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COST-JUSTIFYING REGULATIONS: PROTECTING JOBS AND THE ECONOMY BY PRESIDENTIAL AND JUDICIAL REVIEW OF COSTS AND BENEFITS

HEARING

BEFORE THE

SUBCOMMITTEE ON COURTS, COMMERCIAL AND ADMINISTRATIVE LAW

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

FIRST SESSION

MAY 4, 2011

Serial No. 112–48

Printed for the use of the Committee on the Judiciary

Available via the World Wide Web: http://judiciary.house.gov

U.S. GOVERNMENT PRINTING OFFICE

66–156 PDF WASHINGTON : 2011

For sale by the Superintendent of Documents, U.S. Government Printing Office
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COST-JUSTIFYING REGULATIONS: PROTECTING JOBS AND THE ECONOMY BY PRESIDENTIAL AND JUDICIAL REVIEW OF COSTS AND BENEFITS

WEDNESDAY, MAY 4, 2011

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COURTS,
COMMERCIAL AND ADMINISTRATIVE LAW,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to call, at 3:08 p.m., in room 2141, Rayburn Office Building, the Honorable Trey Gowdy (Vice-Chairman of the Subcommittee) presiding.

Present: Representatives Gowdy, Gallegly, and Cohen.

Staff present: (Majority) Daniel Flores, Subcommittee Chief Counsel; John Hilton, Counsel; Ann Hawks Woods, Counsel; Cecilia Daly, Counsel; Allison Rose, Professional Staff Member; Ashley Lewis, Clerk; (Minority) James Park, Counsel; and Susan Jensen-Lachmann, Counsel.

Mr. GOWDY. The Subcommittee will come to order. I want to welcome and thank all of our witnesses, acknowledge Mr. Cohen, and I believe Mr. Gallegly is on his way.

Today is going to be somewhat unusual with vote schedules, and we want to be sensitive to your individual schedules as well. Mr. Cohen and I are going to waive our opening statements. And, Mr. Graham, I think you may have a plane to catch, so if your compatriots are okay with it, we may let you do your opening statement, direct any questions that may be applicable to you, and then handle the other three witnesses, unless there is vigorous opposition to that.

I think I need to swear the witnesses, which in my other job somebody else did in a black robe. So, let me see if——

Mr. COHEN. They do not have to be sworn.

Mr. GOWDY. They do not?

Mr. COHEN. No, it is not like in a——

Mr. GOWDY. Good. Fine with me.

All right. Let me introduce John Graham, who is the dean of the School of Public and Environmental Affairs at Indiana University, one of the largest public policy schools in the United States. Dr. Graham has a bachelor's degree in politics and economics from Wake Forest University, a master's degree in public affairs from Duke University, and a Ph.D. in urban and public affairs from Car-

negie Mellon University. He is the author and editor of numerous books, articles, and academic papers. From 2001 to 2006, Dr. Graham served as the administrator of the Office of Information and Regulatory Affairs in the Office of Management and Budget. With that, Dr. Graham, we would welcome you for your opening statement?

TESTIMONY OF JOHN D. GRAHAM, Ph.D., DEAN OF THE SCHOOL OF PUBLIC AND ENVIRONMENTAL AFFAIRS, INDIANA UNIVERSITY

Mr. GRAHAM. Thank you, Mr. Gowdy, and thank you to everyone in the room for your flexibility in allowing me to get back to my flight.

Our topic is benefit-cost analysis and its role in Federal regulatory decision making. Let me start by saying that this topic has an interesting bipartisan history, and in the literature, there is some conflict on where it actually begins in American political debate. My own view is the most important starting point was President Jimmy Carter, a small businessman himself who urged and assembled his White House economists to begin looking at regulations, and he also championed the Paperwork Reduction Act, which ultimately established the office in OMB that has a central role in this area.

Ronald Reagan's impact, of course, cannot be underestimated. This the President who established the process of OMB review of regulations with cost-benefit analysis being a central element.

