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THE IMPACT OF REGULATION ON U.S. MANUFACTURING

HEARING

BEFORE THE

SUBCOMMITTEE ON REGULATORY AFFAIRS

OF THE

COMMITTEE ON
GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

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CONTENTS

	Page
Hearing held on April 12, 2005	1
Statement of:	
Duesterberg, Thomas, president and CEO, Manufacturers Alliance/MAPI; Lori Luchak, vice president and marketing director, Miles Fiberglass & Composites, on behalf of the American Composites Manufacturers Association; and Sidney Shapiro, University distinguished Chair in law, Wake Forest University, on behalf of Center for Progressive Regulation	55
Duesterberg, Thomas	55
Luchak, Lori	73
Shapiro, Sidney	84
Frink, Al, Assistant Secretary for Manufacturing and Services, U.S. Department of Commerce; John D. Graham, Ph.D., Administrator, Office of Information and Regulatory Affairs, Office of Management and Budget; and Governor John Engler, president, National Association of Manufacturers	11
Engler, Governor John	27
Frink, Al	11
Graham, John, Ph.D.	22
Letters, statements, etc., submitted for the record by:	
Duesterberg, Thomas, president and CEO, Manufacturers Alliance/MAPI, prepared statement of	58
Engler, Governor John, president, National Association of Manufacturers, prepared statement of	29
Frink, Al, Assistant Secretary for Manufacturing and Services, U.S. Department of Commerce, prepared statement of	13
Graham, John D., Ph.D., Administrator, Office of Information and Regulatory Affairs, Office of Management and Budget, prepared statement of	24
Luchak, Lori, vice president and marketing director, Miles Fiberglass & Composites, on behalf of the American Composites Manufacturers Association, prepared statement of	76
Miller, Hon. Candice S., a Representative in Congress from the State of Michigan, prepared statement of	4
Shapiro, Sidney, University distinguished Chair in law, Wake Forest University, on behalf of Center for Progressive Regulation, prepared statement of	86

THE IMPACT OF REGULATION ON U.S. MANUFACTURING

TUESDAY, APRIL 12, 2005

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON REGULATORY AFFAIRS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:05 a.m., in room 2154, Rayburn House Office Building, Hon. Candice S. Miller (chairwoman of the subcommittee) presiding.

Present: Representatives Miller, Brown-Waite, Cannon, Westmoreland, and Lynch.

Staff present: Ed Schrock, staff director; Rosario Palmieri, deputy staff director; Erik Glavich and Dena Kozanas, professional staff members; Lauren Jacobs, clerk; Krista Boyd, minority counsel; and Cecelia Morton, minority office manager.

Mrs. MILLER. Good morning.

Welcome to our hearing this morning. Our great Nation has just in a few short centuries developed into a society and a culture that is envied by people around the entire globe. They see an America that beat all the odds. They see the American people who have been able to excel because we truly have been the land of opportunity, a place where individuals can reach their highest potential in many cases just by using their creativity and because of a desire to simply work hard. And that ingenuity and work has manifested itself in our ability to build things, things that other people want to buy, commonly called manufacturing. And for many years, it has been widely acknowledged that the manufacturing industry has been a critical component of the backbone of America. And for the most part, government has understood that it does not create jobs. The private sector creates jobs, but the government can help to provide an environment that attracts business investment and encourages job creation.

But unfortunately today, the American manufacturing industry is under attack, and there are a number of dynamics involved in this. And we hear stories each and every day about good-paying manufacturing jobs that leave America for other countries. And we see our trading partners in other countries taking advantage of American generosity in some of our trade agreements. We see nations that live under the blanket of freedom and democracy paid for by American dollars and in some cases by American blood. Today, some of those nations subsidize their own manufacturing industries to the disadvantage of ours. Some of these nations are clearly manipulating their currency, again to the disadvantage of

America. And many of these countries compete against our products by producing similar products in sweat shops or by a wage rate that is so low that we cannot compete with that here in our country. And for these reasons and many more, manufacturing has had a really tough go of it lately, and the statistics clearly show that.

Our manufacturing industry is responsible for 14 million jobs, 14 percent of the GDP, over 60 percent of all exports and over 60 percent of all research and development spending. And yet, in just the past few years, the manufacturing sector has lost several million jobs, both union jobs and non-union jobs, jobs that have provided a high quality of life for so many Americans; that have contributed to raising the standard of living for millions of Americans. And unfortunately, we find that oftentimes it's our very own government, perhaps with the very best of intentions, who has become an unwitting partner in assisting other countries to import not just American products but American jobs. And why? Because of the onerous burden of excessive regulations.

Let's consider a few sobering statistics: The Small Business Administration has estimated that the cost of compliance of government-imposed regulations costs small businesses as much as $7,000 per employee. The National Association of Manufacturers has estimated that the structural costs of American products compared with any of our foreign competitors is 22 to 23 percent higher because of government-imposed regulatory burdens.

And guess what? These regulations and rules were not imposed by countries likes China or Japan. We have done it to ourselves, and the time is long overdue for us to do a cost-benefit analysis of many of these regulations.

Some will say that any attempts to reform these many regulations, even just a handful of the tens of thousands of them that exist today, will begin a decline of our standard of living; that we in America need to set the global standard; that even if we continue to bleed manufacturing jobs, that even if we lose our ability to compete in the global marketplace, it is all for the betterment of mankind and incumbent on America to continue to shoulder the burden.

I am a defender of regulations that protect worker health and safety. I've spent almost three decades in public office as a principal advocate of our environment, and I think of myself as an environmentalist. I think of myself as green. But I must also say that I would like to have a little green in our wallets. And I think that the common standard must always be what is reasonable, what is rational. And that is why we are having this hearing today.

We have an outstanding lineup of panelists today, and I feel certain they will give us excellent ideas for improving the Federal Government's approach to regulations that are in place for the benefit of all Americans. And I know that working together, we can do the right thing for workers and for the environment while leveling the playing field and improving the competitiveness of American manufacturers. I look forward to hearing from all of our witnesses

today.

And at this time, I would like to recognize the ranking member, Mr. Lynch, for his opening comments.

[The prepared statement of Hon. Candice S. Miller follows:]

Statement of Candice Miller
Chairman
Subcommittee on Regulatory Affairs
Committee on Government Reform
United States House of Representatives
Washington, DC
April 12, 2005

Good morning and welcome to our hearing this morning.

Our great nation has developed in just a few short centuries, into a society and a culture, that is envied by people around the globe.

They see an America that beat all the odds, they see the American people who have been able to excel because we truly have been the land of opportunity. A place where individuals can reach their highest potential in many cases by using their creativity and because of a desire to simply work hard.

And that ingenuity and work has manifested itself in our ability to build things. Things that other people want to buy. Commonly called manufacturing.

And for many years it has been widely acknowledged that the manufacturing industry has been a critical component of the backbone of America.

And for the most part, Government has understood that it does not create jobs, the private sector creates jobs, but that government can help to provide an environment that attracts business investment and encourages job creation.

But unfortunately today the American manufacturing industry is under attack.

There are a number of dynamics involved in this, and we hear the stories every day about good paying manufacturing jobs, that leave America, for other countries.

And we see our trading partners in other countries taking advantage of American generosity in some of our trade agreements, we see nations that live under the blanket of freedom and democracy, paid for by American dollars and in some cases, by American blood, today some of these nations subsidize their own manufacturing industries, to the disadvantage of ours.

Some of these nations are clearly manipulating their currency, again to the disadvantage of America. Many of these countries compete against our products by producing similar products in sweatshops or by a wage rate so low that we cannot compete with here in our country.

For these reasons and more, manufacturing has had a really tough go lately and the statistics show it.

Our manufacturing industry is responsible for 14 million jobs, 14% of GDP, over 60% of all exports and over 60% of all research and development spending.

Yet in just the past few years, the manufacturing sector has lost several million jobs. Both Union and non-union jobs. Jobs that have provided a high quality of life for so many Americans. That have contributed to raising the standard of living for millions of Americans.

And unfortunately, we find that oftentimes it is our own government, perhaps with the very best of intentions, who has become an unwitting partner in assisting other countries to import not just American products, but American jobs.

Why? Because of the onerous burden of excessive regulations. Consider some sobering statistics.

The Small Business Administration has estimated that the cost of compliance of governmental imposed regulations, cost small business as much as $7,000 per employee.

The National Association of Manufacturers has estimated that the structural cost of American products compared with any of our foreign competitors is 22 to 23% higher, because of governmental imposed regulatory burdens.

And guess what, these regulations and rules were not imposed by countries like China or Japan. We have done it to ourselves – and the time is long overdue for us to do a cost-benefit analysis of many of these regulations.

Some will say that any attempt to reform these many regulations, even just a handful of the tens of thousands of them that exist today, will begin a decline of our standard of living – that we need to set the global standard.

That even if we continue to bleed manufacturing jobs, that even if we lose our ability to compete in a global marketplace, that it is all for the betterment of mankind, and that it is incumbent on America to shoulder the burden.

Let me just say that I am a defender of regulations that protect worker health and safety. I have spent almost 3 decades in public office as a principal advocate of our environment. I think of myself as an environmentalist, I think of myself as Green. But I must also say that I also think that we need to have a little green in our wallets.

I think the common standard must always be – what is reasonable.

That is why we are having this hearing today. We have an outstanding line up of panelists today and I feel certain that they will give us some excellent ideas for improving

the federal governments approach to regulations that are in place for the benefit of all Americans.

I know that working together, we can do the right thing for workers and the environment, while leveling the playing field and improving the competitiveness of American manufacturers.

Mr. LYNCH. Thank you, Madam Chairwoman. It's an honor for me. This being the first subcommittee hearing, I want to say how honored I am to serve with you. I want to thank you for holding this hearing. And I want to pledge my willingness to work with my Republican colleagues and all the members of this committee.

Just as a matter of my own full disclosure about my own background, especially as it relates to the manufacturing industry, in my prior life before coming to Congress, I actually worked for about 20 years as an iron worker and mostly in steel erection, which has the dubious distinction of being perhaps one of the most dangerous occupations, at least peacetime occupations, in this country and results in more deaths and on-the-job disabilities than almost any other peacetime occupation. In my capacity as an iron worker, I had a chance to work at a number of manufacturing facilities, including the General Motors plant in Framingham, MA, as an iron worker and as a foreman. That was before GM shifted a lot of work into Mexico. I also worked at the General Dynamics shipyard in Quincy, MA, as a welder. I worked as an iron worker at the Boise Cascade Paper Mill in Rumford, ME. I worked as an iron worker at the Shell Oil Refinery in Louisiana and also worked at U.S. Steel in Gary, IN, and worked as an iron worker as well at the Inland Steel Plant in East Chicago, IN.

I must say that, as a iron worker and as a shop steward, I had far too many occasions to attend the wakes and funerals of my fellow workers. And there is no more grim responsibility than reporting to a family that their dad, their father who went out to work that morning was not coming home because he was killed on the job. So I probably have a different perspective about some regulations that affect workers in this country. And there are industries that actually need them and I think work to the betterment of not only workers but also their employers.

I do have a deep appreciation for having had the opportunity to raise a family and earn a decent living working at manufacturing facilities. And I understand we are under a lot of threat, a lot of pressure from foreign competition. And I look forward to strengthening the industry and helping it grow. And I look forward to eliminating unnecessary burdens through regulations that are placed on our manufacturers as well, but we need to do it carefully and thoughtfully. Manufacturing has a major impact on the U.S. economy, providing jobs to over 14 million workers. The focus of today's hearing is on the effect of regulations on the manufacturing industry.

However, this hearing is also an important focus, I think, on the role that regulations play in protecting public health, safety and the environment. And there are countless examples of what can go wrong in the absence of strong regulatory protections. The California energy crisis is one example. Lax regulation allowed rampant market manipulation by Enron and other energy companies that cost California over $9 billion. Enron traders were caught on tape laughing about lying and cheating from grandmothers.

Another example is drug safety. After evidence emerged in the drug Vioxx, that the drug Vioxx was associated with heart attacks and strokes in the year 2000, the FDA could not require that the company immediately conduct a safety study nor could the agency

demand specific changes to information for doctors and patients. And as a result, months and years went by before key label changes were made and more detailed information on safety became available and, finally, the drug was withdrawn from the market in September 2004, 4 years later.

The abusive trading practices of mutual fund companies is another example of what can happen without strong regulatory protections. For years, mutual fund companies were engaged in such practices, such as late trading, where certain investors made transactions after the markets had closed for the day at that day's prices and this allowed traders to make transactions and reactions to new announcements that were released after the market closed and that might affect the next day's closing price. These late traders made profits at the expense of long-term investors. Stronger consumer protections would have prevented this abuse of millions of Americans who rely on long-term mutual investments for their retirement.

A particularly egregious example came in the Massachusetts Department of Health where we conducted an investigation that revealed, from 1969 to 1978 in my own State, an unusual number of children in Woburn, MA, were diagnosed with cancer, and the cause was two companies who were dumping chemicals in ways that were in violation of certain regulations and circumvented others. And they allowed those compounds to reach Woburn's drinking water.

These are just a few examples of why we need regulatory protections. OMB should be evaluating where existing regulations are not providing enough protection for consumers, and instead, unfortunately today, most of these proposals are on OMB's regulatory hit list, and they recommend weakening or gutting existing protections.

For example, OMB includes proposals to reduce the amount of information that the public has and companies have to report under the Toxic Release Inventory. And we will hear today about how such regulations like Toxic Release Inventory cost the industry. But rather, I think we might be focusing on the cost of regulations as well to the public who are damaged by the lack of proper controls. I think it's important to look at the benefits as well. The Toxic Relief Inventory provides an enormous benefit to the public by making information available to them about toxic chemical releases.

I want to thank the Chair for her kindness in inviting me here today, and I want thank the witnesses for appearing here today and offering your help to this committee. Thank you.

Mrs. MILLER. Other opening statements?

I turn now to our vice chair, Representative Brown-Waite.

Ms. BROWN-WAITE. Thank you very much Madam Chairwoman.

She needs to be commended for having this hearing today to assess the impact of regulation on U.S. manufacturing. Certainly the burden of excessive and unnecessary regulation is a hidden tax. That is really what it is. It is a weight that drags down our Nation's economic potential. I'm eager to hear the opinions of today's expert panelists so we can properly assess the burden of regulation on the economy and formulate ways that Congress can help.

Ronald Regan understood the importance of regulatory reform. In his first inauguration speech on January 20, 1981, he expressly stated that government is not a solution to our problem. Government is the problem. Too often in our Nation's past, we have looked to the government to legislate or regulate around a problem. However, this is not always the most efficient solution. There are always unintended side effects that arise whenever government meddles in the workplace.

Sometimes government intervention is merited generally when the benefits to society outweigh the cost of the implementation. However, there are many regulations in effect today that never underwent a cost-benefit analysis before going into effect. As legislators and policymakers, we should never lose sight of the consequences of our actions. Last year, the 2005 House Budget Resolution, there actually was a recognition of the significance of regulatory reform, and let me just quote from that language: It is the sense of this House that Congress should establish a mechanism for reviewing Federal agencies and their regulations with the expressed purpose of making recommendations to Congress when agencies prove to be ineffective, duplicative, outdated, irrelevant or failed to accomplish their intended purpose.

There is a bill in Congress for regulatory reform because the need is just so obvious. We know that excessive paperwork and burdensome regulations thwart the U.S. economy and our global competitiveness. It has been estimated that Americans pay more than $700 billion a year to comply with regulatory burdens. That equals to about $8,000 per household according to a recent survey. Unnecessary and ineffective regulations crowd out capital investment by American businesses large and small.

On the issue of regulatory reform, the States have actually led the way. When I served as a Senator in Florida, I had the privilege of serving on the Joint Legislative Committee on Administrative Procedures [JCAP]. In Florida, it is a bipartisan committee made up of House and Senate members charged with the responsibility and also the authority of reviewing agency rules. I think that some people at JCAP could serve as a great model for Federal reforms. After all, article 1, section 1, of the Constitution delegated all legislative authority to Congress and not to administrative agencies. Therefore, I believe that Congress, the elected representatives of the people, should lessen the regulatory burden by taking back some of its authority that it actually has ceded over the years to agencies. And I think we need to do that by exercising proper oversight.

With these guiding principals, I look forward to today's discussion and look forward to hearing from some people who have great recommendations. Thank you, Madam Chairwoman. I yield back the balance of my time.

Mrs. MILLER. Opening statement from Representative Westmoreland.

Mr. WESTMORELAND. Thank you, Madam Chairwoman, and I want to thank you for holding these hearings.

And I want to thank the witnesses for taking the time to come testify. And Madam Chairwoman, I'm very surprised, with this subject that we are talking about today, that this room isn't

packed, and there aren't people standing out in the hallway waiting to come in here and hear this testimony and hear what we on the committee have to say, because maybe they don't think we are serious about doing anything about this or I promise you there would be a lot more people in this meeting today, because this is a very serious problem we have.

And I think investigating how various regulations harm the manufacturing industry, especially in relation to employees and the threat to making the industry less competitive, is very fitting to this subcommittee's first hearing, and I hope it won't be a continuation of several hearings, but we will hopefully take some action on this problem that we have all identified here today.

It's no secret that the domestic manufacturing industry has steadily lost jobs over the past few years, and we should be quite concerned about that because we have lost approximately 2.8 million jobs. That's a problem, and it's a problem due to our own making in the regulations that we have put on manufacturing. After reading the Manufacturing Institute's report and seeing that the cost to do business in the United States has increased 22 percent because of regulations and restrictions on all levels of government, these things such as corporate taxation, increasing health care and pension benefit costs, tort litigation, rising energy costs and the costs of regulatory compliance, we need to act and need to act now.

Furthermore, the report estimates total regulatory compliance costs for U.S. manufacturers to be $160 billion per year. I'm anxious to hear how we are going to solve these problems, because these are problems that you understand that we have built on our own manufacturing due to the fact that we continue to give agencies, government agencies, more and more power to shepherd or over-regulate the businesses in this country that have made our industry so great here.

I mean, come on, this is equivalent to 12 percent excise tax on manufacturing. I'm anxious to hear what this panel has to say and very interested in what we can do to ease these burdens on our domestic manufacturing industry. After all, the manufacturing sector of this country is an engine, if not the engine, of our economy. Thank you, Madam Chairwoman.

Mrs. MILLER. Thank you.

Before we begin receiving testimony from the witnesses, I want to remind everyone that we would like you to keep your verbal testimony to 5 minutes if you could. And in front of you on the table, you are going to see a little box there that will let you know when your time is up. When it lights up yellow, you have 1 minute remaining. And when 5 minutes have expired, the red light will appear, and we would like you to wrap up your testimony when you see the red light come on. It is the custom of this committee to swear in all of our witnesses, so if you could please rise and raise your right hands.

[Witnesses sworn.]

Mrs. MILLER. Our first witness that the subcommittee will hear from is Mr. Al Frink. He is the Assistant Secretary for Manufacturing and Services within the Department of Commerce. Assistant Secretary Frink was confirmed in September 2004. Prior to coming to Washington, Mr. Frink co-founded the carpet manufacturer

Fabrica in 1974 with $100,000 from the Small Business Administration. He has been a member of several boards and committees and has been particularly active in the Hispanic and Native American communities. In 2004, he was inducted into the prestigious Small Business Administration Hall of Fame.

Assistant Secretary Frink, thank you for being here.

STATEMENTS OF AL FRINK, ASSISTANT SECRETARY FOR MANUFACTURING AND SERVICES, U.S. DEPARTMENT OF COMMERCE; JOHN D. GRAHAM, PH.D., ADMINISTRATOR, OFFICE OF INFORMATION AND REGULATORY AFFAIRS, OFFICE OF MANAGEMENT AND BUDGET; AND GOVERNOR JOHN ENGLER, PRESIDENT, NATIONAL ASSOCIATION OF MANUFACTURERS

STATEMENT OF AL FRINK

Mr. FRINK. I'm watching this clock. Good morning to you, Madam Chairwoman and Ranking Member Lynch and all the other members of the subcommittee. I respectfully ask that my written statement be accepted into the record.

Mrs. MILLER. Without objection.

Mr. FRINK. I would like to thank you for inviting me here today to discuss manufacturing and update you on the Department of Commerce's progress on implementing recommendations from the Manufacturing in America Report, including regulatory reform efforts.

Two years ago, President Bush and former Secretary Donald Evans focused directly on the issues affecting U.S. manufacturing and competitiveness at home and abroad. Under their leadership, 27 roundtables took place across the country which included companies small, medium and large in various industry sectors. The purpose of those were to solicit input directly from a variety of manufacturers.

The results of these discussions were compiled and published in a book called Manufacturing in America. That report was released early last year, and it includes 57 recommendations that are intended to foster conditions that enable manufacturers to compete in this competitive global economy. Some of the recommendations have already been implemented, and some of these include the following: creating the first ever manufacturing council to represent the interests of manufacturing; taking significant steps to protect intellectual property rights; and of course, the newly created position of assistant secretary of commerce for manufacturing services.

I certainly want to thank the President for granting me this honor and opportunity to be of service. Secretary Gutierrez and myself have a profound appreciation for living the American dream and considerable respect for manufacturing. We are both immigrants and have come from humble beginnings and directed successful manufacturing enterprises, of course with my company being much smaller than the great Kellogg's Corp., together—I try to avoid the great—we bring the value of dual perspectives. We understand as you do that the manufacturing sector is crucial to the overall U.S. economy and its importance in creating good jobs.

Manufacturing is often referred to as the engine that drives the economy, as the Congressman mentioned. As such, it should be mentioned that while the manufacturing report reflects my marching orders, you cannot learn everything from reading a book. Therefore, I believe it was crucial in my early stages to go on a listening and learning tour across America to speak with manufacturers on a one-to-one basis and understand their concerns firsthand.

To date, I have personally visited and addressed over 13,000 manufacturers. From these travels, one common concern was expressed. There is a need for regulatory reform. I have seen both the positive and negative impacts of regulations in my own business and the businesses throughout the United States. Well-thought-out regulations can be enacted, and many are, that minimize the cost burdens for manufacturers while still achieving improvements to the quality of our lives.

I have also found that a vast majority of manufacturers are very environmentally conscious. They recognize that they also have to live in the environment they create. For example, in my carpet company, we used to, as a matter of practice, be the biggest user of water in the city of Santa Anna, CA, and the water we used was all reclaimed. And yet the processes we put into place produced water that was actually better than what went into our facility. We used to take a little liberty and say that it was near drinkable quality. We are very concerned about the environment, and I found surprisingly so many companies in my travels feel the same way. Therefore, we are committed to working with OMB, SBA and other Federal agencies to improve the regulatory process for business and for the quality of life, speaking to Congressman Lynch's concerns.

To assist in this effort, we have established an Office of Industry Analysis to provide additional analytical capacity through a regulatory process, and we appointed a new deputy assistant secretary to lead that effort. In addition, Secretary Gutierrez will soon be asking fellow Cabinet secretaries to name a manufacturing liaison from their departments to serve on an interagency task force on manufacturing. This task force will facilitate and coordinate a Federal approach to the challenges facing the manufacturing sector, including the regulatory issues.

I will close by saying, we are continuing to address the issues affecting manufacturing and look forward to working with you and the subcommittee to help manufacturers unleash the creativity, hard work, and innovation that are the engine of the American dream. Thank you.

[The prepared statement of Mr. Frink follows:]

Frink

Testimony of The Honorable Albert A. Frink
Assistant Secretary for Manufacturing and Services
International Trade Administration
U.S. Department Of Commerce
Before the
Subcommittee on Regulatory Affairs
Of the
Committee on Government Reform
U.S. House of Representatives
Washington, D.C.
April 12, 2005

Introduction

Good Morning, Madam Chairman, Ranking Member Lynch and other Members of this Subcommittee. Thank you for asking me to appear today to discuss the current state of manufacturing in America. I would also like to update you on the Department of Commerce's progress in implementing recommendations from the *Manufacturing in America* report, including regulatory reform efforts. But, first, allow me to congratulate you on assuming the Chair of this new Subcommittee. This Subcommittee will be an important forum for addressing regulatory issues concerning U.S. businesses. I look forward to working closely with you and the other members in the months ahead.

