The Job Creation and Wage Enhancement Act of 1995

Testimony Prepared for Presentation to
Committee on Science
U.S. House of Representatives
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By Paul R. Portney, Senior Fellow and President
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Mr. Chairman, former Mr. Chairman, and distinguished members. Thank you very much for inviting me to be here today. I'm very pleased to have the opportunity to present to you my views on Titles III and VII of H.R. 9, the Job Creation and Wage Enhancement Act of 1995.

My name is Paul R. Portney and I am currently vice-president of Resources for the Future, an independent, nonpartisan research and educational organization concerning itself with natural resources and the environment. It is important for me to note at the outset that the views I will present today are mine and mine alone. Resources for the Future takes no institutional position on legislative, regulatory, or other public policy matters. Unlike other "think tanks," we have never been characterized as being Republican or Democratic, liberal or conservative. That is a distinction of which I am proud.

I am an economist by training and, since 1976, my research and policy analytic work has been concerned almost exclusively with regulatory issues, particularly those pertaining to federal environmental regulation. During this time, I spent nearly two years (1979–1981) as chief economist at the Council on Environmental Quality in the Executive Office of the President. One of my responsibilities then was to participate in President Carter's Regulatory Analysis Review Group, an interagency team that regularly scrutinized proposed regulations emanating from both executive branch and independent regulatory agencies and made recommendations about how those proposed regulations might be improved. In large part because of that experience, I have paid particular attention over the last fourteen years to the series of efforts by four Presidents—two Democrats and two Republicans—to put in place and carry out a process of executive branch review of federal regulation. I will draw on the research, teaching, and thinking I have done about regulatory reform over this period of time in the comments I will make today.

Because I will focus most of my remarks on those aspects of Titles III and VII of H.R. 9 that trouble me, I want to take some pains to preface those remarks. First, let me say that I am as troubled by certain aspects of federal regulation—particularly environmental regulation—as I sense many members of this Committee are. Especially troubling to me are those provisions of regulatory statutes that prohibit regulators from even considering costs when making significant policy decisions. To choose but one example, albeit the most economically significant one in all federal regulatory law, Section 109 of the Clean Air Act prohibits the Administrator of the Environmental Protection Agency from even considering costs when setting the National Ambient Air Quality Standards. Similar provisions exist in the Safe Drinking Water Act, Superfund, the Occupational Safety and
Health Act, and other laws. While economic impacts should never be allowed to predominate in standard-setting for health, safety and the environment, we simply cannot make rational federal environmental policy unless costs can be weighed in establishing the goals for policy in these areas.

I might add here that while regulatory reform statutes like H.R. 9 have a very useful role to play, they should generally not be viewed as a substitute for a statute-by-statute reexamination. This need not be done all at once; in fact, it would be better to conduct such a reexamination one statute at a time as they come up for reauthorization. Superfund and the Safe Drinking Water Act provide the first opportunities. This will give the members of Congress the opportunity to reflect carefully on the original rationale behind each of the statutes and the respects in which the passage of time and the accumulation of knowledge may have combined to suggest possibly different approaches.

Equally troubling in federal regulation are the technology-based requirements that often pop up, a recent example being the provisions of the 1990 amendments to the Clean Air Act dealing with hazardous air pollutants. Whether explicit or implicit, such requirements tend to freeze technology, ensure that pollution control costs are higher than they need to be, and consequently, handicap U.S. firms that must compete in international markets with firms in other countries that operate under less stringent or at least more enlightened regulatory regimes. Study after study has shown that giving regulated parties the flexibility to meet environmental, safety or health goals however best they see fit can reduce the cost of meeting those goals by 10–50 percent. Since we currently spend in the vicinity of $140 billion each year to comply with federal environmental regulations alone, these savings would be quite significant.

Titles III and VII of H.R. 9 deal prominently with the role of benefit-cost analysis in federal regulation, the subject to which I will confine my remarks today. Let me make clear my general beliefs about that role. Contrary to the views of many, I believe that benefit-cost analysis is a powerful analytical tool that can play a very useful role in public policymaking. It is my view that it has been consistently under- rather than overutilized by federal regulatory agencies, often—though not always—because Congress has constrained regulators in the latitude they have to consider such information.

