of taxation would be meant neither to punish polluters nor to give them a "license" to pollute. Rather, it would work through the price system to encourage producers and consumers to shift to less polluting ways of producing and consuming goods and services. Price incentives tend to force the environmental agencies to consider explicitly the cost of cleaning up pollution, while direct controls make it very easy to adopt extremely expensive if not unrealistic goals, such as zero discharge.

In the case of the traditional, one-industry type of government regulation (as of airlines, trucking, and railroads), a greater role should be given to the competitive process and to market forces. Unlike the newer forms of regulation, the older forms of regulation are often mainly barriers to entry into a given industry, protecting existing firms from competition by potential new entrants. To date, none of the procedural reforms previously described has been enacted by the Congress. Perhaps the most significant single legislative action in the regulatory reform area in recent years was the law phasing out the Civil Aeronautics Board over a seven year period.

With reference to consumer protection, an information strategy can provide a sensible alternative to compulsory product standards. For the many visible hazards that consumers voluntarily subject themselves to, the most important consideration in public policy is to improve the individual's knowledge of the risks involved rather than limit personal discretion. In their daily lives, citizens rarely opt for zero-risk alternatives and more often trade off between speed and safety, for example.

The more widespread provision of information to consumers on potential hazards in various products may, in many circumstances, be far more effective than banning specific products or setting standards requiring expensive alterations in existing products. The information approach takes account of the great variety of consumer desires and capabilities. Interestingly enough, this approach often is favored in

consumer surveys, although *not* by some of the most vehement representatives of the so-called public interest groups.

Any realistic appraisal of government regulation must acknowledge that important and positive benefits have resulted from many of the regulatory activities—less pollution, fewer product hazards, reducing job discrimination, and other socially desirable goals of our society. But the “externalities” generated by federal regulation do not justify government attempting to regulate every facet of private behavior. A reasonable approach to this problem requires great discrimination in sorting out the hazards that are important to regulate from the kinds of lesser hazards that can best be dealt with through the normal prudence of consumers, workers, and business firms.<sup>17</sup>

## THE SAVINGS FROM REGULATORY REFORM

It is difficult to estimate the specific savings that would occur from the adoption of any of the approaches to regulatory reform suggested here. What is clear, however, is that each of these changes could reduce the economic burden of government rule-making while often increasing the likelihood of reaching the nation’s basic goals and objectives. This is most apparent in the case of economic regulation, where the reliance on competition would be a far less costly way of meeting the public’s transportation demands than the status quo of detailed regulation.

On the basis of the data in Table 4, savings in the area of economic regulation—by deregulating the airline, railroad, trucking, radio and television industries—could well reach \$20 billion a year. In the field of social regulation, a reasonable initial objective would be to slow down, if not halt, the now rapid rise in the issuance—and thus the cost of complying with—new rules and directives. As pointed out earlier, one major new OSHA standard alone may likely generate a larger economic burden of compliance than the entire array of existing rules issued by that agency, which imposes costs of over \$3 billion a year at present. Moreover, the potential cost of new environmental regulations already in the “pipeline” is far greater.

Thus, the measurable dollar savings from regulatory reform surely could be substantial. But, in the long run, the most important benefits from changing the status quo would be the improved productivity, the higher rates of capital formation and innovation, and ultimately the improved living standards that would result for American consumers. That surely makes regulatory reform a worthy and high-priority undertaking.



## NOTES

<sup>1</sup>U.S. Council on Environmental Quality, *Environmental Quality, Ninth Annual Report*, Washington, D.C., Government Printing Office, 1979.

<sup>2</sup>American Industrial Health Council, *Preliminary Estimates of Direct Compliance Costs and Other Economic Effects of OSHA's Generic Carcinogenic Proposal on Substance Producing and Using Industries*, Scarsdale, N.Y., 1978.

<sup>3</sup>Kenneth W. Clarkson, et al., "Regulating Chrysler Out of Business?" *Regulation*, September/October, 1979.

<sup>4</sup>See *Directory of Federal Regulatory Agencies*, second edition, compiled by Ronald J. Penoyer, St. Louis, Washington University, Center for the Study of American Business, 1980.

<sup>5</sup>See Marvin H. Kusters, "Counting the Costs," *Regulation*, July/August, 1979.

<sup>6</sup>U.S. Commission on Federal Paperwork, *Final Summary Report*, Washington, D.C., Government Printing Office, 1977.

<sup>7</sup>M. L. Weidenbaum and Robert De Fina, *The Cost of Federal Regulation of Economic Activity*, Washington, D.C., American Enterprise Institute, 1978.

<sup>8</sup>M. L. Weidenbaum, *The Cost of Government Regulation of Business*, Joint Economic Committee Print, Washington, D.C., Government Printing Office, 1978.

<sup>9</sup>Edward F. Denison, "Effects of Selected Changes in the Institutionalized and Human Environment Upon Output Per Unit of Input," *Survey of Current Business*, January 1978.

<sup>10</sup>Synfuels Interagency Task Force, *Recommendations for a Synthetic Fuels Commercialization Program*, Report submitted to the President's Energy Resources Council, Washington, D.C., Government Printing Office, 1975.

<sup>11</sup>James F. Ragan, Jr., *Minimum Wages and the Youth Labor Market*, St. Louis, Washington University, Center for the Study of American Business, 1977.

<sup>12</sup>Armand J. Thieblot, Jr., *The Davis-Bacon Act*, Philadelphia, University of Pennsylvania, 1975.

<sup>13</sup>Kenneth W. Chilton and M. L. Weidenbaum, *Small Business Performance in the Regulated Economy*, St. Louis, Washington University, Center for the Study of American Business, 1980.

<sup>14</sup>Barry Weingast, *Regulation, Reregulation, and Deregulation: The Political Foundations of a Science of Politics*, St. Louis, Washington University, Center for the Study of American Business, 1980.

<sup>15</sup>George J. Stigler, *The Citizen and The State*, Chicago, University of Chicago Press, 1975.

<sup>16</sup>American Petroleum Institute v. OSHA, No. 78-1253 (5th Circuit, October 5, 1978).

<sup>17</sup>See Charles L. Schultze, *The Public Use of Private Interest*, Washington, D.C., Brookings Institution, 1977.