Current State of Play in Manufacturing

Strengthening American manufacturing is a top priority for President Bush and Secretary Gutierrez and we are taking definitive steps to ensure that manufacturers remain competitive in the global marketplace, including assessing the impact of regulation. Manufacturing is an integral part of the U.S. and global economies. It is part of the network of inter-industry relationships that create a stronger economy and the conditions for growth. The sector currently accounts for 14 percent of GDP and employs over 14 million workers.[1] The United States is the world's largest economy and has the world's largest manufacturing sector. In fact, U.S. manufacturing alone would be the 7th largest economy in the world – nearly equal to China's entire economy.[2]

The U.S. economy went into recession in early 2001 and the President and Congress quickly responded with just what the economy needed: tax relief. Tax relief has continued to help revive the general economy, and the manufacturing sector in particular. Let me give you a few

1 Bureau of Labor Statistics, Department of Labor, and Bureau of Economic Analysis, Department of Commerce
2 International Monetary Fund

economic indicators to describe the current state of play in manufacturing:

- **Manufacturing output** in February 2005 was 10 percent above the recession low in the fourth quarter of 2001[3]

- **Manufacturing productivity** has been growing rapidly over time and has increased 76 percent since 1990, while productivity in the entire economy rose 42 percent for the same period. Manufacturing productivity is up 4.7 percent from a year ago[4]

- **Manufacturing profits** continue their upward trend since the recession low and have risen by more than 25 percent[5] from last year

- **Manufacturing employment** is at 14.3 million, up 23,000 for the year

- **Manufacturing wages** have increased since the fourth quarter of 2001. Nominal hourly wages of manufacturing production workers increased from $14.95 per hour to $16.39 per hour between the fourth quarter of 2001 and the first quarter of 2005[6]

- **Manufacturing capacity utilization** has increased from 72.6 percent in the fourth quarter of 2001 to 78.5 percent in February 2005[7]

- **Manufacturing industrial production index** has gone up from the fourth quarter of 2001 when the monthly average of this index was 110.4. Industrial production in the sector has increased by 9.4 percent to a value of 120.9 as of February 2005[8]

- **Manufactured goods shipments** are also on the rise from the third quarter of 2001, when the monthly shipments averaged $321.3 billion per month. In January of 2005 shipments totaled $389.4 billion, an increase of $68.1 billion, or 21.2 percent[9]

International trade is also vitally important for the manufacturing sector. Exported U.S. manufactured goods account for over 60 percent of all U.S. exports of goods and services, while supporting over 7 million American jobs. Approximately 50 percent is directly attributable to the manufacturing sector with the balance in supplying support from sectors outside of manufacturing. In fact, U.S. manufactured exports are up 12 percent from a year ago and reached $624 billion in December 2004.[10]

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3 See Federal Reserve Board, Industrial Activity: Industrial Production and Capacity Utilization G.17. March 2005
4 Bureau of Labor Statistics, Department of Labor
5 U.S. Census, Department of Commerce
6 Bureau of Labor Statistics, Department of Labor
7 Federal Reserve Board
8 Federal Reserve Board
9 U.S. Census, Current Industrial Report M3
10 U.S. Census Bureau, Foreign Trade Statistics

We at the Department of Commerce are confident that the outlook for manufacturing is good, but we cannot be complacent. The domestic and global economies are fiercely competitive and we will need to work very hard to stay on top. Overall competitive conditions for the United States have been improving and the manufacturing sector is doing well and will do even better in the future.

The President's Plan:

President Bush is committed to building an economic environment that encourages innovation, lowers the cost of doing business, makes our economy more flexible and promotes economic growth. For example, the President's plan:

- Allows families to plan for the future by making tax relief permanent.
- Encourages investment and expansion by restraining Federal spending and reducing regulation.
- Makes our country less dependent on foreign sources of energy through a comprehensive national energy policy.
- Expands trade and levels the playing field to sell American goods and services across the globe.
- Protects small business owners and workers from frivolous lawsuits that threaten jobs across America.
- Lowers the cost of health care for small businesses and working families through Association Health Plans, tax-free Health Savings Accounts, and credits for employer contributions to Health Savings Accounts, Medical Liability Reform, and health information technology.
- Prepares workers for jobs in the 21st century by improving school standards while reforming workforce training and increasing the number of people served.

We are making great strides in supporting the President's plan through implementing the recommendations of the *Manufacturing in America* report. With 18 specific recommendations completed in less than one year, the Department of Commerce will continue making progress on these recommendations and other efforts to ensure the competitiveness of all U.S. manufacturing businesses.

Implementing recommendations from the *Manufacturing in America* report

Madame Chairman, in order to advocate more strongly for the interests of U.S. manufacturers, I set out to learn what was most important to them. Since taking office in September 2004, I have visited more than 70 manufacturers, chaired 47 roundtable discussions, attended three Chamber of Commerce meetings, addressed 24 industry association groups, participated in three Presidential Export Council meetings, led an eight-day trade policy mission to China, met with senior officials in Japan and presided over two Manufacturing Council meetings. I am pleased to tell you that there is a renewed optimism in the manufacturing sector and many of the manufacturers I spoke with have plans to increase investment and hire more workers. The concerns expressed during my "Listening and Learning Tour" are being addressed through our implementation of the key recommendations of the *Manufacturing in America* report:

- Enhance government's focus on manufacturing competitiveness
- Develop analytical expertise and strategies to assess manufacturing competitiveness
- Reduce the cost of regulation and legislation
- Promote open markets and a level playing field
- Facilitate investment in innovation and developing strategies to expand U.S. manufacturing

I will continue to review the progress in each of these areas and especially look for ways to encourage well thought-out, cost-effective regulations.

Enhance Government's Focus on Manufacturing Competitiveness
Manufacturing and Services (MAS) leadership is now in place within the International Trade Administration, where we are addressing manufacturing issues and reaching out to all manufacturing constituencies. We now have an Assistant Secretary for Manufacturing and Services, a Deputy Assistant Secretary for Industry Analysis and a Director for the Office of Economic Analysis. We will continue to build this team to ensure that the concerns of manufacturers are heard and addressed.

In April 2004, the Department of Commerce established the Manufacturing Council, which is structured along the lines of the Industry Trade Advisory Committees (ITACs), to provide oversight and advice on the implementation of the President's Manufacturing Initiative. Secretary Gutierrez will work directly with the Council and rely on its recommendations. In fact, his first domestic trip as Secretary was to the Manufacturing Council's February meeting in Dearborn, Michigan.

The Council will play an integral role in identifying priority manufacturing issues and advising the Secretary. The Council has already prepared task force reports on workforce issues, tort reform and market access. These on-going dialogues will provide sound information about the needs of U.S. manufacturing and the impact of federal government efforts.

Secretary Gutierrez will soon ask fellow cabinet secretaries to each name a manufacturing liaison to serve on an Interagency Task Force on Manufacturing. This Task Force will facilitate

a coordinated Federal approach to the challenges facing the sector, including regulatory issues.

Develop Analytical Tools or Procedures and Expertise to Assess Manufacturing Competitiveness
We are working closely with the Small Business Administration Office of Advocacy and the Office of Information and Regulatory Affairs at OMB and others to develop analytical tools and expertise to assess manufacturing competitiveness. These tools will provide us with the means to better gauge the larger economy-wide effects of regulations and help us determine the validity of pre-regulation forecasts. As such, our analytical focus will be both in assessing new regulations as well as identifying existing regulations that are appropriate for reform.

We are recruiting skilled economists to support this new initiative and will reassign staff to this activity as needed. Additionally:

- In May, we are launching an intensive five-day training seminar for our analysts to develop expertise in the federal regulatory process and in conducting in-depth cost benefit analyses of current and proposed regulations.

- We also recently signed a first-ever Cooperative Agreement with George Mason University to provide a formal framework for enhancing the educational opportunities and skills of Manufacturing and Services staff, which, in turn will improve the industry and economic analysis conducted in the organization.

Facilitate Investment in Innovation and Developing Strategies to Expand U.S. Manufacturing
Innovation is critical for the continued competitiveness of U.S. manufacturing and the U.S. economy as a whole. We must continue to support a business climate where innovation is a fundamental business practice as outlined in the President's pro-growth strategy.

The Department of Commerce currently chairs an interagency working group on manufacturing R&D which serves as a forum for developing a consensus and resolving issues associated with manufacturing R&D policy, programs, and budget guidance and directions. This helps ensure coordination of innovation and productivity-enhancing technologies conducted by the Federal government. We also facilitated the creation of a National Virtual Network of Centers of Manufacturing Excellence and established cooperative research programs that will focus on manufacturing technologies among national laboratories, universities, community colleges, and local technology development associations. The President signed Executive Order 13329, *Encouraging Innovation in Manufacturing*, through the Small Business Innovation Research Program (SBIR). The Department of Commerce is developing action plans to comply with this Executive Order.

Promote Open Markets and a Level Playing Field
Open markets foster innovation, growth and help keep our manufacturers on the cutting edge. We will continue to work with the Office of the United States Trade Representative to promote open markets and ensure a level playing field. I recognize the integrity of this on-going work must be maintained as we build new capabilities to ensure that manufacturers remain

competitive. Let me illustrate some of the work we undertake to support U.S. manufacturers:

- We provide critical input and analysis during virtually all trade and trade related negotiations to ensure that U.S. industries' priorities, especially those of our manufacturers, are taken into account and domestic sensitivities are factored into the Administration's negotiating position.

- We identify best export prospects for U.S. firms based on a methodology that incorporates data analysis and assessments from ITA's industry specialists and country desk officers, effectively linking agreements to the National Export Strategy.

- We publish a variety of comprehensive reports for U.S. suppliers after each negotiated trade agreement. These reports, which are distributed to the business community through US Commercial & Foreign Commercial Service, (US&FCS) posts, focus on export opportunities for specific sectors and agreement-wide gains.

- We work to defend the interests of U.S. manufacturers by conducting comprehensive analyses of sanctions against U.S. exports and by developing recommendations for sanctions against foreign countries resulting from trade disputes.

In addition, ITA has taken several measures domestically to combat unfair trade practices affecting U.S. manufacturing. These include:

- The establishment of the Office of Investigation and Compliance to ensure that our trading partners honor their commitments.

- The creation of the Unfair Trade Practices Task Force to go on the offensive and attack the underlying causes of inequitable trade.

- The placement of intellectual property rights experts in several countries to assist with implementing the WTO Trade and Intellectual Property Rights (TRIPS) agreement.

Similarly, because China's trading practices are a continuing major concern to the Department, we have undertaken a number of new steps to reinforce the Administrations' strategy on China. These include establishment of the Intellectual Property Rights (IPR) Policy and Compliance Investigations Office, increased staffing and recruitment of top language-qualified China experts to manage our China compliance efforts, the creation of a China Office in our Import Administration to focus and deepen our expertise on unfair trade cases from China, and for the first time, using technology to enable compliance officers in China and the United States to work collaboratively on compliance cases in the Market Access and Compliance Bureau on a real-time basis.

International trade is an important means for improving the U.S. manufacturing environment,

and the Department will continue to be vigilant about the trading practices of our partners.

Reduce the Cost of Regulation and Legislation
Now, let me turn to the costs of regulation and legislation.

The Commerce Department supports maintaining high standards for the environment, health, worker safety and other issues that affect our quality of life. Regulations and regulatory reform efforts must be well thought-out and cost-effective while achieving intended goals.

The government must ensure that regulations designed to improve our quality of life are effective and equitable, and that the cost of compliance is minimized to remain competitive in the global marketplace. Reducing the cost of compliance may often be a matter of fine-tuning the implementation of the regulation as opposed to the total overhaul or elimination of the regulation. Or, it might just mean applying some common sense.

This Administration is proud of its activities in the field of regulation and has an excellent record. John Graham, who is here today, highlighted the following points from OMB's draft 2005 report on the Costs and Benefits of Federal Regulations:

- The estimated annual benefits of Federal regulations reviewed by OMB from October 1, 1994 to September 30, 2004 range from $68.1 billion to $259.6 billion, while the estimated annual cost range from $34.8 billion to $39.4 billion.

- The average yearly cost of major regulations issued during the Bush Administration is about 70 percent less than over the previous 20 years.

- The average yearly net benefit of the major regulations issued during the Bush Administration is over double the yearly average for the previous eight years.

Fully assessing the costs and benefits of federal action is complex and resource-intensive. Also, factors that directly impact manufacturing competitiveness must be addressed including: potential declines in product quality, price-induced changes in consumption, loss of business freedom, privacy concerns, security measures, innovation and others.

Regulations often disproportionately affect manufacturing. A study commissioned by SBA's Office of Advocacy found that manufacturing firms face a total regulatory burden approximately six times greater per firm than the average for all firms, and a regulatory burden per employee approximately two times greater than the average for all firms[11].

The additional cost of regulations to small businesses is particularly worrisome. Economies of scale can result in small businesses being disproportionately impacted by regulatory costs.

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11 Crain and Hopkins, the Impact of Regulatory Costs on Small Firms: A Report for The Office of Advocacy, U.S. Small Business Administration. 2001

Equally worrisome to small and large businesses is the increasing regulatory requirements over time.

Clearly, we must strive to reduce unnecessary burdens that negatively affect U.S. manufacturers, while maintaining the spirit and effectiveness of those regulations intended to improve our quality of life. Within Manufacturing and Services, we maintain expertise across a range of industry sectors, including aerospace, motor vehicles, machinery, raw materials, information technologies, and services, to name a few. We will work with OMB, SBA and the regulatory agencies to use this unique expertise to provide assistance, analyses, and recommendations where appropriate.

The 2004 draft OMB Report to Congress on the Costs and Benefits of Federal Regulations also provides an example of how collaborative public-private partnerships can help reduce the burdens imposed by unnecessary regulations. OMB requested public nominations of specific regulations, guidance documents and paperwork requirements that, if reformed, could result in lower costs, greater effectiveness, enhanced competitiveness, more regulatory certainty and increased flexibility. In response to this solicitation, OMB received 189 distinct manufacturing reform nominations from 41 commenters. OMB, in consultation with the Department of Commerce and other federal agencies, determined that 76 of these have potential merit and justify further actions.

The 76 reform priority nominations were categorized as follows:

Agency	Nominations
Environmental Protection Agency	42
Department of Labor	19
Department of Transportation	5
Department of Homeland Security	3
Federal Communications Commission	2
Department of Agriculture	1
Department of Commerce	1
Department of Health and Human Services	1
Department of The Treasury	1
Equal Employment Opportunity Commission	1

Source: Office of Management and Budget, Regulatory Reform of the U.S. Manufacturing Sector

Future actions on these reform nominations range from performing a priority investigation to issuing modernized regulations. Public participation will be solicited before any regulatory reforms are adopted. We will work with OMB and federal regulatory agencies to assess how any proposed changes might affect manufacturers.

Conclusion

In closing, I have spent my entire career in the business sector building a manufacturing company. One of the lessons I have learned, is that business continually needs to innovate to grow, produce new and better products, and remain competitive. Many manufacturers are implementing lean production procedures to remain competitive. While improved means of production is important, I continue to convey that without innovation there is no life after lean.

There are no magic bullets. We realize there are many challenges facing U.S. manufacturing and while we are making progress, there is much more to do. A strong and vibrant manufacturing sector is critical to providing good jobs and maintaining a growing healthy economy. President Bush and Secretary Gutierrez are committed to taking actions that create conditions for economic growth and innovation in the manufacturing and service sectors. We are also devoting renewed efforts to strengthen education, retraining, and economic diversification.

I look forward to working with this Subcommittee to meet the challenges facing U.S. manufacturing and welcome any questions you may have. I am also very interested to listen to the views of the Subcommittee on how we in Commerce might best advance these efforts.

Thank you.

Mrs. MILLER. Thank you very much.

Our next witness this morning is Dr. John Graham, who is the Administrator of OMB's Office of Information and Regulatory Affairs. He was born and raised in Pittsburgh. Dr. Graham founded and led the Harvard Center for Risk Analysis from 1990 to 2001. Confirmed in July 2001, Dr. Graham is on leave from the faculty at Harvard's School of Public Health, where he taught graduate students the methods of risk analysis and cost-benefit analysis.

Dr. Graham, good morning, appreciate your time.

STATEMENT OF JOHN GRAHAM, PH.D.

Mr. GRAHAM. Good morning, Madam Chairwoman, members of the subcommittee, I appreciate the opportunity to testify this morning on the subject of regulation of the manufacturing sector. There is, in fact, a sea of existing Federal regulations. Let me give you some ballpark figures. Since OMB began to keep records in 1981, Federal agencies have adopted over 115,000 new Federal regulations. Of those, we at OMB reviewed and cleared 20,000 of them. And of those, over 1,100 were estimated to cost the economy $100 million or more when they were issued.

Sad as it is to say, I have to confess that most of these regulations have never been reexamined to determine whether they accomplish their purpose, how much did they really cost and what were the benefits. I should also say that not all sectors of the economy are equally impacted by this growth of Federal regulation. We all know, for example, that in the health care industry, physicians and nurses are heavily impacted by Federal regulation and paperwork. But it turns out that economic studies have shown that the sector that is most affected, when you compare it on the measure of burden per employee, is the manufacturing sector of the U.S. economy.

And as you said, Madam Chairwoman, these manufacturing firms are now competing in an increasingly global economy. So when we add additional regulatory burden that is without justification, we are placing these companies and we are placing jobs at risk. In the Bush administration, we have taken modest steps to address this area. In February 2004, we announced an open opportunity for the public to suggest reform of manufacturing regulations. The focus in particular was on ways to help small, medium-sized or any manufacturing firm compete in a global economy without compromising the benefits of Federal regulation, whether those benefits be safety, health, environment or homeland security or otherwise. The result of that initiative is that we received at OMB, 189 suggestions from 41 commentors. We then took those suggestions and we instituted a process of analysis and deliberation, both at the Federal agencies and at OMB. And I'm particularly pleased to report, this morning, I received technical assistance evaluating these nominations from both the advocacy office of the Small Business Administration and our colleagues who are here this morning from the Department of Commerce. The result is the administration has identified 76 of these reform ideas as worthy of further examination and action.

Now I would like to report to you this morning that the mere designation of these 76 priorities means that they will get done.

But I have been in Washington for enough years now to confess to you with some humility that we have a long way to go to get these 76 reforms done. And let me explain to you why that is. First of all, we have found through experience that regulators find it more interesting and more exciting, if you will, to craft new regulatory programs than to go into the existing regulations and modernize them or streamline them. And there can be lots of psychological reasons for why that's the case. And in fact, many cases, the people that need to do this work were involved in crafting those regulations in the first place. The whole task we are talking about engaging in is not one that is the natural inclination of a Federal bureaucracy.

Second, there is no real course to the commentors who suggested these reforms if the agency does not get it done. These are discretionary actions that the agencies may take, but it is not backed up with the threat of litigation which often exists for a new regulation where an agency may be obliged by an act of Congress to do a new regulation or face legal threat in the Federal courts. And then you might ask, why isn't OMB there to make sure the agencies do their work? And I'm here to assure you that we are here, but we are a modest organization. And recently, as you know, cuts in staffing as a result of our last budget, sharing in some of the downsizing that a lot of the American economy is experiencing and our staffing resources are modest to oversee an effort of this magnitude.

I want to conclude on a note of optimism. The 76 ideas are modest; they are practical. They do not threaten the health, safety and environment of our country. They do not require congressional action, but we do however want your support. And the agencies have committed to deadlines and milestones for making decisions in these areas. Thank you very much for your interest in this issue, and we look forward to working with you.

[The prepared statement of Mr. Graham follows:]

STATEMENT OF
JOHN D. GRAHAM, PH.D.
ADMINISTRATOR,
OFFICE OF INFORMATION AND REGULATORY AFFAIRS
BEFORE THE
SUBCOMMITTEE ON REGULATORY AFFAIRS
OF THE
COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

April 12, 2005

Madam Chairman, and Members of this Committee, I am John D. Graham, Ph.D., Administrator, Office of Information and Regulatory Affairs, Office of Management and Budget. Thank you for inviting me to this hearing and for giving me the opportunity to testify today on the reform of regulations that impact the United States manufacturing sector.

Modernizing and streamlining the sea of existing federal regulations is an immense and humbling challenge. Since OMB began to keep records in 1981, there have been 115,966 final rules published in the Federal Register by federal agencies. Of these published rules, 19,538 were formally reviewed by OMB prior to publication. Of the OMB-reviewed rules, 1,068 were considered "major" or "economically significant" rules, primarily because they were estimated to have an economic impact greater than $100 million in any one year.

Sad as it is to say, most of these existing federal rules have never been evaluated to determine whether they have worked as intended and what their actual benefits and costs have been. During President Bush's first term, OMB initiated a program to take a second look at a limited number of these existing regulations, guidance documents, and paperwork requirements, as we are authorized to do under what's known as the Regulatory Right to Know Act.[1] Our February, 2004 request for reform nominations, with a clear focus on the manufacturing sector of the U.S. economy, was the third such solicitation of reforms undertaken by this Administration.

To briefly summarize the previous reform initiatives, in 2001 OMB requested public nominations of rules that should be rescinded or modified. We received 71 nominations from 33 commenters, and OMB determined that 23 of the nominations should be treated as "high priority" review candidates. Federal agencies have taken at least some action (e.g., a proposed or final rule) on nearly 75% of these reform nominations. Overall, OMB regards the 2001 solicitation as a successful endeavor. In 2002, OMB again requested public nominations of reforms. In an important innovation, we included guidance documents and paperwork requirements, as well as rules, within the scope of the solicitation. We received 316 distinct reform nominations from more than 1,700 commenters. OMB and the agencies determined that 156 of the nominations should be referred to agencies for their consideration. In 2002, OMB did not attempt to define "high priority" reforms for two reasons: the large volume of nominations exceeded the capabilities of OIRA staff to evaluate them; and we felt the agencies might take

[1] Section 624 of the Treasury and General Government Appropriations Act of 2001 (31 U.S.C. § 1105 note, Pub. L. 106-554)

greater ownership of reforms if they decided which were to be treated as a priority. We have determined, however, that only about 1/3 of the 2002 nominations referred to the agencies have resulted in agency action. Appendix D of our 2004 final Report to Congress on the Costs and Benefits of Federal Regulation[2] contains an item-by-item update on the status of each of the 2001 and 2002 nominations as of December, 2004.

We decided to focus our 2004 regulatory reform initiative on the manufacturing sector, which is one of the most heavily regulated sectors of our economy. In the 2004 Economic Report of the President, the Council of Economic Advisors found that the recent economic downturn hit the manufacturing sector hard, starting earlier and lasting longer in that sector of the economy. The Department of Commerce, in their 2004 report *Manufacturing in America*, recommended regulatory reform as a key activity government can undertake to ensure the continued competitiveness of U.S. manufacturing. Since U.S. manufacturers compete with firms from both developed and developing countries in an increasingly global economy, the Administration believes it is critical that any unnecessary regulatory burdens be removed.

We also applied the lessons learned from the 2001 and 2002 processes to our latest round of reform requests. First, we offered additional guidance to commenters on how to suggest reforms. We asked that commenters try and make a benefit-cost case for the reform, as many of the rules that are potential reform candidates undoubtedly generate substantial benefits. We also recommended that commenters focus on reforms that agencies can move forward on without statutory change. Our experience with previous years taught us that these are the types of reform suggestions that are likely to lead to agency actions.

In December 2004, OMB released for agency review the 189 reform nominations that were submitted by 41 industry and non-profit groups in response to our request. OMB instructed federal agencies to review the merits of each of the reform nominations and prepare a response for OMB. The responses included a determination as to whether reform action is appropriate, and if appropriate a time-line for action and a plan for public participation. OMB evaluated the reform nominations and collaborated with federal agencies in the development of response plans. OMB also sought evaluations of the recommendations by the Advocacy Office of the Small Business Administration and the Department of Commerce's Office of the Assistant Secretary for Manufacturing and Services.

Of the 189 nominations, 76 were selected by the agencies and OMB for priority consideration and action by the Bush Administration. OMB's report on Regulatory Reform of the U.S. Manufacturing Sector[3] summarizes each of the 76 reform nominations and the time-specified steps Federal agencies will take to address them. The majority of the 76 reform nominations address programs administered by the Environmental Protection Agency and the Department of Labor, a pattern that reflects the large impact of environmental and labor regulation on this sector of the economy. Recommended actions range from gathering and reporting additional information to issuing modernized regulations.

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[2] Available on our website at http://www.whitehouse.gov/omb/inforeg/regpol-reports_congress.html
[3] Available on our website at http://www.whitehouse.gov/omb/inforeg/regpol-reports_congress.html

Many of the regulations recommended for reform may be instances where the rule regulates to what Justice Stephen Breyer in his book *Breaking the Vicious Circle* has called "the last 10 percent," where a regulatory bar is set so high that it imposes unnecessarily large costs for little to no additional benefit.[4] For example, a nomination for reform at EPA (number 117) recommends modifications to the Industrial Pretreatment Program rules regarding wastewater sampling. Currently, industrial facilities discharging to sewage treatment plants must regularly sample their wastewater for all nationally regulated pollutants listed for their industry, even if they do not use the substance and have no possibility of discharging it. The commenter, the Copper and Brass Fabricators Council, suggested allowing this requirement to be waived if a facility can demonstrate that it does not use the pollutant, and thus the pollutant would not be present in its wastewater. EPA proposed similar modifications in 1999 but never finalized the rule. In response to the final report, EPA has agreed to publish the final rule in an expedited manner in June of 2005.

In closing, OMB is dedicated to this initiative; we will oversee the reform process to make sure that agencies make adequate progress in the months and years ahead. Thank you very much for the opportunity to participate today in this very important hearing.

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[4] *Breaking the Vicious Circle: The Oliver Wendell Holmes Lectures, 1992.* Harvard University Press

Mrs. MILLER. Thank you, Dr. Graham.