Benefit-cost analysis can help illuminate cases in which regulatory proposals have not been carefully thought through. It can also, and has done so in the past, provide strong support for additional regulation—as in the case of the removal of lead from gasoline, and as in the case of the original 1970 amendments to the Clean Air Act. In addition, benefit-cost analyses done some years ago by my colleagues demonstrated convincingly that it made much more sense to leave both a free-flowing river and also a pristine wilderness area in their natural states rather than replace them with, respectively, a hydroelectric dam and a ski resort. Benefit-cost analysis, therefore, is inherently neither antienvironmental or antiregulatory. As I will argue below, however, it is not a panacea, and for that reason we must be careful what burdens we impose upon it.
My final prefatory remark pertains to the Committee's recent work. Because I have recently written somewhat critically about certain provisions in an earlier version of the Job Creation and Wage Enhancement Act (Washington Post, January 15, 1995), I want to compliment the members of the Committee on the changes you have made in the revised version. To be sure, I still have serious reservations about a number of features in the bill. But if you continue to modify it as it makes its way through the House, and if subsequent changes are as constructive as those made recently, you will have initiated a debate that is long, long overdue and pointed the way toward constructive reform.

Having established, I hope, my bona fides as a proponent of benefit-cost analysis, I want now to express concern about certain provisions of H.R. 9. For instance, Section 3201(a)(5)(C) requires "A certification [emphasis added] that the rule will produce benefits to human health or the environment that will justify the costs incurred by local and State governments, the Federal Government, and other public and private entities as a result of implementation of and compliance with the rule..." It is not at all clear to me what such a certification entails. It is often the case in environmental benefit-cost analysis that using one set of health studies to estimate the risk reductions that will result from pollution reduction produces significant economic benefits. Using another set of studies—often as carefully done—suggests that the benefits of pollution control are much smaller, sometimes even nonexistent. Similarly, on the cost side, estimates which make no allowance for technological improvement over time in reducing pollution will come out much higher than those which forecast such improvement. (I should point out, incidentally, that I believe our current estimates of environmental compliance costs are too high because they ignore considerable "learning-by-doing" in pollution control that brings costs down with time.)

In a situation like this, where one plausible set of benefit and cost estimates suggests a favorable balance while another, equally plausible set suggests the opposite result, how would a regulator proceed? If this certification is interpreted as a requirement that the regulator say, "In my judgment, the benefits to society from going ahead with this rule will outweigh the costs," then I am comfortable with it. This is because, in my view, we will always have to rely ultimately on the judgment of the officials appointed to carry out regulatory responsibilities. If we do not agree with the judgments they make, the President should fire them. If the President stands by regulators who make unpopular decisions, that is why we have elections.

Let me anticipate one possible response to the issue I have just raised. Surely, you might argue, the risk assessment provisions embodied in H.R. 9 will eliminate the uncertainties inherent in estimating lives saved or illnesses prevented by pollution control, and thereby illuminate the "true" benefit of a regulatory proposal. I do not believe this will be the case. While the provisions in H.R. 9 dealing with risk assessment can help bring some clarity and consistency to a muddled subject, they simply will never eliminate all uncertainties. Thus, it will almost always be the case that a benefit-cost analysis will look favorable under one set of assumptions and unfavorable under another. While I believe firmly that in many such situations we can make judgments about the most likely outcomes, there will always be gray areas where even rigorous analysis points to no clear approach.
I do not mean to suggest that benefit-cost analysis can tell us nothing definitive. We have learned a great deal over the last twenty years, for example, about the values the public places on such things as reduced risk of death from accidents and illnesses, improved visibility in both national parks and in more ordinary settings, enhanced recreational opportunities, reductions in the incidence and severity of both acute and chronic illness, and even the existence of pristine areas that people may never visit but value nonetheless. Similarly, although I believe that estimating the costs of proposed regulations is much more complicated than many people believe, here too great strides have been made. For instance, we now realize that the true economic costs associated with regulation must be measured only after the initial expenditures incurred have reverberated throughout the economy and have manifested themselves as higher product prices, reduced earnings, job losses (and sometimes job gains), and so on. Similarly, we are doing better at taking account of cost-reducing technological change, although we need much more work on this subject.