Our next witness that the subcommittee will hear from is a former Michigan Governor John Engler. Governor Engler is the president of the National Association of Manufacturers, a post he assumed on October 1, 2004. He certainly is a well respected public official in his own right. Governor Engler served three terms as Michigan Governor from 1991 to 2002, years I remember very, very well. He also served 20 years in the State legislature, including 7 years as the majority leader of the State Senate. He was the youngest person ever elected to the Michigan House of Representatives.

Governor Engler, we are proud to have you here this morning and look forward to your testimony, sir.

STATEMENT OF GOVERNOR JOHN ENGLER

Mr. ENGLER. Madam Chairwoman, members of the committee and your very able committee staff, I'm delighted to be here and thank you for the opportunity to address the subcommittee about the regulatory burden on America's manufacturers.

You have limited to me to 5 minutes in my oral representation. I need not tell you that sort of represents cruel and inhumane punishment for someone who has been in public office as long as I have. We have much to say about Federal regulation and its impact on manufacturing and changes that we believe are needed.

I'm delighted to be with my colleagues this morning on this panel, Mr. Frink and Dr. Graham. I, too, will submit for the record. Let me make a couple of points though in the limited time.

Manufacturers in the United States today are caught up in the most competitive marketplace the world has ever seen. Because manufacturing products are easily transported, we must compete with manufacturers all around the world. One result is the relentless downward pressure on prices. As a practical matter, our members have very little pricing power. While they can't raise prices on their products, they have to contend with steadily rising costs of production. These are not just the basic costs of doing business—labor, capital investment—but also include the subject of today's session, external costs associated with taxes, health care, regulations, litigation, energy.

You mentioned it, Madam Chairwoman, in your opening comments. The NAM study issued last year documented some 22.4 percent a year labor costs in manufacturing higher in the United States compared to nine major trading partners. And Tom Dueseterberg, his people worked directly on that study as a partner with the NAM, and there is more detail in his written testimony. Government regulations hit the manufacturing sector harder than any other sector, probably due to the nature of manufacturing that Ranking Member Lynch mentioned. It is complicated and can be dangerous. There are environmental and safety issues. In at least one study, and I cite that in my written testimony, about 30 percent of the total costs of environmental, economic and tax regulations fall on manufacturers. Now, again, there is a recognition, some of this is probably inevitable given the nature of manufacturing, but our members encounter daily regulatory burdens that simply make no sense and serve no purpose or are unnecessary. I'm

going to use three examples to make the point and talk about the categories.

Old regulations not updated, Madam Chairwoman, I know you are a boater and you are very good at this, so this one was picked for you. Years ago, our—and this has been for years, we have an affiliate, the National Marine Manufacturers Association. They have been pleading with OSHA to update its rules for spray finishing flammable and combustible materials that govern application of resins that are in gel coats on new boats. Technical but that is what manufacturing is, very high tech. The rule now in effect dates back to 1969; conspicuously out of date. And technically, what this means, every boat maker using modern methods could be considered in violation of the rule, thus subject to sanctions and fines. And in today's liability environment, that could be an issue. Despite that, OSHA fails to update this important regulation.

A new regulation but implemented in a questionable fashion, the Family Medical Leave Act, which many of us supported, but it has become a headache for some of our members because of the abuses. One company—Ohio-based, 840 employees—reported to us in 2004 that 221 of its employees or 26 percent claimed a total of 4,100 workdays missed under the Family Medical Leave Act. It is not so much the Family Leave Act, not the birth of a child, but the medical leave portion of this, which was, as you recall, almost an afterthought in the legislation. Family leave is where we were headed with this originally. That same company reported 20 employees did not return to work after exhausting their medical leave of 1,200 days. And yet another 10 incidents of people allegedly on leave were found to be actually physically employed doing other work.

Conflicts, and this is conflicts here at home, sometimes among different regions of the same agency, but this is a conflict that deals with international conflicts. Small manufacturers of heat-sealing equipment report to us that they make equipment to meet specifications of the U.S. market and specifications with the Canadian market. Despite that commitment to compliance, when that equipment goes to Canada, there is a physical reinspection that takes place that adds several hundred dollars to the costs.

These are just a couple of other examples that our members have to deal with. We can't afford to keep wasting resources in this fashion, and I think Congress could do something about it. And I'll close with just a final point. Sarbanes-Oxley, NAM supported passage, and it was a way to safeguard investors and restore confidence, but now the compliance costs have risen to the point and studies show that nearly 6 percent of net income before taxes is taken up by compliance. If you take 6 percent off the bottom line, we would like to work with the policymakers and Congress, regulatory agencies to reduce the compliance costs there. Thank you, Madam Chairwoman. My time has expired.

[The prepared statement of Mr. Engler follows:]

COMMENTS OF THE NATIONAL ASSOCIATION OF MANUFACTURERS
BEFORE THE

SUBCOMMITTEE ON REGULATORY AFFAIRS
OF THE
HOUSE OF REPRESENTATIVES
COMMITTEE ON GOVERNMENT REFORM

APRIL 12, 2005

Chairman Miller and members of the subcommittee on Regulatory Affairs, thank you for the opportunity to testify before you today on behalf of the National Association of Manufacturers about the impact of regulations on U.S. manufacturing. This is an issue of vital importance to our members and one that I hear a lot about in my travels and discussions with member companies.

The NAM is the nation's largest industrial trade association representing small and large manufacturers in every industrial sector and in all 50 states. Through our direct membership and our affiliate organizations – the Council of Manufacturing Associations, the Employer Association Group and the State Associations Group -- we represent more than a hundred thousand manufacturers.

I will do my best to handle questions about specific regulations, especially those cited by the NAM as in need of improvement, but there are thousands of federal regulations on the books. Neither I nor anyone I know can speak authoritatively about every regulation.

I take this hearing to be more about process, rather than the substantive issues that a particular regulation deals with. I hope the subcommittee members understand this limitation.

Background

A good starting point for this discussion is the list of 76 regulations that the Office of Management and Budget (OMB) released on March 9 that were deemed worthy of further consideration by agencies for improvement. This was the latest installment of the Bush Administration's Manufacturing Initiative which recognizes that manufacturing is facing unprecedented challenges. Indeed, the last recession was the first since the end of World War Two that manufacturing both led into a recession and lagged in recovery.

In the first phase of the Manufacturing Initiative, the Department of Commerce went on a listening tour around the country in 2003 to find out what was really going on. Subsequently, the Department issued a report in January 2004, "Manufacturing In America: A Comprehensive Strategy to Address the Challenges to U.S. Manufacturers."

We believe this report is historic in that it is the first time since the days of Alexander Hamilton that our government has formally addressed the importance of manufacturing to our economy and actively identified policies to strengthen manufacturing.

Among the report's recommendations was creation of an Assistant Secretary of Commerce for Manufacturing and Services, and a Manufacturing Council. Another was for OMB to include in its 2004 Draft Report to Congress on the Costs and Benefits of Federal Regulations a call for public nominations of regulations that could be improved, especially those affecting the manufacturing sector.

The NAM solicited our members for suggestions, and they were very forthcoming. Our Regulatory Improvement Task Force reviewed these submissions, highlighting those that were identified repeatedly as particularly onerous. These were: the Particulate Matter (PM) and Ozone National Ambient Air Quality Standards (NAAQS); the Toxic Release Inventory; the Definition of Solid Waste; Spill Prevention Control and Countermeasures; SARA Title III; the Family and Medical Leave Act.; and the FCC "Do Not Fax" rule, which is also an issue with trade associations like the NAM.

In our comments on the Draft Report, the NAM asked OMB—specifically, the Office of Information and Regulatory Affairs (OIRA) that is charged with drafting the report—take special note of these regulations. We told OMB that improving these regulations would help manufacturing.

We also submitted another list of more technical regulations that could be improved. We made clear in our submission that these are small fixes which individually may not have much impact but collectively have a big impact.

There are two significant points I will ask you to keep in mind in considering this exercise.

First, as many of our member companies -- especially smaller companies -- will tell you, it is not one or two particular regulations that impact their productivity and ability to compete, but rather the sheer volume of regulatory requirements.

Second, these regulations are symptomatic of a prevalent attitude of indifference among legislators and federal regulators to the impact of regulations on the private sector. Government is a world in which the concepts of profit and loss have little meaning. When manufacturers speak to government officials about the impact of poorly written rules on industrial efficiency and productivity, and the excessive cost of compliance with such rules, our concerns too often fall on deaf ears. Too many members of Congress and too many regulators just don't get it.

<u>The Disparate Impact on Manufacturing</u>

As the final 2004 OMB Report to Congress on the Costs and Benefits of Federal Regulations notes, federal regulations hit the manufacturing sector especially hard.

Because manufacturing is such a dynamic process, involving the transformation of raw materials into finished products, it creates more environmental and safety issues than other businesses. Thus, environmental and workplace health-and-safety regulations have a disparate impact on manufacturers.

Another report entitled *The Impact of Regulatory Costs on Small Firms*, by Mark Crain and Thomas Hopkins, issued in 2001 by the Office of Advocacy of the Small Business Administration, makes the same point. The burden of regulation falls disproportionately on the manufacturing sector.

In this report, which is now being updated, Crain and Hopkins found that the manufacturing sector shouldered $147 billion of the $497 billion onus of environmental, economic, workplace and tax-compliance regulation in the year 2000.

Overall, Crain and Hopkins found that the per employee regulatory costs of businesses with fewer than 20 employees were $6,975, or 60 percent more than the cost per worker of $4,463 for firms with more than 500 employees.

In manufacturing, this disparity was even wider. The cost per employee for small firms (meaning fewer than 20 employees) was $16,920, or 127 percent higher than the $7,454 cost per employee for medium-sized firms (defined as 20–499 employees). And it was 140 percent higher than the $7,059 cost per employee for large firms (defined as 500 or more employees). Crain and Hopkins acknowledge that their methodology does not attempt to capture the benefits of regulation.

In December 2003, the NAM released a report, *How Structural Costs Imposed on U.S. Manufacturers Harm Workers and Threaten Competitiveness,* which has received considerable attention from media, business and policy experts.

This report, which is available over the Internet at www.nam.org/costs, examined structural costs borne by manufacturers in the United States compared to our nine largest trading partners.[1] The principal finding was that structural costs—those imposed domestically "by omission or commission of federal, state and local governments"—were 22.4 percent higher in the U.S. than for any foreign competitor.

The structural costs included regulatory compliance, along with excessive corporate taxation, the escalating costs of health and pension benefits, the escalating costs of litigation and rising energy costs.

In order to determine the effect of regulation on domestic manufacturing compared to our main competitors, the NAM Report used pollution-abatement expenditures because they are the only cross-country regulatory compliance cost data available. Thus, the 22.4 percent higher structural costs that U.S. manufacturers face in comparison with our largest trading partners are significantly understated because the regulatory component includes only pollution-abatement expenditures.

Even so, just including these specific costs puts the United States at a trade-weighted disadvantage of at least 3.5 percentage points. Only South Korea's pollution-abatement costs are higher; all other U.S. trading partners, including the so-called "green" nations in Europe, have much lower regulatory costs.

[1] Canada, Mexico, Japan, China, Germany, United Kingdom, South Korea, Taiwan and France

The NAM recognizes the need for reasonable regulations, but we believe rules should be based on sound science and subjected to a strict cost-effectiveness test.

In most cases, market-based solutions can address our concerns. A market-based approach allows the agency to set a standard but also allows the regulated entities the ability to identify innovative—and probably far more efficient—ways to meet that standard than if the agency relies exclusively on "command and control" methodology and technology.

"The List": What It Means, Its Importance and Next Steps

When OMB released its list of regulations on March 9, there was a predictable hue and cry among some activist groups and the news media that it would lead to a reduction of environmental, worker and consumer protections.

Let's be clear. All OMB did was inform the agencies to review the nominated regulations cited in the OMB Report to see if they should be changed. It did not instruct the agencies what specific action to pursue.

The OMB said merely that administrative fixes should be done sooner rather than later, while more substantive changes should be subject to the standard notice-and-comment procedures.

Let me make one more thing clear: we do not seek to compromise the effectiveness of regulations.

Rather, we seek the review and change of regulations that are either out of date or more restrictive and costly than they need to be to achieve the desired goals.

The list, including its timetables for action, provides a guide for this subcommittee, the authorizing committees, regulated entities, other interested parties and OMB to see how—or whether—the agencies will take this exercise seriously and meet their responsibilities.

Unlike a similar undertaking in the 2002 OMB Report, this time around, the agencies will have less ability to bury the recommendations until people forget about them. At least, that is our hope.

Let's take one particular example. In 2002, the NAM nominated an OSHA regulation dealing with fire protection standards that apply when boat builders are using a specific type of resin.

While I am not expert in all of the details about this regulation, we have been informed by the National Marine Manufacturers Association, an affiliate of the NAM, that these rules are based on a 1969 consensus rule of the National Fire Protection Association, and are conspicuously out of date.

It amazes me to report to this subcommittee that nothing came of this NAM nomination for a regulatory improvement. OSHA has repeatedly been petitioned to update this obsolete fire standard and the agency has not acted. To date, OSHA has given no reason for its intransigence.

This OSHA fire standard is one of the 76 regulations on the March 9 list (Reference Number 153). At first glance, this would seem to be good news. On closer inspection, though, I ask you to observe that OSHA is not actually asked to fix this specific audacious example of a regulation in need of improvement.

To the contrary, OSHA is directed to review *all* of its "standards that are based on national consensus standards." There is no timetable. My fear is that OSHA will use the excuse that reviewing all of its standards is a big job and will once again duck such an easy and necessary fix unless this subcommittee, OIRA and other watchdogs with authority ensure that something is done.

I'd ask the subcommittee to consider, as the NAM noted in its submission to OMB last year, what OSHA's reaction would be upon entering a manufacturing facility and finding that a Material Safety Data Sheet had not been updated in 36 years. Would the inspector look the other way because it was common knowledge that handling procedures have changed?

I don't think so. Remember, this standard is in the Code of Federal Regulations, and thus it has the force of law. A marine manufacturer could, technically, be cited for not adhering to the 1969 standard.

Another regulatory improvement that the NAM suggested as a general matter is for agencies to explore making on-line forms available in multiple formats.

At a minimum agencies should either adopt a process that anybody can use in filling out a form electronically, or at least make their forms available in several formats to reduce the complexity of companies having to convert their reports into different formats.

The benefits reaped by the savings for regulated entities from not having to convert the document would far outweigh any incremental cost to the agency.

As for the seven regulations that the NAM highlighted, I am pleased to note that OMB included five on its list. As this subcommittee knows, however, the PM and Ozone NAAQS regulations are being reviewed under a separate procedure.

The only highlighted regulation not included was SARA Title III. The NAM looks forward to working with the agencies and making appropriate comments as they consider ways to improve the other regulations.

For the Do-Not-Fax Rule, of course, Congress is poised to address this legislatively.

Recommendations

What can this subcommittee do to assist manufacturers confronting a myriad of regulatory requirements?

1. **Conduct Oversight to Ensure that Agencies Act on the March 9 List. While OIRA has an established role both through statutory and executive order authority to oversee agency promulgation of regulations, it has, at best, only moral suasion in its quiver. Congress holds the power of the purse to help ensure that agencies do not ignore these recommendations.**

2. **OIRA Should Have More Staff. OIRA was originally authorized for about 90 staff members, and by the 1990's had been reduced to fewer than 50. It is now closer to 60. This is not sufficient. Staffing levels should be increased further.**

3. **Parts of E.O. 12866 Should Be Made Statutory. President Clinton issued E.O. 12866, the controlling executive order for regulatory review, in 1993. E.O. 12866 calls for sound science, cost-benefit analysis and requires that the regulatory path chosen should be the least burdensome. Congress should give this mandate statutory authority to ensure that its procedures remain in force and will give them certainty. The NAM encourages you to pursue discussions with OIRA on this score.**

4. **Guidance Documents Should Be Subject to OIRA Review and Released Publicly. Guidance documents, issued to inspectors and other enforcement agents, clarify the meaning of a regulation but are far too often not shared**

with the public. They are not subject to notice-and-comment and therefore can change easily. And it goes without saying that the way a rule is enforced can offer a "back door" way to changing the rule itself.

5. The Role of the Department of Commerce in Regulatory Review Should Be Clarified and Made Statutory. In creating the Assistant Secretary of Commerce for Manufacturing and Services, the President included the review of regulations as part of the mandate for the Office of Industry Analysis. The existence of the office, its role in the economic analysis of major rules and how agencies should treat the analysis should be codified. As with making parts of E.O. 12866 statutory, the NAM encourages the subcommittee to begin working with the Administration on how best to achieve this recommendation.

6. Information Quality Act Actions Should Be Judicially Reviewable. The Information Quality Act (also known as the Data Quality Act) required OMB to issue government-wide standards for the dissemination of information, and then required agencies to issue their own guidelines tailored to their specific missions. The public can use the guidelines to petition for information disseminated by an agency to be revised or deleted. A recent ruling by the U.S. District Court for the Eastern District of Virginia stated that agency decisions on such petitions are not judicially

reviewable. I am not certain that a legislative fix is necessary at this point because there may be other courts (particularly the D.C. Circuit) that may weigh in with a different finding. This issue is, nevertheless, one that the subcommittee should be aware of.

7. **Sunsetting Regulations. Major regulations, at least, should be sunset after 10 or 15 years and only extended if they have demonstrated their usefulness and success. Such a review would force agencies to determine how well regulations have met their goals and to see if there are any ways to improve how they work. Those regulations that are effective, of course, could and should be allowed to continue in force.**

8. **Reducing the Cost of International Regulatory Differences. Differences in U.S. and foreign regulatory policies and standards have become a serious trade concern for manufacturers, raising costs of market entry and preventing small and mid-size companies from exporting to foreign markets.**

   The problem is getting worse, particularly in Europe where regulatory policies are diverging widely from those in the U.S. The Administration needs to launch a major new initiative to improve international regulatory cooperation and move toward international harmonization of regulatory policies while maintaining high standards in the United States.

We believe this can be done. OIRA Administrator John Graham has spoken on this issue and expressed his concern but there is not enough concrete action.

In particular, U.S. regulatory agencies need a clearer mandate and additional resources to assess the trade impact of regulatory differences and work with their foreign counterparts to address them. It is interesting that at a time when our competitors in Europe are harmonizing their regulatory systems to eliminate conflicts, we are allowing the 50 U.S. states to move in the other direction.

***A*lthough the NAM is encouraged by the increased awareness and interest in international regulatory issues, it is time for the Administration and Congress to provide more direction and support to regulatory agencies.**

Conclusion

The vast majority of manufacturers are determined to be good corporate citizens and comply with all of the regulatory requirements that affect their companies. In order to do so, they need to understand both the need for the regulation and why certain requirements exist. They also need paperwork to be as simple as possible so that their time can be spent on more productive activities.

As one manufacturer once put it in testifying on behalf of the NAM, his children swim and kayak in the river that his factory sits beside, they play in a nearby playground, and if one of his workers got injured he would have to face that worker—or, worse, the worker's surviving spouse or children—at various locations around town. Thus, to the extent that EPA, OSHA or other agencies can help him ensure that his emissions are not threatening and that his workplace is safe, he is readily willing to incorporate those suggestions and requirements. But to the extent that they come attached with a needless amount of paperwork or production procedures that either do not work or are unnecessarily inefficient, then his ability to make a profit—and thereby provide jobs and other benefits—is compromised.

Chairman Miller, the NAM looks forward to working with you and the other members of this subcommittee to find ways to improve regulations affecting manufacturing. I would be pleased to answer any questions that you or the subcommittee may have.

Mrs. MILLER. Thank you for your insight and thoughtfulness on this very important subject, and I might start the questioning here if I might.

Governor, I thought it was interesting, you used a boat manufacturing analogy. The Federal Government has been after boat manufacturing for some reason when they passed the luxury tax in the late 1980's, ostensibly to get at the rich. They almost put the entire American boat manufacturers out of business because, of course, those that could afford a luxury boat went to a different country and purchased one and documented it somewhere else and brought it here. So it is not surprising that they continue on that. And that's an excellent suggestion that you have made or brought to light there.

Also in your written testimony, Governor, you suggested that the role of the Department of Commerce and regulatory review would be made in statute; actually, that it be made statutory. I'm just wondering, if the mechanics of the process, particularly of small manufacturers as to how they deal with the Federal regulatory agencies, can be made a little bit more customer-friendly or oriented? Do you have any ideas on that?

Mr. ENGLER. I think with Dr. Graham and Secretary Frink, we have two leaders—I know Dr. Graham has been terrific. I think the Commerce Department effort pursuant to the legislation passed after the Department came out with a report about manufacturing in America is designed to help get at that question you're asking, and Secretary Gutierrez and Secretary Frink are making it clear. This is something they want to do. It is going to be a bit of a listing post, and we are excited about being able to talk to commerce, have commerce actually working with us to go to OIRA or go to Dr. Graham.

But I think where it gets hard after that is to get the agencies tagged, and that is where it comes back to the Congress, because so often in the bureaucracy, it is a sense we can wait it out; this, too, shall pass. And in the case of the boat regulation, it has been since 1969 that OSHA has been asked to deal with that. They are going ahead, but why do we have them at risk, and why do we have obsolete rules? I have seen this in air quality with EPA, where in the competition for a manufacturing plant expansion, one region of the country this year went through this where a region in one part where the costs were lower, the rate of ionization was lesser. They also found themselves with a more favorable air quality decision out of the Federal region than was the case back up in Michigan where I happened to be Governor at the time. And we said look, it's a Federal law. Which region is controlling this decision? And today, that's often a problem, too. And when it means dislocation of jobs or General Motors moves from Massachusetts to someplace else, because the northeast's interpretation is different than the southeast's interpretation, that's unfair as well.

Mrs. MILLER. It's true. We do see States sort of cannibalizing one another, and the Federal Government sort of a handmaiden to all of that, probably with the best intentions, but that is the reality of the impact of that.

Dr. Graham, I thought it was interesting that it was counterintuitive to you for some of the regulators to ever really go

back and look at what they have on their hands there in the practical application of some of these things. You said it might go against the very nature. But how can Congress incentivize some of these different regulators to have an annual review process? You mentioned the 76 different priority reforms, which do not require legislation. They are in the rule promulgation stages, I suppose. What can we do to incentivize these different agencies to have an annual review to see whether or not the cost-benefit analysis makes sense, if it's rational or reasonable?

Mr. GRAHAM. The fact that you are chairing this hearing and having this hearing today on this topic and you are expressing interest in the administration's initiative on these 76 manufacturing regulations, that is a very significant boost to myself and the two dozen staff members at OIRA who are working on a day-to-day basis to make sure the agencies make progress in these areas. I want to start with the most basic answer to you, which is, thank you for expressing interest in having this hearing.

Looking down the road in terms of how you can further contribute to this, we have worked out with agencies, some would say negotiated with agencies, deadlines that are in that list of 76 for when they would take specified actions. I encourage you and your staff to track those, to see if we continue to make progress on those and to make it clear that members of this subcommittee care about whether these deadlines are met and provide explanations if some of these are not being met. These are very practical but very real things that need to happen. And we need your assistance to make sure we are making progress.

Mrs. MILLER. A final question for Mr. Frink. You mentioned that you had already visited or had contact with 13,000 different manufacturers and a common element theme that you found in your discussions was a need to reform from all these different manufacturers. Was there a common problem? Was there one or two things you really found that the manufacturers kept coming back to that just leaped off the page at you, a regulation that they found onerous and burdensome?

Mr. FRINK. Sarbanes-Oxley, Sarbanes-Oxley, Sarbanes-Oxley. That was the most resounding plea for assistance from all levels of manufacturing, large, medium and small. It is especially impacting the smaller companies that don't have the resources to comply with the requirements of Sarbanes. Everybody agrees that the legislation/regulation has positive aspects to it. There are just some attachments to it that have created a burden that makes it probably almost so significant. And I think around tax time, it has been especially resounding that it has dwarfed any other regulatory issues in my recent visits in the last 3 months. So I would have to say that one is clearly at the top of the concern level. I think, beyond Sarbanes, I didn't get specifics that I could share, just a general concern that regulations, in many cases, as they vary within the sectors, have tremendous impact on their ability to remain competitive per what Governor Engler mentioned with regard to the varying costs of doing business in this country and that they look at that as one of their main areas of costs that they would like assistance on in terms of reform.

Mrs. MILLER. Thank you. I turn the floor over to the ranking member, Representative Lynch.

Mr. LYNCH. Thank you, Madam Chairwoman.

I want to thank you for appearing before the committee.

Dr. Graham, I actually had sent a letter over to you and I'm hearing now that you are short on staff and that may be the reason for it. I know that Ranking Member Waxman and I sent a letter over requesting information regarding the whole process that you have embarked upon in terms of all these folks that you have met with the idea of engaging in regulatory reform, and this committee is going to be handling a lot of that based on what Chairman Davis has said.

And we are a bit concerned if we're going to get a picture, a snapshot of what's going on. We want to make sure that group is as wide as possible and reflects, not just one viewpoint, but might be reflective of a broader spectrum so that, I mean, let's face it, the work of this committee is sometimes, well, all the time affected by the information we get. We want it to be accurate. We want it to be representative of the entire spectrum of people who are affected out there. And I guess what I would like to know is, how are we doing with the responses to that letter that I did send you?

Mr. GRAHAM. We have received the letter. This is the March 24 letter? We are working on it. And we had hoped to get you a response before the hearing and didn't quite make it. We are still working on it, and just to give people in the room a sense of why we might not have it yet, let me read item four from the letter: Please provide all documents, including e-mails, exchanges between on OIRA staff and any non-Federal employee since January 1, 2003, related to the regulatory process. Obviously, this has taken us awhile to figure out exactly how we are supposed to deal with it.

Mr. LYNCH. It would have been nice if you said, we got your letter and call us up and say, we are having a problem with one of your inquiries. We got silence. I thought maybe it got lost in the mail.

Mr. GRAHAM. We tried to call you Friday, but we are working on it. But I want people to get a feel of the kind of thing we are talking about here.

Mr. LYNCH. You can look at the other questions, too, if we are going to go over that. We would like to know basically the groups you met with this is an initiative to change the regulatory process. And we understand that the administration is very committed to this, and we would like to make sure that it's a forthright process, and there is full disclosure and everyone gets to offer their concerns and comments regarding this process, and it shouldn't be just slanted to one group, as important as that group might be.

Mr. GRAHAM. You raise an excellent point. Just to keep in mind, the process on the manufacturing initiative, this was a public nomination process where any group could submit comments if they wanted to, and all the comments we have received are posted on the OMB Web site. And our policy at OMB is to have an open door policy for visitors from any of the groups, including labor groups, public interest groups, environmental groups. They certainly have an opportunity to participate. And let me assure you, they do.

Mr. LYNCH. In this round of solicitation and comment, 97 percent of the responses have been from manufacturers and 3 percent have been from everyone else.

Mr. GRAHAM. Given who is incurring the burdens of these regulations, you would expect the business community to be the dominant participants. Let me assure you on your interest that you mentioned in your opening statement on the development of new regulations to protect public health, safety and the environment, we do meet with frequency the groups you are talking about on their ideas for new regulations. And they are very aggressive and persuasive in making their case.

Mr. LYNCH. We will be getting that information. And we can talk about the feasibility of getting the information there. We can talk about what we are looking for. Obviously, staff was, I think, trying to cover everything that we might possibly need in response to those efforts. Let me ask as well, the information that we get here, we would like it to be as accurate as possible. And I know a lot of folks come before this committee and others citing certain studies and some reports that say—I've heard various estimates already here of costs of regulation. And I'm one of those folks that likes to look at the underlying documents that generate that number, because in a lot of cases, what I've found, these are guesses. These are largely guesses, and a lot of them are based upon information that was just like some of these regulations, actually, that were gleaned back in the 1960's. I know that the Crane and Hopkins study actually uses data that was gathered back from the 1960's at the same time these regulations came in. So when people offer that information and there is a certain amount of inaccuracy in it, it's just difficult for us to make the quality of our response as accurate as we would like it, because we are working with very, very dated information and, also, some information that is unsound in terms of the process that goes through to reach the conclusion that the report cites.

So I'm sure you are going to be a frequent flyer to this committee; I get the sense. And I want you to know, we are going to look at the underlying studies and reports and the whole analysis to make sure we're basing our collective decisions on accurate information.

And last, if I could—and I don't want to take too much time here—but I was a little surprised that last year, 2004, the administration actually listed some of its accomplishments, one being the listeria rule, which it cited as being one of its accomplishments, albeit a very modest rule, a very weak rule in a lot of peoples' estimates, regarding one of the most poisonous compounds that are out there. I mean, 20 percent of those infected with listeria, based on some studies, those are fatal. And there is tremendous danger in listeria contained in ready-to-eat meat products and poultry that they are extremely dangerous to pregnant women and their unborn children. So I was a little surprised to see it on the hit list. Last year, it was on the accomplishments list, and now it is on the hit list with an attempt to weaken it even further. And I was a little puzzled by that.

Mr. GRAHAM. You can be assured, sir, that we are not talking about eliminating this regulation. The suggestion is ways to reduce

the compliance costs of the regulation without reducing the protection to the consumer in terms of food safety. If you read the comments from the affected industry that indicated that the compliance costs have proven to be much more substantial than was projected before the regulation was adopted.

Mr. LYNCH. Let me get this right. Last year, it was an accomplishment?

Mr. GRAHAM. The regulation as a whole was an accomplishment, but there are ways in which you can refine and fine tune the regulation to achieve the same level of protection for the consumer but at lower costs to the industry.

Mr. LYNCH. I yield back.

Mrs. MILLER. Thank you.

The Chair recognizes the vice chair, Representative Brown-Waite, for her questions.

Ms. BROWN-WAITE. Thank you very much. My first question is for Governor Engler. Obviously, in order to reduce the regulatory burden on businesses, we have to get rid of some old inefficient rules and maybe some rules that bureaucrats sort of snuck in there. I think that was the case when we did the regulatory reform in Florida. I believe that Michigan has something very similar to what I described before as a Joint Administrative Procedures Committee. And if you could briefly describe that and the success or lack of success. But I heard it was very successful. If you could just share that with the committee, I would appreciate it.

Mr. ENGLER. During my tenure as Governor, Congresswoman, we established an Office of Regulatory Reform. And part of the challenge we had was that agencies, in some cases, refused to promulgate rules that they were required to promulgate. And so when the legislature would have fixed the statute, that wasn't followed through in other cases. As has been described here, sometimes it's easier to do something new rather than go back and clean up what is. We required that a central point exists where all agencies had to bring the rules in and you could harmonize them to make sure that they were internally consistent; that a new rule being promulgated in one agency wasn't in conflict with an existing rule over in another agency or in conflict with a pre-existing rule of the same agency.

At the same time, we said, if you are promulgating a rule in maybe a health standard, if you're in an area of the administrative code, then while you're there, clean up the obsolete references, the old language. The net of this was to reduce by more than a third the administrative code of the State of Michigan, while I think strengthening compliance and reducing compliance costs. All in all, it proved to be a very effective way to get at this problem. We didn't always have the ability to—if there were pre-existing problems to faithfully implement the statute, we would say to the legislature, you know, that cannot be changed by the agency, you have to go back and change the underlying statute. And so there is a mixture of these, and that is why the work of the committee is so important because there is this delineation and the classification of what are we dealing with, because they are going to differ from agency to agency and department to department.

The one thing that I would add, it is sort of the environment that we are in, because this was out of today's paper—and it's a challenge for the committee that goes right to your mission—a little article, Business Looks to the Panel's New Leader for Relief, entitled, The Regulators. The Chair of the committee suggests that the problem is cost regulation where some rules have outlived their usefulness and cost-effectiveness.

The Chair of the committee suggests the problem is with cost regulation where some rules outlived their usefulness, cost-effectiveness. "My approach is the largest room is the room for improvement, particularly when it comes to regulation."

In the same article, something described as a public interest community, which I think I am part of the public interest community because we want to put good manufacturing products out there.

The public interest community views the Miller regulatory agenda as extreme. Now, I don't think it's extreme to say room for improvement, but that's the environment—and cautions it's mobilizing to fight business-backed initiatives that would limit health and safety regulations or create procedural roadblocks to regulations like sunset reviews. Now, sunset review, if I understand that right, that terminates something—it isn't a roadblock to enacting it. It merely says we ought to take a look at it.

Ms. BROWN-WAITE. Right.

Mr. ENGLER. But that's how dug in—and so when Dr. Graham puts out a call and comes in for 97 percent of the manufacturers, that is because the status quo has 97 percent of the rules in place, and they are happy with this bureaucracy, but they are not trying to make a profit in today's world. So what you are doing is real important.

Ms. BROWN-WAITE. Well, certainly the chairwoman and I come from the States that, you know, took this issue on, and I think it's our goal to make sure that the Federal Government does that also; that we look at overlapping and duplicative regulations that do nothing for public safety, that do nothing for the good of the business community or even the environment, but rather are just duplicative and outdated. I appreciate your response. Hopefully we can accomplish the same thing at the Federal level.

I wanted to just ask Mr. Frink one question, and that was on Sarbanes-Oxley. I serve in the Financial Services Committee, and I, too, have heard from small businesses about their audit that's necessary for compliance with Sarbanes-Oxley. I was wondering if you had come up with some suggestions to make it a little easier for small businesses so that the accountants and auditors don't overcomply and, therefore, drive up the cost. That's what I am hearing from small businesses.

Mr. FRINK. Congresswoman, I think that's a good question, and it's the same question that I have posed to people that have brought that concern to me. I felt they were in the best position to be able to provide advice. I also recommended that they put together a legitimate case to quantify what their actual costs are so that we could bring back legitimate information that would substantiate what everybody is saying. Because I think that, speaking to Congressman Lynch, is concern for quantification, accuracy of

quantification. I wanted to have that kind of information available so that I could come back and then present it in a manner that would have some teeth.

So what I would like to do is to allow me to pursue that information gathering and report to you subsequent to this hearing with what I think you are asking for.

Ms. BROWN-WAITE. May I followup? Did you give the small businesses a timeframe to get back to you with these suggestions? Because one of the things that I found is that in Congress the "we will get back to you" becomes years. Not only—this is only my 3rd year here.

Mr. FRINK. You know, in the spirit of the meetings I had, there was a sense of urgency. But, you know, to answer your question honestly, no. But I will do that subsequent to this meeting. I think it's—I have experienced the same thing. So I will get back to those individuals and tell them, look, I think we have a chance to really try to get some value to addressing of your concern, I need it by this time.

Ms. BROWN-WAITE. Thank you, Madam Chairwoman. I yield back the balance of my time.

Mrs. MILLER. The Chair recognizes Representative Westmoreland for questions.

Mr. WESTMORELAND. Thank you, Madam Chairwoman.

Governor Engler, let me thank you for bringing recommendations to this committee for things that we can do right now to help with our manufacturing, and I want to thank you for doing that.

Dr. Graham, in your testimony you said that since 1981, there have been 115,996 final rules published in the Federal Register by Federal agencies. It says that the office looked at a little over 19,000 of those.

When government agencies—and I apologize for my ignorance—but when government agencies do new rules and regulations, what process do they go through before they actually go into the Federal Register?

Mr. GRAHAM. Yes, sir. An agency typically will draft a regulation, submit it to OMB and other interested agencies for review. Then once there is a decision made to go forward with that proposal, there is then a period of public comment.

Mr. WESTMORELAND. Who makes the decision to go forward? Do you have any authority to stop any regulation put forth by an agency?

Mr. GRAHAM. Well, as you know, the executive branch is all one big family, and we work together on these issues, but we do have authority in the Presidential Executive order to ask an agency to reconsider a proposal.

Mr. WESTMORELAND. But do you have the ability.

Mr. GRAHAM. That's the authority that I have through Executive order.

Mr. WESTMORELAND. Just to ask them to review it.

Mr. GRAHAM. To reconsider.

Mr. WESTMORELAND. To reconsider it.

Mr. GRAHAM. Yes.

Mr. WESTMORELAND. If they choose not to reconsider it, then they can do it regardless of what you say.

Mr. GRAHAM. Well, if they disagree with Dr. Graham, then they can appeal that decision to my boss Mr. Bolten, the OMB Director. And as the Executive order indicates, if there is still a disagreement, that can go the Chief of Staff, to the Vice President or to the President himself. But everyone in the executive branch is working for the President, and in the final analysis, all resolutions, if necessary, go to the President.

Mr. WESTMORELAND. But they—but the only thing you can do is ask them to reconsider it. Who is the person that can tell them, no, you are not going to implement that rule?

Mr. GRAHAM. Well, I can be, as a starting point, by asking them to think about it some more. But if they feel strongly about it, and they want to continue to push it, they can appeal that and elevate that decision above my level into the White House.

Mr. WESTMORELAND. OK. I don't know if I don't understand what you are saying or if you don't understand what I am saying.

Mr. GRAHAM. In the final analysis it will still be the President's decision, the final say.

Mr. WESTMORELAND. OK. So he says, yes, you can, or, no, you can't. If you ask him to reconsider it—and that is basically you are telling them, please don't do this.

Mr. GRAHAM. I am the person representing the President on regulatory matters.

Mr. WESTMORELAND. OK.

Mr. GRAHAM. If they don't want to deal with Dr. Graham, then they need to get their Cabinet officer, whatever, to call the President or the Vice President or Andy Card and work it out.

Mr. WESTMORELAND. So, of these that were put on the final registry at some point in time, the President had to say, this is OK.

Mr. GRAHAM. We, as OMB, and the Executive Office of the President cleared over 20,000 of those regulations.

Mr. WESTMORELAND. OK. That had a cost of a little over—or a potential cost of a little over $100 million a year.

Mr. GRAHAM. 1,100 of them——

Mr. WESTMORELAND. Right.

Mr. GRAHAM [continuing]. Had estimated costs of over $100 million a year.

Mr. WESTMORELAND. Do you know what the cost of the other 18,000 or so were, or were they just——

Mr. GRAHAM. Fabulous question. I don't think anybody, frankly, really knows the answer, because the way the Executive order is designed is it focuses the cost estimates on the most expensive of the regulations. But there are a large number of less expensive regulations that aren't analyzed as seriously, so the cumulative burden of those other regulations is, of course, an unknown.

Mr. WESTMORELAND. Mr. Frink, one question for you. On page 3 of what I have in your testimony, it says you talk about the manufacturers' report. With 18 specific recommendations completed in less than 1 year, the Department of Commerce will continue making progress on these recommendations and other efforts to ensure the competitiveness of all U.S. manufacturing businesses.

Of the 18 specific recommendations that have been completed in less than a year, what were the total number of recommendations—maybe I have missed it somewhere—in here?

Mr. FRINK. The total are 57 initiatives from the book of Manufacturing America, of which, when I came on board in September, I believe there was about seven to eight of those accomplished. So in the last 6 months there's been an additional 10, making 18, and we have another 4 close to completion, another 17 that are further out.

Mr. WESTMORELAND. Are these recommendations doing away with some of the regulations that is only manufacturing, or regulations—I mean, what are these recommendations?

Mr. FRINK. Well, none of them would be the Office of Industry Analysis. That is a newly formed industry or sector within our department. That individual is a new DAS, and as a new DAS for Industry Analysis is going to be working very close with OMB and SBA on their regulatory process to help assist with the information gathering, the evaluation, hopefully the impact of regulations. So I think in that regard, some of our best work is ahead of us.

So that signal area is probably the one that is most focused on getting results in achieving reform with regard to the regulatory process.

Mr. WESTMORELAND. But really nothing has changed as far as the regulations on manufacturing. We have just—you have come up with some ideas about how to judge what those regulations really do, because I think we already know what they do.

Mr. FRINK. Correct.

Mr. WESTMORELAND. I mean, I know that this other agency is probably helpful, but the last thing I think we need in government is another agency.

Mr. FRINK. Well, actually I think that in this case we do. The need for focus on regulations has not, to my knowledge, been in place specific to manufacturing. And we have needed a sector in the manufacturing focus that is clearly looking at the regulatory process, and not just looking at the results, but perhaps analyzing the process to see how we can affect regulations, even perhaps before they become official.

So to have that focus, I don't know of any other agency or service within government that was doing that besides OMB. So we are adding our efforts to theirs and that of SBA. It's such a daunting task, I think it needs as much attention as can be given to it.

Mr. GRAHAM. Yes, sir.

Just a quick condition, if I may, on that question.

Mr. WESTMORELAND. Yes.

Mr. GRAHAM. Keep in mind that at large regulatory agencies, like Department of Transportation, the Labor Department, the Environmental Protection Agency, they have hundreds, sometimes even thousands, of people who are available to work on regulatory proposals. We at OMB have two dozen for the entire Federal Government. The prospect of an analytic unit at the Commerce Department that would have a couple dozen additional analysts working on these regulations, that makes people in OMB very optimistic about the prospects for further progress.

Mr. WESTMORELAND. Good. Do you think there's a possibility that we could get a list of those 57 recommendations and the ones that's been checked off and how many more are to go?

Mr. FRINK. It would be my pleasure. I will make sure you get followup information on that.

Mr. WESTMORELAND. Thank you, sir.

Mrs. MILLER. In the interest of time, I will forego the second round of questions, but I would like to recognize the ranking member, Representative Lynch.

Mr. LYNCH. Thank you, Madam Chairwoman.

Mr. Graham, if I could just come back with you a little bit. In your statement, at least initially, from what I heard today was that there is an attempt to draw a direct link between the recession and job losses and the existence of certain regulations. I am really concerned that what OMB has done here is create a hit list somewhat of environmental health and safety protections that industry would like to see weakened or eliminated.

Now, what I don't understand is how OMB is making the connection between job losses that we have seen in the last 4 years and the list of regulations that OMB is now supporting for reform. For example, though we started seeing major job losses in 2001, many of the regulations that I see on OMB's hit list have been around for much, much, much longer than that, and actually during periods of high job growth for that matter. For example, the toxic release inventory and cleanup requirements for PCBs, a very dangerous substance in our—especially in industrial sites, and Title 5 of the Clean Air Act around permitting, they have all been around for many, many years, and yet these important environmental protections are all targeted on OMB's hit list.

It just seems to me, now I have grappled with this for some time, the job loss issue, and it seems to me—I mean, I visited China, Shanghai, not long ago and talked to some manufacturing workers in the Otis Elevator plant there in Shanghai. I asked the technician there what he was making, what he was earning, and he told me he gets paid about $25 a month. And I know that my elevator constructors and the folks in that industry are probably paid $25 an hour, at least.

I mean, let's just set aside for the moment the fact that the Chinese worker has no freedom of expression, can't own a home, has no solid health care, has no freedom of religion or expression, or the right to join a union. Let's set that aside for a moment. But given the economic reality, the labor costs, the difference between one worker making $25 a month, our workers making $25 an hour, shouldn't we be looking at our trade policies and labor policies and the incentives that some companies are given right here today in the United States to locate jobs overseas to take advantage of that much, much cheaper labor market?

Mr. GRAHAM. I agree that it requires a broad-based examination, not just regulation, but liability reform; certainly we need to look at trade policy, and we are doing that. There are a range of issues that need to be looked at. But let's not deflect from the importance of just the regulatory burden on the long-term competitiveness of American businesses in the world economy. It may not solve the next recession, but it helps them compete in the global economy when they don't have unnecessary cost burdens imposed on them.

Mr. LYNCH. OK. Thank you.

The other thing, I just wanted to go back to that Listeria. I was reading my notes on the way in on the plane that actually OMB's recommendation was to rescind the rule, was because it was OMB's position that the benefits of the Listeria rule were overstated. So it wasn't just—wasn't just around costs, but that the benefits of this rule were overstated. That's in your own report here.

Mr. GRAHAM. Yes, page 66 of the report, the summary. There is a summary of what the commenter suggested. There is not an OMB recommendation.

Mr. LYNCH. OK. All right. So you don't think it's——

Mr. GRAHAM. And what the commenter has said is that—both that the costs are more costly than USDA estimated, that's line 3; and you are correct, they also say that the benefits were overestimated.

Mr. LYNCH. Right. The benefits——

Mr. GRAHAM. So you are actually making both arguments.

Mr. LYNCH. Yes. So you don't believe——

Mr. GRAHAM. The USDA is now in the process of reexamining those in light of the comments made on the interim final rule.

Mr. LYNCH. OK. But is that your, OMB's, position——

Mr. GRAHAM. No. In fact, I think I was clarifying for you is that language on page 66 is the language of the commenter, not the language of OMB.

Mr. LYNCH. OK. I want to be certain.

Mr. Frink, Graham and Engler, I want to thank you both as well. Although I haven't really bothered you as much as well, I want you to know I really do appreciate your working on this issue, and we will have to grapple if we are going to solidify, stabilize the manufacturing industry in this country, and I appreciate all of your work on that effort.

Thank you. I yield back.

Mrs. MILLER. Thank you very much. I certainly sincerely as well thank all of our witnesses, our panelists, for being here today. It's been very interesting for us.

This is a committee that does look to improvement, certainly. I don't think that's a radical agenda. In fact, something that might be a radical example of Federal Government regulations, this morning we are talking about manufacturing, and sometimes we think of heavy industry or what have you in manufacturing. But other things are being manufactured, like bread. And it's interesting, talking to the American Bakers Association, that the Federal Government has regulated breadmaking to the extent that they think that the smell of fresh-baked bread is smell pollution, and it has to be regulated out of existence. So you can't have that fresh smell any more.

But I think that might be a little extreme agenda, but we do, as I say, want to continue to examine or explore, do what is right for all of the workers of America, and our environment as well. I certainly think that we can do so working together.

Governor Engler, do you have a final comment, sir?

Mr. ENGLER. One last thing, Madam Chairwoman, to submit for the record that addresses something that Ranking Member Lynch mentioned earlier in terms of the freshness of studies. This is a 2003 study. A reference has been made to it in your comments and

some of my testimony, about how structural costs imposed on U.S. workers can harm workers' competitiveness. A lot of the source documents are in here with the graphs and the attributions so that you can go right to the source and go through that to seek verification of the data. And it's a wonderful study and quite authoritative, I think, that gets to the work of the committee.

Thank you for your time.

Mrs. MILLER. Thank you all very much. At this point we will just take a few minutes recess for this panel to take their spots. Thank you again.

[Recess.]

Mrs. MILLER. I will call the meeting back to order here. I am interested to hear from our next panel of witnesses. Again, it is the committee's desire that we swear you all in. So if you could all raise your right hands, please.

[Witnesses sworn.]

Mrs. MILLER. Thank you very much. We appreciate that.

Our next witness the subcommittee will now hear from is Dr. Thomas Duesterberg. Dr. Duesterberg is president and CEO of the Manufacturers Alliance. The alliance has more than 425 corporate members engaged in manufacturing and business services, and conducts economic and policy research relevant to its membership.

Doctor.

STATEMENTS OF THOMAS DUESTERBERG, PRESIDENT AND CEO, MANUFACTURERS ALLIANCE/MAPI; LORI LUCHAK, VICE PRESIDENT AND MARKETING DIRECTOR, MILES FIBERGLASS & COMPOSITES, ON BEHALF OF THE AMERICAN COMPOSITES MANUFACTURERS ASSOCIATION; AND SIDNEY SHAPIRO, UNIVERSITY DISTINGUISHED CHAIR IN LAW, WAKE FOREST UNIVERSITY, ON BEHALF OF CENTER FOR PROGRESSIVE REGULATION

STATEMENT OF THOMAS DUESTERBERG

Mr. DUESTERBERG. Madam Chairwoman, thank you for having me here today. I want to commend you and Mr. Lynch for holding this hearing on regulation on U.S. manufacturing.

As you mentioned, I represent the Manufacturers Alliance, which is a 501(c)(6) organization devoted to economic research and executive development.

My remarks draw on a number of our studies issued in the last few years, and I want to try to do something a little bit different today, which is to do basically two things: To put into context the competitive situation of the manufacturers, especially with regard to the international competition and the cost pressures that affect manufacturers, and to address a few of the larger issues of regulation, which sometimes are forgotten in the effort to deal with these 100-and-some thousand regulations that Mr. Graham mentioned earlier this morning.

I have a few charts and graphs that I will—your staff is going to help me with as I go through this. But what I wanted to do today is first call attention to a gradual decline in the performance of the manufacturing industry, starting somewhere in the late 1990's.

First, we note that, if we could put the first chart up, there had been a certain consistency in plant openings and closings in the manufacturing sector dating back about 40 years, and our research, drawing on the Commerce Department, indicates that there was a break in this.

This is the—can't see it very well, but the bottom line, bottom two lines, show that the number of plant closings has remained steady over time, but the number of plant openings started to trend downward in the late 1990's. About 10,000 plants each year that would have been opened were not opened. If you look at hiring and firing in the manufacturing industry, that trend is the same. So there's been a trend downward in the annual spurts of entrepreneurship, if you will, affecting all manufacturing.

Second, and if we could go to the second slide, this is also reflected in the profit margin, this is—especially of durable goods manufacturers. Again, these profits have been highly cyclical, but durable goods tended to run a little bit less than the nondurable goods manufacturers for a number of years. But in the late 1990's and in this decade, they have trended downward again and have not recovered to the extent they should have at this point in the recovery.

The third thing I would mention is that everyone is familiar with the trade numbers—and again, we had numbers come out again this morning—which were the worst trade deficits in U.S. history. And it affects especially the goods-producing sector, whether—it's between $600 billion and $700 billion in deficit each year.

Again, if we could go to the next slide, this shows the percent of domestic output that goes to exports, which is the bolder blue, and the lighter blue is the percent represented by imports, and the import number keeps going up and up. It is now 35 percent of domestic consumption, pardon me, and as our exports have trended downward since about 1997.

So how to explain this. The growth in international competition is certainly a major explanation of this, but the role of cost pressures, which Governor Engler mentioned, which Madam Chairwoman mentioned in your opening statement, also is important.