Nevertheless, despite this real progress, we are still some ways away from the point at which we can confidently make precise estimates of benefits and costs, particularly for programs that result in aesthetic improvements or ecosystem protection. The required certification in Section 3201(a)(5)(C) will be no more than a means to prevent any regulation—good or bad—if it is interpreted as requiring conclusive "proof" that benefits exceed costs. It is very important that the Committee clarify this language and realize that, ultimately, there is no substitute for good judgment on the part of regulatory officials.

On less pressing matters, Section 3201(c)(1) suggests that both "direct and indirect" costs be taken into account for the purposes of the benefit-cost requirements. Presumably, indirect costs are those incurred by parties who are not regulated directly, but who ultimately bear economic burdens as a result of regulation elsewhere. (For instance, regulations falling initially on electric utilities will have significant impacts on aluminum producers because the latter use a great deal of electricity.) In addition, I presume that indirect costs might also include the imputed value of people's time spent waiting to have a car inspected, or waiting to get a permit.

It is perfectly reasonable to include such indirect costs in a benefit-cost study. Indeed, failing to include such costs could give regulators an incentive to shift costs from those directly imposed to those imposed more circuitously. But if indirect costs are to be taken into account, so too must indirect benefits. For instance, air pollution controls that protect a forested area not only benefit the owner of the forest, but also those who might pass by it regularly and enjoy its scenic beauty. Failure to include such benefits as this would bias downward the benefit-cost ratio in a regulatory analysis, in the same way that ratio would be biased upward if all costs were not counted. I would like to see the language in the bill reflect this symmetry.

Let me turn now to Title VII of the bill, which spells out the requirements that the economic analyses must meet. I have several observations to make. First, Section 7004(b) offers a different definition of "major rule" than that offered in Section 3201(c)(2). I strongly urge the Committee to use the latter rather than the former definition. My educated guess is that using the much lower threshold for a major rule (defined in Section 7004(b) as a rule that
affects 100 persons or more, or that requires the expenditure of $1,000,000 by any person) will expand by about tenfold the number of regulations for which benefit-cost analyses must be done. Since many of these regulations could truly be considered minor, there is little to be gained by bogging regulatory agencies down with analytical requirements. Much better to concentrate their attention on the regulations that have really significant economic impacts.

The one caveat to my recommendation here involves possible "unbundling" of regulations by agencies. If it turns out that, in an effort to evade the requirements to do careful analysis in support of rules, agencies break major rules down into separate pieces and issue them individually, it may be necessary to lower the threshold for analysis. Until and unless that is seen to be the case, however, the definition in Section 7004(b)(2) is not only inconsistent with the earlier definition, but also unwise.

In my view, by far the most controversial provision in the Job Creation and Wage Enhancement Act of 1995 is Section 7005. Interestingly, I have heard relatively little discussion of this provision to this point. In its entirety, the provision states, "An agency may not adopt a major rule unless the final Regulatory Impact Analysis is approved in writing by the Director of the Office of Management and Budget or by an individual designated by the Director for that purpose."

Whether intentionally or not, this provision would give the Director of OMB de facto control over the entire federal regulatory apparatus. It would, in other words, make him or her the Director of Federal Regulation as well as the Director of the Office of Management and Budget. And because of the uncertainties and—yes—value judgments that will always characterize both benefit-cost analysis and quantitative risk assessment, it will always be possible to find fault with a Regulatory Impact Analysis. Evidence that convinces a regulatory agency head that benefits are likely to exceed costs may not be convincing to the Director of OMB. Evidence that convinces the regulator that the proposed approach is the least expensive may not be convincing to the Director of OMB. Such statements could be made for many of the requirements that Regulatory Impact Analyses would have to meet under Section 7004(c).

Thus, while I am an avid supporter of the increased use of benefit-cost analysis and other analytical techniques in regulatory decisionmaking, while I am quite critical of a number of rules issued by federal regulatory agencies, and while I believe that a President must have an effective regulatory oversight operation within the executive branch, I am concerned by the power this provision would give to the Director of OMB. Far better, it seems to me, to give our regulators the statutory mandate to balance carefully the pros and cons associated with proposed rules, as well as the resources necessary to conduct the requisite analyses, and then hold them strictly accountable for the decisions they make.

This concludes my prepared remarks. Thank you again for giving me the opportunity to appear before you. I will be happy to answer any questions you may have.