And if we could go to my final chart, which is really a summary of our costs study, which we did a couple of years ago, it indicates that if you take unit labor costs, which are adjusted for productivity, compare it with our nine leading trading partners, everyone from the advanced countries like Germany and France to China and Mexico, there's about a $5-an-hour wage differential. And, again, this is corrected for productivity and for capital inputs.

U.S. productivity has been so good that over the last 12 years unit labor costs have actually declined in the United States, but nonetheless, we have been unable to keep pace. Part of reason for this we think is the structurally imposed costs.

We were able to calculate on a comparative basis corporate taxes, employee benefits, tort, natural gas costs and pollution abatement costs. When all of these are averaged out for our nine leading trading partners, it shows that this subtracts about $3 an hour from their costs. And so this averages out to a 22 percent increase in the cost of domestic production.

I focused them on four separate areas of regulation which I think merit the attention of this committee. Energy, especially natural gas, where, for the last decade or so, we have encouraged consumption and discouraged production. We believe that easing up on the ability to import LNG is a near-term solution to this problem which has affected especially the chemicals and fertilizer industry. We have lost 100,000 jobs in the chemicals industry, partly as a result of our higher prices.

I focus on the telecom industry, where even though we have—the language of deregulation has been used, we have—the regulatory bar in Washington, DC, has grown by 73 percent since the deregulation bill. Again, the industry has declined by a third in terms of employment because of—partly because of overregulation. They think we need to pay attention to that.

The third thing I have mentioned in the testimony is the costs of Sarbanes-Oxley. We have done a number of studies of our membership, the most recent of which was a survey of CFOs of our member companies. We found that the costs, all end costs of Sarbanes-Oxley Section 404 compliance, total almost 6 percent of net income before taxes. And this excludes companies that are not making money, so it's probably an understatement. We think that is probably an example where we can do better in terms of our regulation, and we offer a number of constructive suggestions for improving the way Sarbanes-Oxley is implemented.

Finally, I wanted to call attention to the new phenomenon of regulation through litigation. The practice involves the employment of private trial lawyers by State and local governments who conduct a coordinated litigation effort against an entire industry purportedly for the purpose of attacking serious public health and safety problems.

We think that regulation should be accomplished, as our Constitution indicates, by the Congress of the United States or by State legislatures, not by the judicial branch. This problem could rise to more importance as the targets of the litigation go from politically disadvantaged industries like tobacco and firearms to the auto industry, the pharmaceutical industry and the food industry.

So all in all, Madam Chairwoman, we think that we need to pay attention to the regulatory costs in this increasingly competitive global environment, because it impairs the ability of American firms to compete against the Chinas, the Indias and even the Mexicos and Canadas of this world.

Mrs. MILLER. Thank you very much.

[The prepared statement of Mr. Duesterberg follows:]

Testimony of

Thomas J. Duesterberg
President and Chief Executive Officer
Manufacturers Alliance/MAPI Inc.

on

"The Impact of Regulation on U.S. Manufacturing"

Before the

Subcommittee on Regulatory Affairs
Committee on Government Reform
U.S. House of Representatives

April 12, 2005

Madam Chairman and Members of the Subcommittee. My name is Tom Duesterberg, and I am here in my capacity as President and Chief Executive Officer of the Manufacturers Alliance/MAPI, a membership organization representing some 450 firms predominantly from the manufacturing sector. The Alliance is the leading executive development and economic research organization serving the manufacturing sector. Our activities range from management and policy research to economic forecasting and to the operation of some 30 executive councils and conferences for senior executives in nearly every major management discipline. My remarks today draw on a number of our studies and books issued in the last few years examining the competitive pressures on U.S. manufacturing firms in an increasingly globalized economy, and on direct feedback from the 2,000 senior executives who participate in our programs.

Introduction: The State of U.S. Manufacturing in 2005

It is widely recognized that the manufacturing sector is exposed to competition from around the world and that the scope and quality of this competition is constantly growing. The manufacturing sector is nearly four times more exposed to international competition than the much larger services sector.[1] Despite the hugely successful efforts of manufacturers to respond by improving productivity and accelerating the pace of their quality improvements and product innovation, international competition from developing countries, led initially by the four tigers of East Asia, later by Mexico and Brazil, and now by the emerging economic superpowers of China and India, has taken a toll on the ability of firms to survive and prosper. The headline numbers of a loss of 2.9 million manufacturing jobs since the dawn of the new millennium, and the growth of a trade deficit that now stands between $600 billion and $700 billion on an annual basis, are testimony to the difficult competitive landscape. The steady growth of global manufacturing capacity, and the willingness of global competitors to put market share before profits, puts a lid on any price increase by domestic

[1] This is calculated on the basis of the sum exports and imports in both goods and services as a proportion of total GDP in the United States. If only imports are included, the manufacturing sector would be some 10 times more exposed.

firms even when their input costs increase. Many nations, especially our main East Asian competitors, also keep the value of their currencies artificially low. In this environment, manufacturers are especially sensitive to their cost structures in relation to their global competitors, and any costs imposed by, or related to, regulation become a factor in their ability to survive.

Before exploring the impact of regulatory costs in greater detail, a bit of historical perspective is in order. After the Second World War, U.S. manufacturing was globally dominant and grew steadily along with the world economy. In the 1960s and 1970s, Western Europe and Japan resumed their pre-war position as capable competitors to U.S. industry. To this landscape was added, gradually over time, new manufacturing powers in East Asia and parts of Latin America. With the cost problems and inflation associated with the oil crisis of 1973 through 1981 added to the strong challenge from Japan and the four tigers, many in the United States began to fear the "hollowing out" of domestic industry. Particularly hard hit were traditional manufacturing symbols such as steel and autos. But U.S. industry, aided by sound monetary policy and the low-tax, deregulatory environment of the 1980s, responded successfully. In the 1990s, the creative genius of American innovators and entrepreneurs was unleashed by technological innovation, a stable domestic policy environment, and strong global growth. With the flowering of new industries like information technology, communications, and biotechnology, manufacturing grew much faster than the overall economy and was indeed its principal engine for growth.[2]

The first half of the 21st Century, however, has witnessed the evolution of a much more difficult competitive landscape. The double-dip manufacturing recession that stretched from 2001 into 2003 was the longest (in this sector) since the Great Depression of the 1930s. The rise of China and other developing country export powerhouses, disruptions due to terrorism and its aftermath, rising energy and commodity prices, deflation of the technology bubble, and the poor performance of the European and Japanese economies, all contributed to the long downturn in U.S. manufacturing.

We can point to a number of indicators which begin to give a picture of the new competitive landscape. A good place to start is with longer term data on the creation and distribution of manufacturing plants and jobs in the United States.[3]

The relentless forces of creation and destruction, first described by Joseph Schumpeter, can be measured in the numbers of plant openings and closings over the past four decades. Data collected by the U.S. Department of Commerce show remarkable stability in both creation of new plants and their destruction between 1967 and 1997. Before 1998, we consistently saw about 52,000 plant openings annually. Consequently, between 1967 and 1998, the total number of plants operating in the United States grew from around 310,000 to 375,000. But, in the new millennium, the number of new startups dropped off to an average of 36,000 to 40,000 per year. Plant closings remained stable from 1967 to the present, at a rate of slightly more than 50,000 per year. In contrast, the number of new establishments in the nonmanufacturing sector grew by 848,000 since 1994, in sharp contrast to the loss of 23,000 manufacturing plants in the same time frame. The turning point for manufacturing was around 1998, as the total count of operating manufacturing plants dropped by about 9 percent after this year, for a cumulative loss of some 35,000 plants. Chart 1 shows plant openings and closings since 1992.

This decline cannot be explained by the undeniable fact that some plants have been moved abroad. We do not have fully comparable data regarding plant openings and closings abroad by U.S. manufacturing firms. We do, however, know that between 1999 and 2002, the total number of foreign manufacturing subsidiaries of U.S. firms grew by only 250, while the number of plants located in the United States fell by over 20,000.

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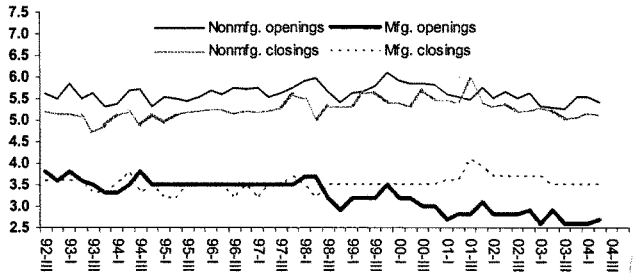
[2] See Thomas J. Duesterberg and Ernest H. Preeg, *U.S. Manufacturing: The Engine for Growth in a Global Economy* (New York: Praeger, 2003).

[3] For a fuller discussion of this trend, see Daniel J. Meckstroth, *The Dynamic Nature of the U.S. Economy: The Churn of Firms and Jobs*, Manufacturers Alliance/MAPI, February 2005.

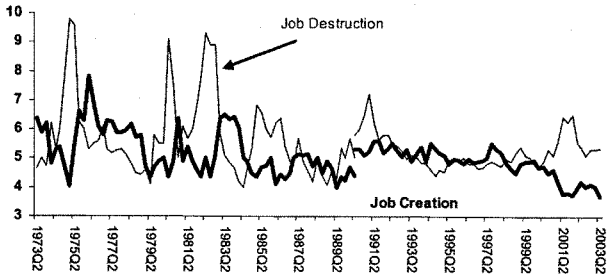
Chart 1
Establishment Openings and Closings By Industry
Seasonally Adjusted Quarterly—1992 III to 2004 I



Source: U.S. Department of Labor, *Business Employment Dynamics Survey*

The manufacturing labor market shows a similar pattern to that of plant openings, as shown in Chart 2. The recession of 2001-2003 in manufacturing saw the worst job performance in this sector since the Great Depression. While about 2.9 million jobs were lost, only about 100,000 have been regained in manufacturing since the recovery began. In six of the past seven months, we have seen job losses in the manufacturing sector. It is the anemic rate of new hires, the counterpart to low levels of new plant openings, that explains the huge loss of manufacturing jobs. Despite a solid recovery in production to previous peak levels by late 2004, employment remains 15 percent below its total at the start of the recession. At this point in the average recovery characteristic of the post-World War II era, we could expect a loss of only 4 percent of manufacturing jobs.

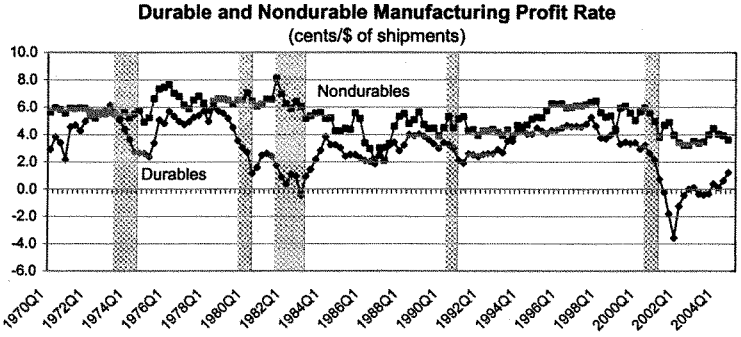
Chart 2
Job Creation and Destruction in Manufacturing
Not Seasonally Adjusted 1990 II to 2003 II
(Percent of total jobs)



Source: Jason Faberman

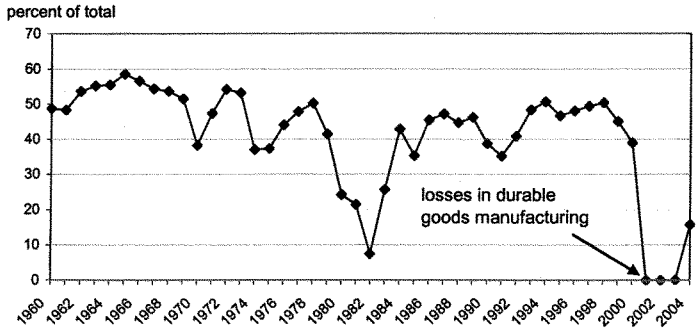
This shift in a long-term pattern of plant openings and job creation dates back to at least 1998 and has continued through the recession and current recovery. Two other disturbing patterns also seem to date back to the late 1990s. First, profits in manufacturing, especially in the durable goods sector—which is the real strength of American manufacturing in terms of technical innovation and productivity growth—have been trending lower in the last decade, as Charts 3 and 4 indicate.

Chart 3
Durable and Nondurable Manufacturing Profit Rate
(cents/$ of shipments)



Source: U.S. Bureau of Economic Analysis (profits) and U.S. Bureau of the Census (shipments)

Chart 4
Durable Goods Industry Profits as a Percentage of Total Manufacturing Profits,1960-2004



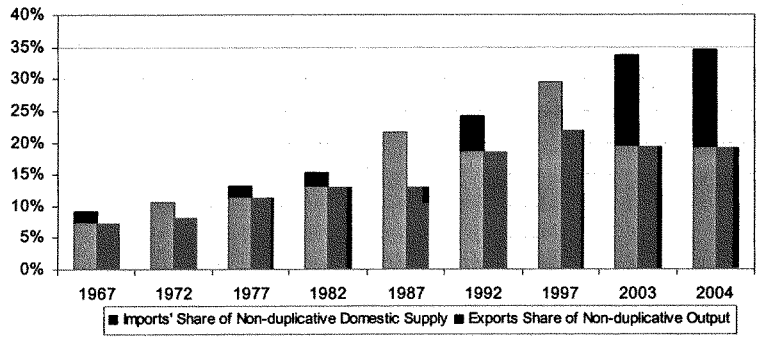
Source: U.S. Department of Commerce, Bureau of Economic Analysis

In the 1980s and 1990s, profits in the manufacturing sector were much higher, as a percent of all corporate profits, than the sector's share of the total economy. While manufacturing represented some 17 percent to 18 percent of total value added in the U.S. economy in 1987, it provided 24 percent of total profits. By 2003, manufacturing provided roughly 14 percent of total output but only 7 percent of profits.

Second, the trade deficit in the goods-producing sector has continued to grow despite the recession earlier in this decade, despite a fall in the value of the dollar against some trading currencies such as the euro, and despite huge gains in productivity which have led to stable-to-lower unit labor costs among U.S. producers. Last year, the trade deficit in goods reached nearly $666 billion, 22 percent larger than in 2003. Even more noteworthy is the growing deficit in so-called "advanced technology products" (ATP), such as computers, aerospace, automation equipment, and pharmaceuticals, which clearly ought to be the growth industries of the future in our sophisticated, innovative, and research-oriented economy. In 1998, we had a $32 billion trade surplus in these products. By 2002 we experienced our first deficit in ATP trade, and last year the deficit grew to $37 billion. Altogether imports have grown from about 9 percent of domestic supply in 1967 to 35 percent in 2004. Export performance has not lost pace; exports were 7 percent of domestic output in 1967, reached a peak at just over 22 percent in 1997, and fell back to under 19 percent in 2004, as Chart 5 shows.

Chart 5

Growth of Imports and Exports in Manufacturing as a Share of Domestic Production



What can explain this rate of new plant openings and hires so far below historical patterns and the structural decline in our balance of trade and in profits in manufacturing? Rapid productivity growth and working off excess capacity from the ebullient 1990s in the manufacturing sector certainly account for some hesitancy in new risk-taking, and thus in decisions to hire and open new plants. Import penetration has grown from 29 percent to 35 percent of the domestic market since 1997, reflecting enhanced competition from China. Nonetheless, in the midst of a global synchronized boom, a falling dollar, and strong global demand for capital equipment—a U.S. strength—other factors are at work to sap the willingness of corporate executives to assume the risks attendant to building new plants and hiring new workers, and to erode the competitive advantages of our high-technology industries which flowed from several generations of technological leadership and steady investment in research and development.

Structural Cost Pressures

One place to start in trying to understand this secular decline is research by my colleague Jeremy Leonard which shows that a combination of cost pressures from energy, health care, tort litigation, corporate taxes, and regulation raises the base price of U.S. manufacturing by more than 22 percent

over raw labor costs alone, when compared to our nine leading trading partners. Such structural costs, when added onto already generous (by global standards) U.S. labor costs, greatly complicate the job faced by corporate executives in convincing their boards and their shareholders to put new money at risk. Table 1 summarizes the basic findings of this study.

Table 1
Effect of Key "Overhead Costs" on Raw Cost Index of Nine Largest U.S. Trading Partners, 2002
(U.S. dollars per hour)

	United States	Average of nine partners	Canada	Mexico	Japan	China	Germany	United Kingdom	South Korea	Taiwan	France
Raw cost index	**24.30**	**19.30**	**27.57**	**8.11**	**16.92**	**5.34**	**29.60**	**28.30**	**23.96**	**16.41**	**26.50**
Difference relative to U.S. costs in percent											
Corporate tax rate	–	-5.6%	-3.4%	-6.0%	2.0%	-15.0%	-0.4%	-10.0%	-10.3%	-15.0%	-5.7%
Employee benefits	–	-5.5%	-4.8%	-9.4%	-9.4%	-12.6%	3.6%	-5.1%	9.0%	-11.5%	10.7%
Tort costs	–	-3.2%	-3.1%	N/A	-3.3%	N/A	-0.7%	-3.4%	N/A	N/A	-1.3%
Natural gas costs	–	-0.5%	-6.0%	-2.3%	12.5%	-2.3%	0.6%	2.1%	4.1%	15.3%	-4.2%
Pollution abatement	–	-3.5%	-2.8%	N/A	-2.3%	N/A	-2.4%	-3.0%	N/A	N/A	-1.5%
Manufacturing production costs relative to the United States accounting for differences in overhead costs (dollars per hour)											
Effective cost index	**24.30**	**16.02**	**22.46**	**6.19**	**16.64**	**3.50**	**29.77**	**23.14**	**22.67**	**12.85**	**25.77**

Source: Jeremy Leonard: *How Structural Costs Imposed on U.S. Manufacturers Harm Workers and Threate Competitiveness* (2003)

Note: Data for tort costs and regulatory compliance costs are limited to the industrialized partners. Conservati assumptions have been made in estimating the missing values. Thus, the absence of these data likely understates th overall cost advantage of U.S. trading partners.

Our study started with raw unit labor costs in the United States and its nine leading trading partners, expressed in dollar value. These include both high-cost producers—Germany, Canada, France, and the United Kingdom—and low-cost producers such as China and Mexico. When comparative data for costs from taxes, natural gas energy inputs, benefit costs, tort litigation costs, and environmental regulation as an average for the nine countries are factored in, the result is equivalent to adding more than $3.00 per hour to the labor cost disadvantage of the United States. As Jim Berges, President of Emerson, and sponsor of our study, concluded:

> U.S. manufacturing has demonstrated the ability to overcome pure wage differentials with trading partners through innovation, capital investment and productivity. But when the structural cost multipliers Leonard describes in this paper are piled on, the task becomes unmanageable even for best-in-class companies. . . .[4]

Since we first published our structural cost study in 2003, some of the input costs we analyzed have become even more burdensome for U.S. producers. For example, benefits costs in the United States continue to escalate at an alarming rate. Between 2000 and 2004, total benefits costs as a share of total compensation grew from 31.6 percent to 35.1 percent. Health care costs remain the primary driver of this escalation, rising from 7.2 percent in 2000 to 8.4 percent of total compensation

[4] See Jeremy A. Leonard, *How Structural Costs Imposed on U.S. Manufacturers Harm Workers and Threaten Competitiveness*, National Association of Manufacturers and Manufacturers Alliance/MAPI, December 2003, p. iii.

costs in 2004. Employer-paid contributions to pension plans, albeit a smaller share of total compensation, grew even faster than health care costs. Workers' compensation costs have also grown substantially in this period, despite the fact that injury and illness rates in manufacturing have declined by 25 percent.[5]

Taxes are among the most important policy-related, structural costs; and in this arena, too, the international competitive environment has trended against U.S.-based producers. Despite the helpful reduction in corporate income tax rates for manufacturers in 2004, many global competitors continue to be aggressive in lowering their corporate income taxes and providing tax incentives for local production. The headline case recently is Germany, which has announced its intention to lower the corporate income tax rate by roughly 20 percent, thus effectively ending its opposition to tax competition and opening the door to further tax cuts throughout the European Union.

The gravity of the situation with regard to higher corporate taxation in the United States was underscored by Paul Otellini, President of Intel, in testimony before the President's Advisory Panel on Federal Tax Reform. Intel is the world's largest semiconductor company, a leader in high-technology research and innovation, and a company that has retained 75 percent of its production in the United States. But Otellini argued that Intel's next generation microprocessor facility would save up to $1 billion over 10 years by locating in one of many lower-tax venues outside the United States.[6] Otellini cited the need for lower corporate tax rates and permanent extension of the research and innovation tax credit. If, as Otellini argues, we are in danger of losing research-based, high-technology operations to foreign locations due to tax policy, then the entire U.S. manufacturing base is likely to be threatened.

Because of intense foreign competition in the goods-producing sector, manufacturers have little ability to raise prices when their own costs of production increase. Given this difficult competitive situation for the manufacturing sector, any additional burden related to policy, which by definition is a controllable cost by society but not by individual companies, is problematic. I would like to focus today on four major areas where the ongoing thrust of regulation is particularly harmful to the manufacturing sector. Much of the debate over regulation tends to focus on the thousands of discrete, important, and oftentimes costly regulations that, while in many cases helpful in achieving agreed social goals, add to the cost of building products in the United States. Too often, however, we forget that government policies which affect the entire economy or major subsectors are equivalent to regulation on a large scale, and have commensurately greater impact. The four areas I will touch on today are: energy regulation; telecommunications regulation; new corporate regulation resulting from the Sarbanes-Oxley Act; and the relatively new phenomenon of regulation by litigation. This last issue is one of the most dangerous, because it often results from the actions of the judicial branch, promoted by private parties and state attorneys general, and not subject to the normal oversight by elected officials. Other sectors, of course, are highly regulated and important to the future of high-technology manufacturing in the United States, such as medical products, but time does not permit a full exploration of the relevant issues.

Energy Regulation—Natural Gas

The U.S. manufacturing sector is the largest user of energy resources in our economy. Given the daily attention to the record costs of energy, especially oil, but also including natural gas and electricity, it is not easy to recall that, for much of the 19th and 20th Centuries, U.S. industrial might was driven by abundant and (relatively) inexpensive supplies of energy. Just a few decades ago, entire industries in the United States were globally dominant in part due to our natural endowment of energy. Primary metals production—including aluminum which depended so heavily on hydropower

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[5] See Jeremy A. Leonard, *Pressures on Manufacturing Costs: It's More Than Health Care*, Manufacturers Alliance/MAPI, March 1, 2005.

[6] See Paul Otellini, "Impact of Taxes on U.S. Semiconductor Company Decisions." Testimony Before the President's Advisory Panel on Federal Tax Reform, San Francisco, California, March 31, 2005.

and nuclear power—chemicals, plastics, glass, paper, and metalworking industries all thrived in an era of energy abundance. U.S. automakers, too, thrived in an era of low energy prices. The current, high price environment is a result of both enhanced global competition for resources, and of domestic regulation which impedes the production, transformation, and transmission of domestic (or North American) resources. The situation is most critical, and most directly related to policy, in the arena of natural gas production.

Since 1998, average natural gas prices in the United States have risen over 300 percent. Demand has risen faster than for other energy resources largely because natural gas is the most environmentally friendly fossil fuel. Also contributing to the rise in price is the reality that natural gas is not easily transported from distant locations.[7] Much of the demand growth resulted from government policy to promote the use of natural gas for electricity production. Between 1986 and 2002, consumption for this purpose grew by 215 percent and is expected to continue its upward path. At the same time, production in the United States has trended lower, falling by 5 percent in the new millennium. Canadian imports have also fallen for a variety of reasons, not the least of which is diversion to local uses such as inputs to the massive projects to recover oil from tar sands in Western Canada. Domestic production in the United States has been discouraged by the many political choices to limit exploration in environmentally sensitive areas and to limit construction of input facilities for liquefied natural gas (LNG).

The resulting supply/demand squeeze explains the huge increase in natural gas costs that affects both consumers and industrial production facilities. The manufacturing sector is especially hard hit because it accounts for about 34 percent of total natural gas consumption. This is especially important because U.S. prices are now significantly above those of major competitors—for example, average U.S. prices are more than 25 percent greater than in Europe, which imports significantly more natural gas than does the United States. Alan Greenspan recently contrasted LNG import prices in Europe, between $2 and $4 per million Btu, and Japan, between $3 and $5, with a consumer price over $6 in the United States.[8] Moreover, unless there is a significant change in policy, prices for natural gas could grow by another 80 percent by 2020.

Almost all manufacturers use natural gas in one form or another, but it is especially important as a preferred heat source in the glass and metal-forming industries. It is, of course, absolutely critical to the chemicals and plastics industries as both a raw material and a heat source. Whereas oil prices are generally set in global markets (and priced in dollars), natural gas markets are more localized and price differentials across countries are significantly greater than for oil or coal.

As an input to the chemicals and plastics industries, natural gas represents about two-thirds of the feedstock in the United States. Oil accounts for the other third. In Europe the proportions are reversed. Hence, the local price disadvantage for natural gas is leveraged in the chemicals and plastics industries vis-à-vis European competition, where prices have been more stable and more natural gas is used.

Recent data on production and international trade in chemicals highlights the deterioration in the terms of trade for this industry. For example, natural gas is the most important cost component for manufacturing nitrogen fertilizer (also known as anhydrous ammonia). Domestic commercial production of ammonia fell from 16.6 million tons in 1999 to just 9.5 million tons in 2001 as a result of higher natural gas prices and weather-related decreases in demand. Exports of ammonia fell from 0.924 million tons for the fiscal year ending June 30, 2000 to 0.576 million tons for the year ending June 30, 2003. Over the same period, ammonia imports rose from 4.7 million tons to 7.3 million

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[7] For a detailed summary of this issue, see Donald A. Norman, *Liquefied Natural Gas and the Future of Manufacturing*, Manufacturers Alliance/MAPI, September 2004.

[8] Alan Greenspan, Remarks Before the National Petrochemical and Refiners Association Conference, San Antonio, Texas, April 5, 2005.

tons. In addition to worsening the trade balance, higher fertilizer prices raise the cost of farming and, ultimately, food.

For the chemical manufacturing industry as a whole, the balance of trade swung from a trade surplus of $16.1 billion in 1997 to a trade deficit of $11.2 billion in 2003 as higher gas prices reduced the competitiveness of domestic producers.[9] The deficit was reduced somewhat in 2004 to an estimated $6.8 billion as global demand rose strongly. Not surprisingly, employment in this technologically sophisticated and innovative industry decreased by over 100,000 between 2000 and early 2005. This loss represents 10 percent of total chemical industry employment in 2000.

Other industries vulnerable to higher natural gas prices include iron and steel and the aluminum industry because of their high gas and electricity use. Anecdotal evidence highlights the challenges higher natural gas prices pose for specific companies. Natural gas costs for PPG Industries, a global supplier of paint, glass, fiberglas, and chemicals, increased 50 percent from 2002 to 2003.[10] Dow Chemical announced that because of higher gas costs, it would reduce its workforce in North America by 3,000 in 2004 after cutting 3,500 jobs the previous year.[11] A Dow spokesperson pointed out that the prices the company pays for natural gas currently are $2.05 to $3.08 per thousand cubic feet (Mcf) cheaper in Europe than in the United States.[12]

There are several ways to address what can only be called a crisis in domestic natural gas costs. One is through increased domestic production, perhaps in conjunction with imports from energy-rich Mexico and Canada. Another is through the use of other abundant domestic resources—coal, nuclear, wind—for generating electricity, hence taking the pressure off natural gas for new production. Finally, the Alliance supports increased imports of LNG as the best ***near-term*** solution to the crisis.[13] New facilities can be brought on-line within two to three years of regulatory approval, at economically competitive prices. Under conservative assumptions for new LNG import facilities, we believe that the current price of natural gas could be ***lowered*** by 25 percent over the next 5 to 10 years, with an enormous benefit for manufacturers.

There are, of course, many other ways to reduce regulatory impediments that increase the price of energy, including electricity. One trade-off for ***not*** taking some of these measures is a punishing cost disadvantage for American manufacturers and continued job destruction and loss of market share in important sectors such as chemicals and plastics.

Telecommunications Regulation

Telecommunications regulation has been highly contentious since the birth of the industry over 100 years ago. In recent decades the industry has been one of the most important in terms of growth, technological innovation, and centrality to the information economy. Success in this sector is vital to the modern economy and also to national security. Although the United States has been and remains among the world leaders in this sector, its performance lags in important international comparisons. The ability of domestic producers (and the service providers who are the largest purchasers of telecommunications equipment) to thrive is closely tied to the regulatory environment, as this sector remains among the most highly regulated of all American industries.

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[9] International Trade Commission, U.S. Department of Commerce. Data pertain to the chemical industry as categorized by NAICS code 325.

[10] "Chemical, Farming Industries Detail Price Woes," *Platts Gas Daily*, March 26, 2004, p. 1, www.platts.com.

[11] "High Gas Costs 'Wreak Havoc' on Manufacturers," *Platts Gas Daily*, July 2, 2004, p. 1, www.platts.com.

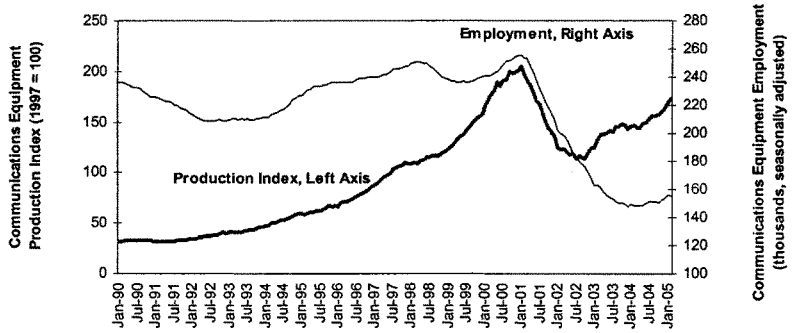
[12] *Ibid.*, p. 6.

[13] Norman, *Liquefied Natural Gas*, *op. cit.*, p. 25.

The story of telecommunications over the past two decades is one of classic boom and bust. Due in part to the deregulation which started with the AT&T divestiture in 1984 and accelerated with the 1996 Telecommunications Act, the industry grew at a dizzying pace in the 1990s. Technical innovation, especially in the essentially new industries of cellular telephony and Internet data transmission, also helped contribute to an unprecedented boom in this industry. As Chart 6 indicates, the 1990s saw a more than 500 percent increase in U.S. production of communications equipment. In late 1999 into mid-2000, new orders in this sector grew by an astounding 73 percent! In 2001 and the years that followed, this sector saw an almost equally precipitous decline. As production volumes plummeted by more than 60 percent, more than 80,000 workers, or one-third of the workforce, in the equipment industry lost their jobs.

Chart 6

Production and Employment in the Communications Equipment Industry 1990-2005



Sources: Bureau of Labor Statistics, U.S. Department of Labor, and Federal Reserve Board

In the last few years, the United States has fallen behind global leaders in some measures of performance in the communications industry which is so central to the modern economy. From what was in 1997 a trade surplus of $8.2 billion in communications equipment, we reached a trade deficit of $5 billion in 2004. In terms of broadband subscriptions per 100 inhabitants, the United States ranks only eleventh among the OECD countries. It lags most European countries, Japan, and the Asian tigers in terms of wireless telephone subscribers. In March, the World Economic Forum announced that America fell from first to fifth place in a measure called its "Networked Readiness Index" covering the information and communications technology sectors.[14]

Despite the heady optimism unleashed by the Telecommunications Act of 1996, this sector has remained highly regulated and highly taxed, which are key factors explaining the collapse and slow recovery of the industry since mid-2000. Analyst Greg Sidak calculated that membership in the Federal Communications bar grew by 73 percent after the 1996 Act, driven by a tripling in the number of pages of regulations in the *FCC Record* and a 37 percent hike in the funding of the

[14] Harold Furchtgott-Roth, "Our National Economic Insecurity," *The New York Sun*, March 15, 2005.

agency.[15] Both the FCC and state (in some cases local) governments retain a significant regulatory role over: allocation of electromagnetic spectrum; deployment and pricing of broadband services; pricing and service offerings of basic telephony providers; and services, pricing, and ownership of broadcast and cable television.

The telecommunications sector also remains one of the most highly taxed in the modern economy. Some of this is historic—such as the federal excise tax which dates to the time of the Spanish-American War, or the depreciation schedules which often predate the invention of modern digital switches—and some is more recent. For example, the 1996 Act called for a "universal service" program, which eager regulators have liberally interpreted as an open invitation to impose a tax on all telecommunications users. The tax has grown from 6.6 percent to 11.1 percent on certain interstate services in the new millennium, at a time when over 95 percent of the population already has telephone service. All told, the typical transition tax burden for telecommunications services is 18.17 percent, compared to an average of 6.12 percent for all industries.[16] These taxes are ***over and above*** normal corporate income taxes.

This combination of ubiquitous (and growing) regulation and heavy taxation has put a damper on the capital investment and basic research needed to keep the United States in the forefront as a leader in the telecommunications industry.[17] As Chart 7 shows, capital investment among telecom services providers fell by over 57 percent between 2000 and 2003. Almost one-third of the total jobs in the equipment industry have been lost since June 2000. The deployment of advanced services such as broadband, which are enablers for other industries such as the Internet, is lagging international competition. Valuable electromagnetic spectrum needed for expansion of broadband connectivity lies idle. The United States is in danger of ceding leadership in one of the marquee growth industries of the future. We need as a consequence to revisit the way we employ regulation and the related taxation of this industry. We need to free up broadband providers; make spectrum available to the most economic uses; recalibrate the tax structure affecting this industry, especially the various excise taxes and depreciation schedules; and find ways to promote domestic research and capital investment. We should not allow high-tech industries—especially those vital to national security—to go the way of the textile industry. Regulatory reform is a large part of the renewal process.

Regulation of Corporate Governance

One of the most effective responses to global competition is lean manufacturing and its various offshoots. This concept applies to management as well as to production functions. Senior corporate executives have broader responsibilities as their firms downsize, and the complexity of their work increases in direct proportion to the rapid pace of change which characterizes the modern goods-producing sector. It is in this context that we can try to understand the impact of the enhanced regulation of corporate governance resulting from the Sarbanes-Oxley Act of 2002 (SOX).

The serious breach of trust (and law) by executive malfeasance at high-profile companies such as Enron, MCI, and others over the past five years, along with a loss of confidence in corporate reporting after the market crash early this century, led to passage of SOX. Implementation of this new law has proven to be extremely costly, both in terms of the time devoted by senior executives to compliance with the Act and the added costs, both internal and external, necessitated by the new audit and control requirements. Through the more than 500 finance, accounting, and tax executives

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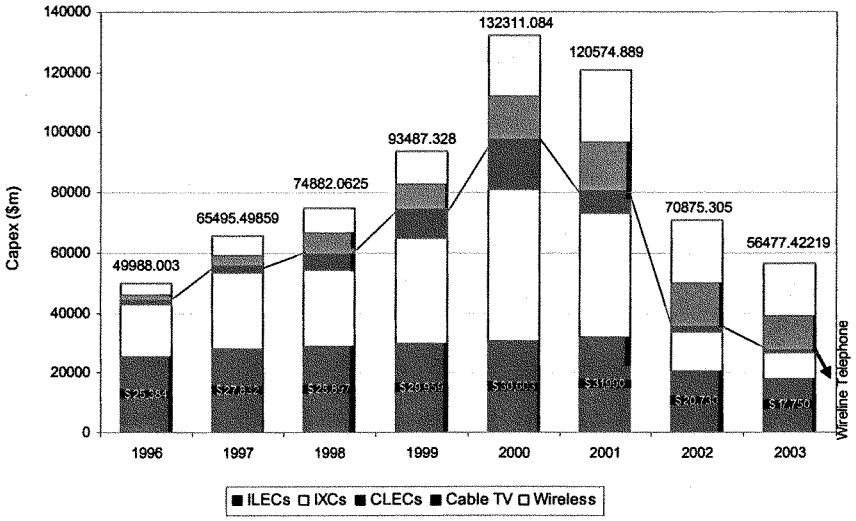
[15] As summarized by Adam Thierer, "The Non-Revolution in Telecommunications and Technology Policy," in Chris Edwards and John Samples, eds., *The Republican Revolution 10 Years Later*, Cato Institute, 2005, p. 175.

[16] See Telecommunications Tax Task Force of the Council on State Taxation, "2004 State Study and Report on Telecommunications Taxation," 2005.

[17] It is also costly to consumers; a recent study estimates that federal regulations cost consumers up to $105 billion annually in higher prices and foregone services. See Jerry Ellis, *Costs and Consequences of Federal Telecommunications and Broadband Regulations*, Arlington, VA, Mercatus Center, 2005.

Chart 7

Capital Expenditures by U.S. Telecom Service Providers: 1996-2003



Note: ILECs (Local Phone Companies); IXCs (Long Distance Carriers);CLECs (Competitive Local Exchange Companies

Source: T. Rowe Price and Company Reports

participating in MAPI programs, we have been closely following management efforts to comply with SOX. We have done four separate surveys of the direct costs associated with implementation. At each successive iteration, these costs are multiplying. Our most recent survey of some 60 senior financial officers at medium to large companies on the costs of compliance with Section 404 is revealing. Key results are as follows:

- The cost of compliance for respondent companies, expressed as a percent of net income before taxes, averaged 5.9 percent. The median percentage was 4.1 percent. These percentages are high and indicate that the cost of 404 compliance has significantly impacted the bottom lines of many companies.

- External auditor fees for 404 compliance totaled an estimated $110.2 million, almost as much as the $124.2 million spent by the 54 respondent companies on the external financial statement audit excluding 404 attestations.

- The cost of compliance, including external audit fees, external (non-audit) assistance for compliance, and internal audit costs for 404 compliance totaled an estimated $352.7 million for the 56 firms who participated in this survey.

- Most firms (42 out of 47 who responded) report that their audit costs for 404 attestations exceeded initial quotes. Of the 42 firms reporting that audit costs exceeded initial quotes, 63 percent reported that the excess was 50 percent or higher.

- Sixty-nine percent of the respondents say that the relationship between their company and its external auditor has deteriorated to varying degrees. The remaining respondents indicated "no change" (21 percent) or "improved" relations with their external auditors (10 percent).

It is quite startling to learn that the average cost of compliance at this sample of companies represented ***5.9 percent of net income before taxes***.[18] By any measure, not the least of which is the profit squeeze already affecting the globalized manufacturing sector, this represents a significant burden. Compliance costs may be even more burdensome for smaller companies and probably discourages them from going public. Thus, they are more isolated from our large and liquid capital markets.

Equally troubling is the time and energy needed by senior management to comply. Some large companies estimate that compliance with section 404 of SOX adds 100,000 man hours per year, with one company reporting 130 employees working full time on section 404.[19] A recent study by executive recruiter Russell Reynolds Associates corroborates anecdotal evidence and testimony we have received from our members: "Increased pressure for regulatory compliance is driving more chief financial officers out the door." The two main reasons for increased dissatisfaction and turnover in the ranks of corporate chief financial officers, according to the study, are SOX compliance and pressures to meet investors' short-term earnings expectations.[20]

Sarbanes-Oxley is a disheartening example of overregulation that puts American companies at an international competitive disadvantage. Advanced technology companies are probably hurt the most because they have to be flexible and constantly alert to the need to change and innovate to stay ahead of their competitors. SOX implementation saps their time and works to slow down decision making at all levels. SOX compliance not only takes enormous time, money, and energy from senior executives, their boards, and their firms, the Act also dangles the sword of Damocles over their heads with new criminal liability provisions. In summary, SOX compliance hits the bottom line of manufacturing firms hard, saps the time and energy of management which could be devoted to a creative response to globalization, and discourages risk taking.

Regulation Through Litigation

As if the threats to the competitiveness of U.S. industry posed by a civil justice system that has run amok, rising structural cost pressures, and a crippling burden of regulations were not enough, a disturbing convergence of these problems has been cultivated in recent years in the form of regulation through litigation. In addition to its anti-competitive impact on industry, this emerging problem represents nothing less than an effort to employ liability litigation in a manner that usurps Congress's constitutionally mandated role in lawmaking.

The practice I am referring to involves the employment of private trial lawyers by state and local governments to conduct a coordinated litigation effort against an entire industry, purportedly for the purpose of attacking serious public health or safety problems.[21] To date, these so-called government recoupment lawsuits have been brought against controversial, politically disfavored industries such

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[18] MAPI comments to the SEC on Sarbanes-Oxley were filed on March 31, 2005, as File 4-497. This provides a comprehensive review of compliance costs and constructive suggestions for changes to the SOX procedures.
[19] "404 tonnes of paper," *The Economist*, December 18, 2004, p. 116.
[20] See Erin White, "Call It Sarbanes-Oxley Burnout: Finance-Chief Turnover Is Rising," *The Wall Street Journal*, April 5, 2005, p. B-4.
[21] For a more detailed discussion of this problem, see Frederick T. Stocker, *I Pay, You Pay, We All Pay: How the Growing Tort Crisis Undermines the U.S. Economy and the American System of Justice*, Manufacturers Alliance/MAPI, Arlington, VA, 2003, Chapter 7.

as tobacco and firearms. Suits against such industries tempt socially activist judges into ignoring developed principles of civil law and establishing new theories of liability and duties based upon their individual public policy preferences. The problem is that courts which bend rules for controversial products set precedents that will apply equally to all industries. A situation results where governments are presented with a template to follow in suing other industries whose products or services—although they were legally sold and, at that time, may not even have been recognized as posing any health or safety risk—are now perceived to constitute some public harm that can only be alleviated through litigation.

In this type of litigation, state or local governments seek to recover considerable monetary damages for their claimed losses, as well as to force some changes in industry practices as a means of ameliorating a societal ill for which that industry is seen as having some responsibility. The sheer magnitude of potential damages is a major negotiating lever to induce an industry to change practices. In the case of the firearms suits brought by dozens of local governments in numerous jurisdictions, defense costs alone threatened to bankrupt an industry and served as a considerable inducement to settlement. In short, organizational changes that normally occur in response to state or federal legislation or regulations instead occur as a result of litigation initiated by pressure groups in search of victories in court that could not be achieved at the ballot box.

The lurking threat behind this trend is that yesterday's suits against the tobacco and firearms industries become today's suits against adult beverage, pharmaceutical, or even automobile manufacturers; the lead paint industry; the entertainment and gaming industries; and Internet providers or fast food restaurant chains. The list of industries that might be fertile targets for these suits that threaten their continued competitiveness is limited only by the ambitions of state and local politicians and the imagination of trial lawyers. The deep pockets of the target industry—not the underlying processes or products of the companies—are often the determining factor in this type of legal action.

Finally on this point, legislating public policy in the courts threatens the separation of powers doctrine and reveals an astonishing contempt for the democratic process and for elected legislators. I believe that the role of the legislature is to legislate and the role of the courts is to interpret the law. These distinct roles should not be confused by state and local legislators in the name of political expediency, by their trial lawyer partners seeking personal gain, or by an activist judiciary desirous of making a social statement.

Conclusions

In the face of relentless foreign competition, lack of pricing power due to that competition, zealous regulators and prosecutors, and difficult cost pressures (now magnified by high materials costs), the animal spirits of risk-taking in the manufacturing sector are themselves at risk, as witnessed by historic lows of plant and job creation. These conditions are exacerbated by falling profit margins and by a significant deterioration in the terms of trade. The role of regulation in this environment is crucially important. This includes not only the type of regulation at a macro level described above, but the thousands of specific and narrow-gauge regulations that manufacturers must contend with every day. We must do a better job of balancing the risks and rewards of regulation. We should not allow ourselves to despair, as if current conditions and trends are irreversible.

Fortunately, there are deep reservoirs of optimism among American executives, buttressed by the efficient creative genius of our best innovators and researchers. Moreover, the American legal, cultural, and business environment remains even today superior to that of many of our global competitors in nurturing the constant pursuit of innovation, change, and risk needed to succeed in the modern economy. These forces, however, urgently need assistance from our policy makers. A more rational tort and regulatory environment, better controls on health care costs, pro-growth energy and telecommunications policies, more openness and less mercantilism in international markets, a tax structure that does not penalize domestic production and encourages research and investment, and a

better educated workforce, all could contribute to a better environment for risk-taking and innovation. The rise of China and India represents the greatest challenge to manufacturers in recent memory, but also, with their enormous demand for new goods, the greatest opportunity for risk-takers emboldened and properly incentivized to meet the challenge.

Mrs. MILLER. Our next witness this morning is Lori Luchak. She is the vice president and marketing director for Miles Fiberglass & Composites in Portland, OR. Mrs. Luchak is testifying on behalf of the American Composites Manufacturing Association, which is the world's largest trade association representing the composites industry.

Miles Fiberglass & Composites is a family owned corporation founded in 1963 with plants in Portland and Oregon City. In 2003, Oregon Business Magazine scored Miles Fiberglass one of the top 100 best companies to work for.

Mrs. Luchak, we certainly want to thank you for making the trip to Washington, DC, this morning. The committee welcomes you and looks forward to your testimony.

STATEMENT OF LORI LUCHAK

Ms. LUCHAK. Madam Chairwoman and members of the committee, thank you for the opportunity to testify today.

Miles Fiberglass & Composite employs 60 employees in our two plants located in Oregon. Our company manufacturers component parts for the RV and light rail train industry. I am here representing the 1,000 member companies of the American Composites Manufacturers Association.

Our industry supported the recent OMB initiatives to identify specific regulations needing reform to lessen unnecessary burdens on manufacturers. Of the 76 regulations identified by OMB and Federal agencies as justifying reform measures, several directly or indirectly impact the composite industry.

Beyond these targeted efforts, we would like to suggest some general principles for rulemaking that the committee might consider in its oversight of their regulatory process. These general principles are drawn from our efforts over the years to work in partnership with the government agencies to protect the health of our workers and neighbors.

First, industry and other stakeholders should be given a seat at the table very early in the development of any regulation, policy or determination. Stakeholders often have data on feasibility, health impacts, control options, energy use, cost and other factors, or can readily develop such information that can play a key role in shaping the early development of rules, policy, or determinations. But too often we find that agencies are already well along the way before they sit down with us and start accepting our input. At this point, agencies have spent months or years developing narrow approaches based on lesser-quality data, analyses, viewpoints and assumptions.

Our information, if brought into the development process from the start, can result in better decisionmaking and more efficient regulatory development. When stakeholders are brought in only late in the development process, we run the risk that the agency will argue that it is not able to consider our suggested alternative approaches because their regulatory schedule does not allow them to back up and collect the necessary data or do the needed analysis in time for the required decision.

Second, development of rules, policy, guidance or determination should be managed transparently. By this we mean that all the

data and analyses that may be relied on by an agency should be made available for stakeholders' review as early as reasonably possible. Further, all decisionmakers and peer reviewers who may be involved should be identified and stakeholders allowed a reasonable opportunity to present data analysis and other information to these decisionmakers and reviewers. There should be no black boxes; that is, no data or decisionmaking processes that are not open to at least some level of reasonable stakeholder input.

Agencies often argue that the integrity of the system requires them to keep stakeholders less involved; however, we believe the opposite is true. Without the opportunity for a meaningful and open stakeholder involvement, the integrity of the decisionmaking process is often compromised.

Third, regulatory agencies should embrace the use of best quality data at every stage of developing rules, determinations or policies. This should include internal checks on data quality as well as timely opportunities for stakeholders to informally appeal quality decisions before poor quality data is used to prepare and justify preliminary or draft agency decisions. Finally, agencies should be more willing to take responsibility for full economic and societal impacts of regulatory actions and determinations.

Efforts by regulators and government health scientists to consider the economic, competitive and other broad impacts of proposed rules, policies or determinations are often precluded by narrow program objectives, or are no more than meaningless "check the box" responses to OMB or congressional directives completed after the key decisions have been made. These impact assessments can be difficult and time-consuming, but actions promulgated without considering these impacts can needlessly result in severe damage to our ability to make products and provide employment.

To summarize, our experience has shown that adoption of the following principles would result in a more effective partnership of government and industry to protect the public health: A seat for stakeholders at the table early in the regulatory process; a transparent development process, with stakeholders given a reasonable opportunity to present data and discuss regulatory options; a clear commitment to using the best available science and making decisions with an opportunity for stakeholders to point out where they believe the commitment is not being fulfilled; a meaningful commitment to understand the economic and societal impacts of all decisions before decisions are made to pursue them; and improvements in the openness of the scientific health assessment processes of the Federal agencies, and efforts to coordinate their reviews and avoid overlap and duplication.

These are the principles that in our small way we are attempting to express and promote in our interactions with these regulatory agencies in the context of specific ongoing assessments and regulations about which we are concerned. However, we hope that because these principles are of a wider scope, they may be helpful to the committee in framing its oversight and any possible legislation or guidance to the regulatory agencies and the administration as a whole.

Our industry is proud of our record of working both independently and in partnership with regulatory agencies to protect the

health of our workers and neighbors. Our industry sponsored a thorough review of health risks by the Harvard School of Public Health in 2002, and we comply with the recommendations made by the Harvard panel. Our industry also voluntarily negotiated with OSHA to establish a recommended occupational exposure limit well below the official OSHA limit. And we continue a 15-year, $15 million history of conducting state-of-the-art research to make sure we fully understand the health risks that may result from our operations.

I appreciate the opportunity to deliver these comments to you today, and we would welcome any requests by this committee for assistance in helping to improve the regulatory climate for manufacturers in America while still protecting the health of our employees and neighbors.

Thank you very much.

Mrs. MILLER. Thank you so much.

[The prepared statement of Ms. Luchak follows:]

April 12, 2005

Testimony before the
U.S. House of Representatives
Committee on Government Reform
Subcommittee on Regulatory Affairs

Lori Luchak
Miles Fiberglass & Composites
Portland, Oregon

On behalf of the
American Composites Manufacturers Association[1]
Arlington, VA

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[1] ACMA contact: John Schweitzer, Senior Director of Government Affairs, 1010 N. Glebe Rd., Arlington, VA 22201, telephone 734.622.0162, e-mail jschweitzer@acmanet.org.

Good morning. I am Lori Luchak, and I am the Vice President and Marketing Director of Miles Fiberglass & Composites. We employ 60 people in our two plants located in Oregon. Our company manufactures component parts for the RV industry, interior/exterior parts for the light rail train industry, railcar liners for the heavy rail industry, equipment housings for the medical equipment manufacturers, and lubrication pits for truck/car lubrication centers. I'm here representing the 1,000 member companies of the American Composites Manufacturers Association.

There are a number of challenges to successful manufacturing in the US today. High and unpredictable energy costs make it too expensive to buy raw materials and run our plants. The cost and threat of groundless lawsuits drains millions of dollars of productive capital out of our economy and dampens our country's entrepreneurial spirit. Estate taxes unfairly burden small family-owned manufacturers. And imports from foreign countries with unfair monetary practices and poor labor and environmental conditions make it hard to keep Americans employed.

But today I'd like to talk about how excessive and unreasonable regulations can make it harder for manufacturers like Miles Fiberglass & Composites and others in my industry to grow our businesses and employ people in communities across America.

Our industry supported the recent OMB initiative to identify specific regulations needing reform to lessen unnecessary burdens on manufacturers. Of the 76 regulations identified by OMB and federal agencies as justifying reform measures, several directly or indirectly impact the composites industry, including EPA's AP-42 emission factors, Title V operating permits, "potential to emit" and "volatile organic compound" definitions,

hazardous waste identification rules, and OSHA's adoption of updated versions of national consensus standards.

But beyond these targeted efforts, we'd like to suggest some general principles for rulemaking that the Committee might consider in its oversight of the regulatory process. These general principles are drawn from our efforts over the years to work in partnership with government agencies to protect the health of our workers and neighbors.

First, industry and other stakeholders should be given a "seat at the table" very early in the development of any regulation, policy, or determination. Stakeholders often have data on feasibility, health impacts, control options, energy use, costs and other factors – or can readily develop such information – that can play a key role in shaping the early development of rules, policy or determinations. For example, in large part because of the extensive data and analysis provided by industry, EPA's recently issued "maximum achievable control technology" standards for composites manufacturing set aggressive control requirements while still giving my industry the cost-effective control options we need to continue making products and innovating to serve new markets.

But too often, we find that agencies are already well along before they sit down with us and start accepting our input. At this point, agencies have spent months or years developing narrow approaches based on lesser-quality data, analyses, viewpoints, and assumptions. Our information, if brought into the development process from the start, can result in better decision making and more efficient regulatory development. When stakeholders are brought in only late in the development process, we run the risk that the agency will argue that it is not able to consider our suggested alternative approaches

because their regulatory schedule does not allow them to back up and collect the necessary data or do the needed analysis in time for the required decision.

Second, the development of rules, policy, guidance or determinations should be managed transparently. By this we mean that all the data and analysis that may be relied on by an agency should be made available for stakeholder review as early as reasonably possible. Further, all decision makers and peer reviewers who may be involved should be identified, and stakeholders allowed a reasonable opportunity to present data, analysis and other information to these decision makers and reviewers. There should be no "black boxes" – that is, no data or decision making processes that are not open to at least some level of reasonable stakeholder input. Agencies often argue that the "integrity" of the system requires them to keep stakeholders less involved; however, we believe the opposite is true. Without the opportunity for meaningful and open stakeholder involvement, the integrity of the decision-making process is often significantly compromised.

Third, regulatory agencies should embrace the use of the best quality data at every stage of developing rules, determinations, or policy. This should include internal checks on data quality as well as timely opportunities for stakeholders to informally appeal data quality decisions before poor quality data is used to prepare and justify preliminary or draft agency decisions.

Finally, agencies should be more willing to take responsibility for the full economic and societal impacts of regulatory actions and determinations. Efforts by regulators and government health scientists to consider the economic, competitive, and other broad impacts of proposed rules, policies or determinations are often precluded by

narrow program objectives, or are no more than meaningless "check the box" responses to OMB or Congressional directives completed after the key decisions have been made. These impacts assessments can be difficult and time consuming, but actions promulgated without considering these impacts can needlessly result in severe damage to our ability to make products and provide employment.

We are currently participating in a pilot project conducted by EPA's Air Office to involve stakeholders very early in the development of a smaller rule involving our industry. We applaud EPA for taking the initiative in this case to study better ways of gaining stakeholder participation, increase transparency, and improve the quality of data and analysis used in a rulemaking, and we look forward to EPA's eventual application of the lessons learned during this pilot to other rulemaking programs.

However, there is another area where we are very concerned that the lack of stakeholder involvement, transparency, and responsibility for down-stream consequences may have a severe impact on our and other industries. Three independent health hazard assessments are currently underway on a chemical widely used in the composites industry. One of these assessments is being managed by EPA in the form of an update to the Integrated Risk Information System listing for this chemical, and the other two are being managed by the HHS National Toxicology Program.

We and the scientific experts in our broader industry are working hard with EPA and NTP to increase our ability to provide data and analysis, improve the transparency of the processes, minimize unwarranted harm to our industry, and improve coordination among these three programs. However, in different ways, the decision making processes

employed by these agencies seem to be designed to minimize stakeholder scientific input and to ignore the potential economic consequences of their decisions.

Scientific health assessments have traditionally been carried out behind closed doors in the Federal government, with stakeholders learning of the results and the underlying reasoning only after the assessments are sent out to external peer review or announced to the public. And while the agencies intend the assessments to serve as inputs to subsequent site-specific risk management activities, in reality the assessments are often taken by local regulators and members of the public as the "final answer" regarding the risk of chemical health effects, with serious unwarranted consequences to manufacturers.

We believe a more collaborative endeavor among all the knowledgeable parties, including those scientists who work for or with stakeholders, is the most sure way to arrive at both the best possible scientific conclusions and the best ways to communicate these conclusions to local risk mangers, workers, and plant neighbors. In addition, greater coordination among the agencies carrying out these health assessments would make it easier for stakeholders to participate, and would avoid the likelihood of conflicting announcements of potential health effects by different agencies. Today, each of these agencies schedules its work independently.

To summarize, our experience has shown that adoption of the following principles would result in a more effective partnership of government and industry to protect the public health:

- A seat for stakeholders at the table early in the regulatory process;

- A transparent development process, with stakeholders given a reasonable opportunity to present data and discuss regulatory options;
- A clear commitment to using the best available science in making decisions, with an opportunity for stakeholders to point out where they believe this commitment is not being fulfilled;
- A meaningful commitment to understand the economic and societal impacts of all actions before decision are made to pursue them; and
- Improvements in the openness of the scientific health assessment processes of the Federal agencies, and efforts to coordinate their reviews and avoid overlap and duplication.

These are the principles that, in our small way, we are attempting to express and promote in our interactions with these regulatory agencies in the context of the specific ongoing assessments and regulations about which we are concerned. However, we hope that because these principles are of a wider scope, they may be helpful to the Committee in framing its oversight and any possible legislation or guidance to the regulatory agencies and the Administration as a whole.

Our industry is proud of our record of working both independently and in partnership with regulatory agencies to protect the health of our workers and neighbors. Our industry sponsored a thorough review of health risks by the Harvard School of Public Health in 2002, and we comply with the recommendations made by the Harvard panel. Our industry also voluntarily negotiated with OSHA to establish a recommended occupational exposure limit well below the official OSHA limit. And we continue a 15

year – $15million history of conducting state-of-the-art research to make sure we fully understand the health risks that may result from our operations.

I appreciate the opportunity to deliver these comments to you today, and we would welcome any request by this Committee for assistance in helping to improve the regulatory climate for manufacturers in America while still protecting the health of our employees and neighbors.

Mrs. MILLER. And our last witness today is Sidney Shapiro, distinguished Chair in law at Wake Forest University. Mr. Shapiro is testifying on behalf of the Center for Progressive Regulation, which is an organization for which he is a member of the board.

The Center for Progressive Regulation is a nonprofit research and educational organization of university-affiliated academics with expertise in the legal, economic and scientific issues related to regulation of health, safety and environment.

Mr. Shapiro.

STATEMENT OF SIDNEY SHAPIRO

Mr. SHAPIRO. Thank you, Madam Chairwoman. Many Shapiros, but I am a Shapiro.

For the last several years, OMB has invited nominations of regulations that should be reformed. Lately it sought to justify this process on the ground that regulation makes U.S. business less competitive. The scholarly literature, however, provides little or no support for the conclusion that such a tradeoff exists.

Academic scholarship has focused on the impact of environmental regulations on plant location decisions and on trade flows. Neither type of study supports a link between regulation and competitiveness. The leading study in the field states that there is "overall, relatively little evidence to support the hypothesis that environmental regulations have had a large adverse effect on competitiveness, however that term is defined."

This result should not be surprising for two reasons. First, compliance costs are only a very small percentage of the total value of shipments made by manufacturers. Pollution abatement costs, for example, average less than 1 percent of the total value of manufactured goods in the United States. Industry sectors with high abatement costs pay less than 1½ percent of the value of shipments. Second, many claims about regulatory costs are suspicious because they rely on cost estimates that come from industry sources that have an incentive to overstate the costs for regulatory and public relations purposes. OSHA itself, in its latest report, admits that existing economic studies do not establish a competitiveness regulatory tradeoff. Its response is that manufacturing industries have disproportionately higher regulatory costs than other industries. But manufacturers are also responsible for a larger portion of the environmental and occupational safety and health problems in the country.

The government should look back at existing regulations, but this should be done as part of an overall priority-setting process that includes an evaluation of when and whether additional regulation is also necessary and appropriate. Instead, OMB's process unbalances how regulatory priorities are set in the Federal Government in favor of the pet projects of certain industries.

While 85 percent of the reform nominations were made by industry, as we have heard, 15 percent were submitted by public interest groups. But on the final list approved by OMB, 97 percent of the reforms were industry-sponsored, and a paltry 3 percent were from the public interest community.

Instead of an ad hoc process, OMB should require agencies to consider regulatory reform requests in the context of an agency's

annual regulatory plan. This plan gives an agency the opportunity to place such requests to modifying regulations within the hierarchy of all agency business and give appropriate priorities to all agency business.

OMB also seeks to justify its nomination process as necessary to protect the small business community. While the small business community is deserving of special consideration from regulators, it already receives such consideration through existing exemptions and protections. More importantly, perhaps, very few of the final OMB hit list recommendations appear to address small business concerns. Of the 71 final reforms, only 11 purport to focus at all or in part on small business.

Finally, no one should object to an effort to make it less costly to meet existing levels of regulation, assuming that the changes lead to the same level of regulatory protection. Some of the nominations address this objective. Many of the nominations, however, seek to reduce the level of regulatory protection of people and the environment.

At the same time, OMB has almost entirely disregarded the nominations and ways to improve such protections as I have stated earlier.

I thank you for the opportunity to testify.

Mrs. MILLER. Thank you very much.

[The prepared statement of Mr. Shapiro follows:]

Testimony of

Sidney A. Shapiro

University Distinguished Chair in Law
Wake Forest University
Winston-Salem, N.C.

Scholar
Center For Progressive Regulation

Before the
Subcommittee on Regulatory Affairs
Committee on Government Reform
U.S. House of Representatives

Hearing on
"Impact of Regulations on U.S. Manufacturing"

April 12, 2005

Testimony of
Sidney A. Shapiro
University Distinguished Chair in Law
Wake Forest University
Winston-Salem, N.C.

Scholar
Center For Progressive Regulation

Before the
Subcommittee on Regulatory Affairs
Committee on Government Reform
U.S. House of Representatives

April 12, 2005

Thank you for the opportunity to testify before you today. My name is Sidney A. Shapiro. I am the University Distinguished Chair in Law at Wake Forest University, Winston-Salem, N.C. I have also been the John M. Rounds Professor of Law at the University of Kansas, Lawrence, Kansas. I hold a B.S. in Economics from the Wharton School of Finance and Commerce, University of Pennsylvania, and a J.D. from the University of Pennsylvania Law School. My expertise is in administrative law and regulatory policy. My most recent book is *Sophisticated Sabotage: The Intellectual Games Used to Subvert Responsible Regulation*, published by the Environmental Law Institute Press. I am also the co-author of *Risk Regulation at Risk: Restoring a Pragmatic Approach*, published by Stanford University Press, two law school textbooks, on regulatory law and practice and administrative law, as well as a one-volume administrative law treatise. I have published over 40 articles.

I am also a Scholar at the Center for Progressive Regulation (CPR). The Center for Progressive Regulation is a nonprofit research and educational organization of university-affiliated academics with expertise in the legal, economic, and scientific issues related to regulation of health, safety, and the environment. CPR supports regulatory action to protect health, safety, and the environment, and rejects the conservative view that government's only function is to increase the economic efficiency of private markets. Through research and commentary, CPR seeks to inform policy debates, critique anti-regulatory research, enhance public understanding of the issues, and open the regulatory process to public scrutiny.

Recently, the Office of Management and Budget published a report entitled "Regulatory Reform of the U.S. Manufacturing Sector."[1] The report indicates that in

[1] Available at http://www.whitehouse.gov/omb/inforeg/reports/manufacturing_initiative.pdf.

2004 OMB invited nominations of specific regulations that, if reformed, could result in lower costs, greater competitiveness, more regulatory certainty and increased flexibility. Having received 189 reform nominations, OMB, after consultation with the relevant agencies, determined that 76 nominations had potential merit and merited further action.

In the report, OMB maintains that reform of regulation of the manufacturing sector of the United States is necessary because "manufacturing bears a disproportionate share of the overall regulatory costs in the economy." OMB indicates further that since U.S. manufacturers "compete with firms from both developed and developing countries in an increasingly global environment, the Administration believes it is critical that any unnecessary regulatory burdens be removed."

My testimony today reaches the following conclusions:

- **No Regulation-Competition Link**: The scholarly literature provides little or no support for the conclusion that regulation hinders the competitiveness of manufacturing industries or is the cause of the significant job losses in those industries. The primary reason that Federal regulation is not responsible for American manufacturers being less competitive is because ***regulatory costs average less than one percent of the total value of manufactured goods*** in the United States.

- **OMB's Lack of Evidence:** OMB recognizes the previous evidence and admits that it does not establish a competitiveness-regulatory tradeoff. Its response is that manufacturing industries have higher regulatory costs than other industries, but manufacturing industries are also responsible for a larger portion of the environmental and occupational problems in this country.

- **Real Priority Setting**: The government should look back at existing regulations, but this should be part of an overall priority setting process that includes an evaluation of where additional regulation is necessary and appropriate. Instead, OMB's nomination process unbalances how regulatory priorities are set in the federal government in favor of the pet projects of regulated industries.

- **The Small Business Excuse**: While small business is deserving of special consideration from regulators, it already receives such consideration through existing exemptions and protections. Moreover, very few of the OMB final hit-list recommendations appear to address small business concerns.

- **The Reform Masquerade**: While some reform nominations looks for ways to decreasing the cost of meeting existing levels of regulation, many

nominations seek to lower the level of protection of people and the environment. At the same time, the OMB almost entirely disregarded nominations of ways to improve the protection of people and the environment.

I. No Regulation-Competitiveness Link

When OMB claims that regulation harms the competitiveness of United States business, it is merely echoing a long-standing claim of the business community. The scholarly evidence, however, refutes this claim. While the business community may be hampered in competing in global trade, regulation is not at fault. The business community, however, has nothing to gain by publicizing the real reasons for its difficulties, such as lower wages paid in other countries. The idea that regulation causes competitive decline is the product of a public relations campaign, rather than careful scholarly work.

The anti-competitiveness myth is fueled by reference to the hundreds of millions of dollars spent by American industry on regulatory compliance.[2] These citations, however, provide a dubious basis to criticize regulation for three reasons.

Regulations Produce Net Benefits: Citations to the high cost of regulation do not establish that regulation is unwarranted because they completely ignore what we gain from these expenditures. While protecting people and the environment may cost a lot of money, it also produces far larger benefits. As OMB reports to Congress every year, regulation in the United States generates aggregate benefits that greatly exceed the cost of the federal regulations.[3]

Overblown Cost Estimates: Moreover, many claims about regulatory costs are suspicious because they rely on cost estimates that come from industry sources that have an incentive to overstate the costs for regulatory and public relation purposes. According to a recent influential study:

> [E]x ante cost estimates have usually been high, sometimes by orders of magnitude, when compared to actual costs incurred. This conclusion is not at all surprising in light of the strategic environment in which the predictions are generated. In preparing regulatory impact assessments for proposed rules, agencies are heavily dependent upon the regulated entities for information about compliance costs. Knowing that the agencies are less likely to impose regulatory

[2] *See, e.g.*, Jeremy A. Leonard, How Structural Costs Imposed on U.S. Manufacturers Harm Workers and Threaten Competitiveness (Prepared for The Manufacturing Institute of the National Association of Manufacturers) (2003).

[3] OMB, Draft 2005 Report to Congress on the Costs & Benefits of Federal Regulation, at 7 Table 1-1 (aggregate benefits of $12,596-108,483 billion dollars and aggregate costs of $3,840-4,073 billion).

options with high price tags (or to support them during the review process), the regulatees have every incentive to err on the high side.[4]

Small Percentage of Costs: Finally, and most importantly for these purposes, regulation cannot be blamed for a decline in competitiveness or other economic ills because compliance costs are only a very small percentage of total value of the shipments made by manufacturers. On the basis of data from the World Bank, Professor Kevin Gallagher (Boston University) finds the "sum of all marginal pollution abatement costs in the United States is less than one percent of value added production."[5] Department of Commerce data confirm this estimate. This information indicates abatement expenditures are an average of 0.62 percent of the value of shipments of all industries.[6] Industry sectors with high abatement costs pay between 1.27 and 1.51 percent of the value of shipments.[7]

Other regulatory costs – such as loss of productivity, unemployment, price increases, and the loss of consumer welfare – are derivative of direct compliance costs.[8] Since low direct costs generally will produce low indirect costs,[9] regulation overall should have a minor competitive and labor impacts.

The scholarly evidence backs up this claim. Economists have considered the impact of environmental regulations on plant-location-decisions (do pollution-intensive industries build disproportionate number of new factories in countries or areas of the United States where there is weak environmental regulation?) and on trade flows (do exports from developed to developed countries show an increasing percentage of pollution-intensive goods?). Neither type of study supports a regulation-competitiveness link.

The leading summary of the research is by Adam Jaffee (Brandeis University, National Bureau of Economic Research), Steven R. Peterson (Economics Research Group), Paul R. Portney (Resources for the Future) and Robert N. Stavens (Harvard University, Resources for the Future). In their review of plant location and trade flow studies, they found that "studies attempting to measure the effect of environmental regulation on net exports, overall trade flows, and plant-location-decisions have produced estimates that are either small, statistically insignificant, or not a robust to test of model specification."[10] As a result, they concluded, there is "[o]verall ... relatively little

[4] Thomas O. McGarity & Ruth Ruttenberg, Counting the Cost of Health, Safety & Environmental Regulation, 80 Tex. L. Rev. 1997 (2002).
[5] Kevin P. Gallagher, Free Trade and the Environment: Mexico, NAFTA, and Beyond 98 (2004).
[6] Adam B. Jaffee, Steven R. Peterson, Paul R. Portney & Robert N. Stavins, *Environmental Regulation and the Competitiveness of U.S. Manufacturing: What Does the Evidence TellUs?*, 33 J. Econ. Lit. 132, 141 (1995) (table 5).
[7] *Id.*
[8] Richard Parker, *Grading the Government*, 70 U. Chi. L. Rev. 1345, 1401 (2003).
[9] *Id.*
[10] Jaffee, *supra* note 1, at 158.

evidence to support the hypothesis that environmental regulations have had a large adverse effect on competitiveness, however that elusive term is defined."[11]

These scholars are not the only ones to reach this conclusion. Kevin Gallagher (Boston University) notes: "The vast majority of studies have found no systematic evidence that the share of developing country exports and production is becoming more pollution-intensive. In addition, no studies have indicated that there is substantial evidence that pollution-intensive industries flee developed countries with relatively high (and costly) environmental standards)."[12] Similarly, Eban Goodstein (Lewis & Clark College) concludes, "[T]he direct evidence on firm-location decisions and the indirect evidence from the trade-flow literature find precious little support for any significant pollution-haven phenomenon."[13]

It is true that there are gaps in our knowledge and that there may be competitive-regulatory tradeoffs that have not yet been identified. This much is clear, however. Those who claim a regulatory-competitiveness tradeoff are a long way from proving their claim.

II. OMB's Lack of Evidence

OMB recognizes the previous evidence and admits that it does not establish the existence of a competitiveness-regulatory tradeoff.[14] To attempt to overcome this admission, OMB makes three arguments.

The New Research: OMB first observes that economists are studying whether there are some types of industries are more disadvantaged than other industries because of regulatory costs. This weak literature hardly justifies OMB's invitation to all industries to seek regulatory relief. Moreover, if OMB wants to cite potential new evidence in the literature, it should also cite new studies that refute a competitiveness-regulation tradeoff, including evidence that investment in Mexican industry has grown at a time when Mexican regulations were becoming much stricter,[15] consistent with the " Porter hypothesis" that regulation may actually stimulate growth and competitiveness[16]; the fact that growth is positively correlated with pollution reduction within the Los Angeles

[11] *Id.*
[12] Kevin P. Gallagher, Free Trade and the Environment: Mexico, NAFTA, and Beyond 26 (2004).
[13] Eban Goodstein, The Trade-Off Myth: Fact and Fiction About Jobs and the Environment 65 (1999).
[14] Office of Management & Budget, Progress in Regulatory Reform: 2004 Report to Congress on the Costs and Benefits of Federal Regulations and Unfunded Mandates on State, Local & Tribal Entities 53-56 (2004).
[15] Ebru Alpay et al., Productivity Growth and Environmental Regulation in Mexican and U.S. Food Manufacturing, 84 American J. Agricultural Economics 887 (Nov. 2002).
[16] Michael E. Porter, America's Green Strategy, Scientific American (April, 1991), at 168.

area[17]; the intriguing discovery that restrictions on timber harvesting caused by protection of the spotted owl under the Endangered Species Act may have had net benefits for timber companies, by raising the value of their non-protected timber[18]; and the demonstration that some occupational safety and health regulations increase productivity in manufacturing in Quebec.[19]

No Disproportionate Costs: OMB also observes that regulatory reform is justified because manufacturing is a substantial segment of the U.S. economy and regulatory costs are higher for manufacturing industries than other industries.[20] At the same time, however, the manufacturing industry is the source of most of the air and water pollution in this country and many of the safety and health problems to which workers are exposed. Thus, there is nothing disproportionate about this burden if manufacturing produces a large portion of the environmental and occupational problems in the country.

Inapplicable World Bank Study: Lastly, OMB relies on a World Bank report to conclude that national wealth, productivity, and employment rates are all positively correlated with less regulation.[21] The World Bank study, however, does not even concern itself with most of the types of regulations about which OMB is concerned. The World Bank's conclusions are pretty simple: avoid unnecessary interference with competitive markets, enhance property rights, expand technology, reduce court involvement in business matters, and make reform a continuous process.[22] While these general propositions may be worthy of some consideration, OMB's regulatory agenda, as expressed in the latest list of regulations to be reconsidered, is something very different. The World Bank report does not speak to the type of regulations that OMB would like to undo, and OMB's efforts to tie this effort to the report are entirely unpersuasive.

III. Real Priority Setting

OMB's effort to elicit nominations for regulatory revisions should be part of an overall priority setting process that includes an evaluation of where additional regulation is necessary and appropriate. Instead, the process unbalances how regulatory priorities

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[17] Matthew E. Kahn, Smog Reductions Impact on California County Growth, 40 J. Regional Science 565 (Aug. 2000).
[18] Ted W. Chiles, Jr., and Joy Clark, Environmental Regulation and the Spatial Distribution of Capital and Resources, 29 Review of Regional Studies 51 (Summer 1999).
[19] Charles Dufour et al., Regulation and Productivity, 9 J. Productivity Analysis 233 (May 1998).
[20] *Id.* at 47, 49.
[21] *Id.* at 38-43.
[22] There are numerous other problems with relying on the World Bank report. See Testimony of Robert R.M. Verchick Before the Subcommittee on Energy Policy, Natural Resources, and Regulatory Affairs, Committee on Government Reform, U.S. House of Representatives, Hearing on Regulatory Accounting (February 25, 2004), available at http://www.progressiveregulation.org/articles/Verchick_CB.pdf; Letter to Lorraine Hunt, ORIA from Lisa Heinzerling, Georgetown University, and Frank Ackerman, Tufts University (May 20, 2004) (Comments on 2004 OMB Draft Report to Congress), available at http://www.progressiveregulation.org/articles/cost_regs_2004_comments.pdf.

are set in the federal government in favor of the pet projects of regulated industries. Regardless of the merits of such proposals, they must be balanced against the other commitments of regulators, including especially the necessity of protecting people and the environment.

Unbalanced Priority Setting: An appropriate metaphor for regulatory priority setting at any agency is that of a business establishment with a front door, a side window, and a back door.[23] Petitions, information about environmental, safety and health risks in the scientific literature and from health and safety professionals, and information from agency staff all press at the front door, vying for the agency's attention. Meanwhile, OMB is at the agency's back door demanding the agency reconsider some previously enacted rule. At the same time, the courts are pushing some rulemaking initiatives through the side window in response to lawsuits filed against an agency because it is not acted in a timely manner on their requests for a regulation.

What is immediately noticeable about OMB's nomination process is that it is addressed only to the back door. OMB invited nominators to "suggest specific reforms to rules, guidance documents or paperwork requirements that would improve manufacturing regulation by reducing unnecessary costs, increasing effectiveness, enhancing competitiveness, reducing uncertainty and increasing flexibility."[24] There is no similar call to arms about pressing public health and environmental problems. Yet, we know that greenhouse gases, unregulated under federal law, threaten America's future health, productivity, and even national security.[25] We know that asthma, a disease related to urban air pollution, has become the number one childhood illness in the United States.[26] We know that sewage pollution costs Americans billions of dollars annually in medical care, lost productivity, and property damage.[27] Concerning these subjects, OMB has no interest.

Both the nominations and outcome of the process likewise was addressed to the back door of regulatory relief. While 85% of the reform nominations were made by industry, 15% were submitted by public interest groups (Public Citizen and People for the Ethical Treatment of Animals). On the final list approved by OMB, however, 97% of the reforms were industry sponsored and a paltry 3% from the public interest community.

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[23] See Thomas O. McGarity & Sidney A. Shapiro, Workers At Risk: The Failed Promise of the Occupational Safety and Health Administration 188 (1993).

[24] Draft 2004 Report to Congress on the Costs and Benefits of Federal Regulations 1 (February 2004).

[25] *See* Mark Townsend and Paul Harris, Now the Pentagon Tells Bush: Climate Change Will Destroy Us, GUARDIAN (U.K.), Feb. 22, 2004, *available at* http://www.guardian.co.uk/usa/story/0,12271,1153531,00.html.

[26] EnviroHealthAction, Children's Environmental Health, *available at* http://www.envirohealthaction.org/children/asthma/.

[27] Natural Resources Defense Council, Press Release, Aging U.S. Sewer Systems Threaten Public Health, New Report Finds, *available at* http://www.nrdc.org/media/pressreleases/040219a.asp.

A Real Process: Instead of an ad hoc process, OMB should require agencies to consider regulatory reform requests in the context of an agency's annual regulatory plan.[28] This would give an agency the opportunity to consider such back-door requests in the context of what other business is at the front and side-doors. Even if back-door requests to modify existing regulations are valid, this plan gives an agency the opportunity to place such request within the hierarchy of all agency business, some of which is likely to be more pressing than such requests.

Shrinking Agency Budgets: A more organized and efficient priority setting process is not only good management, it is essential at a time when agency's budgets are shrinking, as they have been for years.[29] Agencies simply cannot get to all of the business on their plates. In this context, a decision to emphasize only the back-door, as OMB has done, constitutes a politicization of the priority-setting process, because it elevates the modification of existing regulations over the introduction of new regulations without carefully considering whether the business at the front or side doors is of higher priority.

Politicization of Priority-Setting: Finally, but hardly least of all, OMB's flawed nomination process must be understood in the context in which it is occurring. The Bush administration is engaged in an all-out effort to centralize control over the regulatory process in the White House.[30] The White House has a legitimate interest in management of the federal bureaucracy, but the administration's micro-management of the government creates two undesirable side-effects. First, White House micro-management gives regulated industries substantial and unaccountable influence over the regulatory process. The millions and millions of dollars that industry donated to the President's reelection campaign gives industry lawyers and officials substantial access to the White House to seek regulatory relief. Needless to say, the public lacks similar access to balance out the process. Second, White House micro-management is unlikely to improve decision-making because it elevates the role of political officials and generalists and decreases the role of agency experts and persons more familiar with regulatory problems.[31]

IV. The Small Business Excuse

OMB seeks to justify its nomination process on the need to alleviate the regulatory burden on small business. While small business is deserving of special consideration

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[28] *See* Exec. Order 12,866, §3(c).

[29] The Administration, for example, has proposed a $450 million dollar cut in EPA's budget. Center for American Progress, Making the Wrong Choices: An Analysis of the President's 2006 Budget, at 9, available at http://www.americanprogress.org/atf/cf/{E9245FE4-9A2B-43C7-A521-5D6FF2E06E03}/Wrong%20Choices%20An%20Analysis%20of%20the%202006%20Budget.pdf.

[30] *See* Paul Singer, By the Horns, National Journal, May 26, 2005, at 898.

[31] Sidney A. Shapiro, Political Oversight and the Deterioration of Regulatory Policy, 46 Admin. L. Rev. 1 (1994).

from regulators, it already receives such consideration. Moreover, very few of the OMB final hit-list recommendations appear to address small business concerns.

Solicitude for Small Business: The small business community is a major source of innovation and employment in this country. Like their larger counterparts, however, small businesses are also responsible for social ills addressed by regulations[32] Workers at small firms, for example, are injured by workplace accidents or exposed to toxic chemicals. Additionally, small firms are a not insignificant source of environmental pollution. Thus, there is a valid need to protect the public and the environment from harm caused by small businesses. At the same time, it can be more relatively more expensive for small business to comply with regulations than large companies, which creates a need to find ways to both protect the public and lower the cost of regulation for such businesses.[33]

This, however, has already been done. Small firms receive direct government subsidies such as outright and government guaranteed loans from the Small Business Administration (SBA) as well as indirect preferential treatment through federal procurement requirements and tax provisions.[34] Additionally, small business is treated to many exemptions or special treatment in the area of regulation. For example, employers with less than 15 people are exempt from the Equal Employment Opportunity Act,[35] and OSHA levies lighter penalties for smaller firms, exempts businesses with less than 10 people from recordkeeping requirements, and provides free on-site compliance consultations.[36]

Perhaps more importantly, small business has its very own law, the Small Business Regulatory Enforcement Fairness Act (SBREFA) that requires agencies to give special consideration and voice to small business as part of the rulemaking process as well as expanded judicial review for small businesses wishing to challenge agency decisions.[37] Nonetheless, small business continues to object to any regulation perceived as burdensome even when it has completed the SBREFA screening and input process.

Big-Business Orientation: Even assuming that the nomination process is necessary to ensure proper attention to the concerns of small businesses, very few of the final hit-list recommendations appear to address small business concerns. Of the 71 final reforms, 11 purport to focus all or in part on small business. This tally was made by counting final reforms either recommended by the SBA or whose description mentioned alleviating a

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[32] Richard J. Pierce, Jr., *Small is Not Beautiful: The Case Against Special Regulatory Treatment of Small Firms*, 50 Admin. L. Rev. 537 (1998).
[33] C. Steven Bradford, *The Cost of Regulatory Exemptions*, 72 UCMK L. Rev. 857 (2004).
[34] See Richard J. Pierce, Jr., *Small is Not Beautiful: The Case Against Special Regulatory Treatment of Small Firms*, 50 Admin. L. Rev. 537 (1998).
[35] 42 U.S.C. §2000e(b) 2005.
[36] OSHA Small Business Benefits, http://www.osha.gov/dcsp/smallbusiness/benefits.html.
[37] 5 U.S.C. §601 et seq. 2005.

small business burden. Many of those requests, however, were joined by a number of other petitioners representing large corporations as well.

Consider, for instance, reform #188, a request to rescind the rule controlling listeria in ready to eat lunch meats, was made by SBA as well as the National Association of Manufacturers. Rescinding the rule would affect all manufacturers, not just small ones, leading to the conclusion that big businesses (as well as small businesses) are attempting to dilute an important health control. This is not surprising given industry's influence in weakening the listeria rule from its original proposal.[38] Ironically, OMB lists the listeria rule as having annual benefits of $44-$154 million and costs of only $16 million and touted it as a "regulatory reform accomplishment" as recently as December.[39] Moreover, the rule to which the objection is being made is an interim-final rule and USDA is already considering whether to modify the rule.[40] The nomination appears to be entirely superfluous except as a signal from OMB to weaken the existing rule.

Thus, while regulations affecting small business merit evaluation, this already occurs via the SBREFA process as part of rulemaking. Additionally, regulation of small is business is important as small business is responsible for a disproportionate share of environmental pollution, worker injuries and racial discrimination compared to larger firms.

V. The Reform Masquerade

No one should object to an effort to make it less costly to meet existing levels of regulation, assuming that the changes lead to the same level of regulatory protection. Many of the nominations, however, seek to reduce the level of regulatory protection of people and the environment.

Same Protection, Less Cost: Some of the nominations address this objective. For instance, nomination #34 recommends using common identifiers for all EPA databases and #10 recommends eliminating duplicative energy appliance labeling. These appear to be valid suggestions and true "housekeeping" measures as characterized by the U.S. Chamber of Commerce.[41] Others, following OMB criteria to reduce uncertainty, request agencies to clarify rules or standardize procedures.[42]

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[38] See Consumer Federation of America, *Not Ready to Eat*, Dec. 2004 http://www.consumerfed.org/CFA_Not_Ready_to_Eat.PDF.

[39] OMB, 2004 Report to Congress on the Costs & Benefits of Federal Regulation, at 21 & 111. http://www.whitehouse.gov/omb/inforeg/2004_cb_final.pdf, and see OMB Watch, *White House Adds Rule to Hit List After Calling it 'Accomplishment.'* http://www.ombwatch.org/article/articleview/2770/1/331 (Apr. 4, 2005).

[40] *Id.*

[41] Cindy Skrzycki, *OMB to Reconsider Some Rules*, Washington Post, E01 (Mar. 22, 2005).

[42] *See e.g.* Regulatory Reform, *supra* note 1, at #7 (clarify security requirement overlaps) and #175 (standardize drawback recordkeeping requirements).

Less Protection: Corporations, however, used the nomination process to seek outcomes that would result in less protection of people and the environment. For instance, Deere and Company recommended privatizing all government regulatory activities, and the National Association of Manufacturers suggested that the US Fish and Wildlife Service should "work with Congress to tighten the [Endangered Species Act] so that it must use mainstream science to evaluate species for listing."[43] Similarly, the Copper and Brass Fabricators Council objected to industrial storm-water regulations under the Clean Water Act (CWA) that actually required collection and treatment of storm-water runoff because it cost more than non-technology methods.[44]

Privatizing an entire public function, changing a statutory standard for use of science, and objecting to CWA requirements to ensure less polluted runoff are clearly outside the scope of such a housekeeping exercise, and yet OMB's call for reforms presents the perfect opportunity to lobby for such changes under the guise of regulatory reform. Fortunately, OMB rightly rejected the above referenced nominations, but only after valuable agency resources were spent reviewing such unreasonable and out of place suggestions.

Other nominations that seek to weaken regulatory protections did, however, make the final hit-list. For example, the American Public Power Association recommends that EPA does not need to regulate cooling water intakes structures at electric utility generating plants with capacity of <50 million gallons a day (MGD) for reduction of fish entrainment and impingement under the CWA because such standards are "unlikely to yield net benefits ..."[45] Moreover, since this nomination addresses an ongoing rulemaking under CWA §316(b),[46] it is not a look-back nomination at all. In this circumstance, this appears to be another signal from OMB to EPA to adopt a weaker regulation.

Several attacks on EPA's Toxics Release Inventory (TRI) are a second example of the desire to weaken regulatory protections disguised as regulatory reform.[47] TRI is widely supported as a useful and important regulatory program. Environmentalists like TRI because it supports the public's right to know about the toxic substances to which they are exposed. Conservatives like TRI because, as Donald Elliot observes, "disclosure of TRI data to the public has been a powerful incentive to promote 'voluntary' pollution reductions."[48] Nonetheless, complaining about TRI imposed burdens is a favorite

[43] *Id.* at #2 and #132.
[44] *Id.* at #115.
[45] *Id.* at #68.
[46] See http://www.epa.gov/waterscience/316b/basic.htm.
[47] *See e.g.* Regulatory Reform, *supra* note 1, at #43 and #52.
[48] E. Donald Elliott, *Environmental TQM: Anatomy of a Pollution Control Program that Works*! 92 Mich. L. Rev. 1840, 1851 (1994).

pastime of some industry groups,[49] and so it is no surprise that the nominations made the final hit-list.

The first complaint regards the lowering of the TRI reporting threshold for lead to 100 pounds from 10,000 pounds because it affects many small businesses and small lead emitters. However, the rule was promulgated because lead is a persistent bio-accumulative toxic that is dangerous even at low levels and little information is available to local communities regarding lead emissions.[50] Yet, at the behest of industry, OMB has deemed that the recommendation merits further action.

Similarly, a number of petitioners simply want all use of material reporting thresholds increased. Again, these requests go to the substantive basis of the TRI program that was designed by Congress to provide important information to the public on the cumulative amount of toxics used and released. Further, the request appears to be redundant as the procedural component of this complaint regarding reporting forms is already being addressed through EPA's TRI Burden Reduction Rule in which industry has been an active participant.[51]

New Protections Ignored: Finally, responses to the nominations submitted by public interest groups were practically nonexistent and reveal the continued bias of OMB against true reforms that would actually provide benefits to a wide swath of society as opposed to one special interest sector. For instance, as mentioned above, while 15% of the reform nominations were submitted by groups working to improve regulations to protect the public, only 3% of the final action items addressed public interest submissions, with the rest all responses to industry concerns. Moreover, of the two public interest nominations surviving on the final list, only one had a substantive action item.[52] In response to Public Citizen's nomination to establish an occupant vehicle ejection standard, OMB provided a timeline for rulemaking. In contrast, DOT will provide a summary of research in the area of vehicle compatibility standards in response to the one other public interest nomination on the hit-list. Thus, two out of 71 reform nominations address public interest concerns, and only one of those actually pledges any real action.

Meanwhile, there are plentiful environmental and public health and safety issues that remain unaddressed by regulation. For instance, important consumer protections to

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[49] *See e.g.*,Testimony of Todd McCracken, President, National Small Business Association, House Government Reform Subcommittee on Energy Policy, Natural Resources, and Regulatory Affairs Nov. 17, 2004), available at http://www.nsba.biz/docs/todd_11-17_testimony.pdf.

[50] See US EPA, *New TRI Reporting Requirements for Lead and Lead Compounds* http://www.epa.gov/tri/lawsandregs/lead/pb_fact_sheet.pdf.

[51] See US EPA, Burden Reduction Stakeholder Meeting http://www.epa.gov/tri/programs/stakeholders/TRIburdenreductionmeetingsummary_oct192004.pdf, and OMB Watch comments http://www.ombwatch.org/article/articleview/2728/1/241?TopicID=3.

[52] Regulatory Reform, *supra* note 1, at #18 and #22.

prevent auto vehicle deaths such as establishment of a rollover crashworthiness standard and coverage of 15-passenger vans by NHTSA safety standards, both proposed by Public Citizen were left off the final list despite the fact that motor vehicle deaths are the leading cause of death for Americans aged 4 to 34. Likewise, other recommendations to protect citizens from mad cow disease, meat fecal contamination and workers from ergonomic injuries and beryllium exposure were likewise rejected despite the need for "reform" in these areas.

Mrs. MILLER. I have a question for Ms. Luchak, if I might. I was interested to hear you speak for the need for transparency from some of the agencies as they are going through their process there. And I thought you were sort of indicating that some of these decisions are essentially being made almost behind closed doors, I suppose, when they are bringing forth all the different information gathering. It certainly creates uncertainty, I would imagine, for your industries and others.

Do you think that the process negatively impacts your ability as an industry to be creative—I am sure you are always very innovative and looking for new processes and new types of products within your industry. Does rulemaking impact that negatively by not having transparency about the kinds of things they are looking for?

Ms. LUCHAK. Yes. I believe that we know our industry is the best, and there may be input that we could provide before they get well along the way that could, you know, be very helpful in, you know, making up a rule. I know with Title 5, you know, the first thing they thought of was putting after-burners on, but within our industry, we knew there was a lot of other things that could be done, like low styrene resin is possible, which did come about. Controlled spray really reduces emissions. There are a vast amount of things that you can do that—you know, just by not being in the industry you would be unaware of.

Mrs. MILLER. Thank you.

Dr. Duesterberg, if I could, and as we talked in this subcommittee hearing today, we keep going back to the 22 or 23 percent of the structural costs for the manufacturing industry in America, and a lot of different dynamics, as you mentioned, are in that study, certainly, besides regulation. And you mentioned here that regulation by litigation is sort of a creeping phenomena, and I think you said that you have had some experience, I guess what I am asking, if you could cite examples, are there some States that there are locals, municipalities, that are actually hiring these trial attorneys to try to rulemake themselves in this way? That's the first time I have really heard of this phenomena, as you say, regulation by litigation. So I am interested to know what you mean by that.

Mr. DUESTERBERG. Well, the gun industry is the current target. There have also been cases with regard to the food processing industry, which you mentioned. There have been cases with regard to the pharmaceutical industry as well.

The point that we would like to make is simply that this bears a lot of scrutiny on the part of the Congress. None of the gun industry suits so far, as far as I know, have succeeded. None of the fast-food industry cases, as far as I know, have succeeded. But there's a lot of money on the part of the trial bar to invest in cases like that, and they are so investing.

So I think it just bears watching on the part of the Congress, especially since I believe it involves the jurisdictional issue, if you will, that you should be aware of.

Mrs. MILLER. I appreciate that. Actually the House did pass some legislation in regards to the gun industry, as you were speaking of that. And in regards to the food industry, I think we call it the cheeseburger bill, where you had a—we had quite a bit of con-

sternation, certainly expressed on behalf of the restaurant association.

You also mentioned different regulatory costs associated with several key elements. You mentioned energy, telecommunications, corporate governance. I am just wondering, of the three, do you have any idea of or observation of which of them you think might present the greatest challenge to the manufacturing industry?

Mr. DUESTERBERG. Well, Assistant Secretary Frink mentioned Sarbanes-Oxley. That's certainly on the radar screen of almost every senior management executive today, because they are having to come into compliance, and it's taken a good deal more of their effort and time than they had anticipated, as well as money. And also the guidance given by the PCAOB and the Big Four audit firms has been internally inconsistent, and so they frequently will have problems knowing exactly what the standard is that they are supposed to meet.

But that being said, I think the other major issue is natural gas costs. We have tripled natural gas costs in this country since the late 1990's. Again, it's partly because of the increase in demand, but demand use in natural gas was favored for a number of regulatory actions; production was constrained.

There are certain industries, chemicals, plastics, glass, paper, fertilizer industry, which have been severely hit because they use some gas as a heat source, but also as a feedstock in many cases. This is an issue that I think can be addressed, and there are ways to meet the increased demand. There could be substitution, for instance, of other energy resources for electricity production, because one of the major areas of increase for natural gas use has been in the production of electricity. So if we could figure out ways to move electricity into other sources, both traditional like nuclear and coal, but nontraditional wind energy, for instance, as well, then that would be very helpful to this case. And I mentioned the regulation of the siting of LNG import facilities is something we think could be of immediate assistance.

Mrs. MILLER. Well, the energy bill, as you know, will be coming to the floor of the House, I think, next week, perhaps, I am not quite sure, but soon, and it's interesting, as you mentioned—I know we are talking about regulation today, but in my State of Michigan, I don't think we have had a new electrical grid built there for over 20 years because of some of the different situations that we have had.

In fact, again, I know we are talking about regulation, but my final question would be to you, you did mention about a lot of the different challenges from some of the other countries, China, India, some of these emerging nations, with their manufacturing sector. In Michigan, actually, our largest trading partner is Canada. It's our largest trading partner. We have a lot of consternation about how NAFTA is being enforced.

I just wonder as an association whether or not you have any observations about some of the trade agreements that we have, how that might impact some of the regulatory burdens that we have, or if you have taken any positions on some of the upcoming trade agreements, or generally are we enforcing our trade agreements as we should be?

Mr. DUESTERBERG. Well, we are generally in favor of trade-opening measures. That being said, it is important for our trading partners to enforce the obligations which they take on in joining these agreements. That has not always been the case. We focused a lot on China because it's the growing source of competition, and there are clear examples which the Trade Representative chronicles each year; it took 60 pages, I think, to go over China in their annual report to the Congress. They haven't enforced their intellectual property rights, some of the rights of companies to set up operations, distribution operations and the like.

With regard to Canada, I don't have any specific examples where I think there is a major issue there. There are irritants of all sorts, but these are being litigated through the NAFTA dispute settlement procedures and sometimes the WTO. So I think we are addressing those issues that we had with Canada. We should probably be doing more to address issues with China and some of the other trading partners.

Mrs. MILLER. Thank you.

I will recognize the ranking member, Representative Lynch.

Mr. LYNCH. Thank you, Madam Chairwoman. I just want to thank each of you for your testimony here this morning.

Dr. Duesterberg, actually, I am right in the middle of a process now trying to get an LNG facility, an offshore facility, approximate to Boston Harbor, which I represent, so I can certainly understand and agree with your assessment of that whole process. It's been painful.

Ms. Luchak, I think you have come up with some very solid, rather straightforward proposals in terms of having a seat at the table early on, and having a transparent process, and having accurate information, things that I believe could really help this process, and I want to thank you for taking your time to testify today, and I think you added a lot to the hearing.

Mr. Shapiro, I do want to ask you a couple of questions. As someone who worked, has worked, for 20 years in the manufacturing industry, isn't there a reason that I heard a lot of complaints today, or concerns today, about the heavy level of regulation in manufacturing? But considering my surroundings, when I worked at U.S. Steel and Inland Steel, and working at blast furnaces, and even working at, you know, a General Motors facility, isn't there a reason that, you know, the regulations regarding worker safety and environmental impact are targeted in some respects more to manufacturing than to clerical or any other industries?

Mr. SHAPIRO. Certainly, Congressman, it is among our most dangerous industries in terms of occupational health and safety, along with logging and construction. And that's actually part of a more general problem.

Certainly these cost figures are overwhelming. They are staggering, indeed, when you look at the amount of cost of some regulations, and that should give us pause. And if we can find cheaper ways to do things, by all means we ought to do it. But under an economic methodology, one would also have to look at the benefits which are generated by these regulations, and that's the trouble with these figures about how much money the manufacturing in-

dustry is paying in terms of regulatory costs. You also have to compare that to the regulatory benefits.

Now, OMB, in its draft 2005 report to Congress, totals up aggregate benefits of all regulation and aggregate costs. And aggregate benefits, OMB says, are somewhere between $12.6 and $108 billion as against the regulatory costs of $3.8 to $4 billion. So there's enormous aggregate benefit that the American public and the environment get from these regulations. Now, that doesn't mean that individual regulations are necessarily reasonable or sensible. We do need to look at individual regulations. But over all, we get enormous benefit for these many, many dollars that we also have to pay.

Mr. LYNCH. Thank you.

The last question, actually, follows up on that. We are responsible here with trying to assess what the costs and benefits are, and a lot of the information that we get in terms of studies and reports are somewhat outdated, and I spoke of that with the earlier panel. This Crane and Hopkins study, I am not sure if you are familiar with that.

Mr. SHAPIRO. Yes.

Mr. LYNCH. It is one of the older ones. Do you agree because they are the ones you speak of who make this aggregate cost estimate, do you see underlying problems with that particular study?

Mr. SHAPIRO. This is very hard to do. OMB itself does a Herculean task to try to report to the Congress each year its own costs and benefits, and in the course of doing that, they explain time and time again the difficulty of coming up with these figures.

Professor Hopkins' figures have been around for a long time, and OMB has already said that it basically can't use them when it itself tries to attempt to collect these costs and benefits, because they are drawn from various sources, and they are very general.

The other problem with them is there is a group of figures dealing with paperwork costs, dealing with tax compliance costs, dealing with regulatory costs, even dealing with transfer costs, like farm subsidies. So it's very hard to pick out of these figures, for purposes of blaming one thing, which of these various sources are feeding into that. So I think they have tried to do their best, but this is at best a guess, I think, by them as to these totals.

Mr. LYNCH. OK. Thank you, Mr. Shapiro.

Mrs. MILLER. Thank you very much.

I certainly again want to thank all the witnesses for their wonderful testimony and their input. It is a very complicated issue, and certainly as the committee and the Congress struggles forward, tries to move forward positively, we want to continue to create an environment where we can have—incentivize business to invest and to create new jobs, etc., here in the American manufacturing industry, and we look at how these regulations certainly impact manufacturers, both positively and negatively.

So again we thank you very, very much for your testimony, and with that, we will adjourn the meeting.

[Whereupon, at 12:06 p.m., the subcommittee was adjourned.]

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