President Clinton reaffirmed a lot of these basic strategies and, I think importantly, focused the efforts on the most significant of the Federal rules so that the effort around analysis and economics would be concentrated.

I worked for President George W. Bush. He made strong efforts to improve information quality and peer review as it relates to cost-benefit analysis. And I am very pleased that President Obama has reaffirmed the importance of cost-benefit analysis in the regulatory process.

So, this raises the following question: if all of these Presidents are in agreement that cost-benefit analysis is important, it should be part of the regulatory process, why would people be considering legislation where Congress would require agencies to move in this direction? And I think there are two basic answers to that question.

One is that a President's political preferences sometimes get in the way of the basic good government principle at looking at the benefits and costs of regulatory action. And I will give you as an illustration the President I worked for.

After 9/11, the political imperative to pass Homeland Security regulations was overwhelming. And I must admit there were many regulations submitted to me as OIRA administrator under the banner of homeland security that were fairly expensive and fairly intrusive. Can I testify to you that each and every one of these was subject to a careful, cost-benefit analysis that looked at less expensive alternatives? To be honest with you, we did the best we could under the circumstances, but a President does not always want to go forward with the cost-benefit test when they have other political

reasons to want to support another activity. As a result, we quantified by 2004 that half of the cost of all new regulations in the Federal Government were due to Homeland Security regulations.

My own view is if Congress had required us to do cost-benefit analysis of these regulations and it had been judicially enforceable, you would have given the airline industry, the colleges and universities who were impacted by these regulations, an ability to put reasonable pressure, not undue pressure, on the Federal Government to make sure that these regulations were necessary and worthwhile.

So, the first reason that we need legislation is that presidential preferences do not always lead to faithful implementation of the cost-benefit requirement in these executive orders.

The second reason is that the career staff at the agencies and OMB are human beings, and they are imperfect. And they develop regulations and promulgate them oftentimes without adequate economic and scientific basis. If, however, you have an enforceable check in court against the quality of their work, their incentive to do that work increases substantially. And as a consequence, there is a large body of literature showing the limitations of the existing—the quality of the existing activity.

So, what should be the basic components of any kind of cost-benefit mandate of legislation in this area? One, it seems to me all cabinet and independent agencies should be subject to this type of benefit cost requirement. My own view is you should just start with the principles in the Clinton-Gore executive order in 1993, codify them unless there is a compelling reason to use other language.

Second of all, I think this should be applied not only to regulations, but to so-called guidance documents that are really rules in their actual practical effect on businesses and on state and local governments.

Third, I think it needs to be a judicially enforceable requirement; otherwise, you have not done anything different than what the Presidents have already done by issuing an executive order requiring cost-benefit analysis.

And finally, it needs to be a benefits-justified cost test to make sure that the executive branch can account for qualitative factors as well as the quantitative benefits and costs.

So, I have given you some examples of the kinds of things that should be in there. Let me conclude by saying cost-benefit analysis, like accounting and other tools, can be gamed. There is a garbage in/garbage out problem that needs to be worried about. There are ways to address this in the legislation by requiring OMB to issue technical guidance on how to do benefit-cost analysis, and by referencing the information quality and peer review requirements that OMB has already adopted.

So, in short, I think that really cost-benefit analysis as a tool, as part of a process of regulation is a good government principle. There are times when Presidents would prefer not to follow good government principles for whatever reason. The regulated communities, whether they be business or state and local governments, need to have safeguards in situations when the executive branch does not adhere to these principles.

Thank you very much for the opportunity to be here today.

[The prepared statement of Mr. Graham follows:]

Prepared Statement of John D. Graham, Ph.D., Dean,
Indiana University School of Public and Environmental Affairs

INTRODUCTION

My name is John D. Graham, Ph.D. I am currently Dean of the Indiana University School of Public and Environmental Affairs—SPEA (Bloomington and Indianapolis, Indiana). SPEA is one of the largest public affairs schools in the United States and has graduate programs that are ranked in the top five by US News and World Report and by the National Research Council/National Academy of Sciences. Prior to joining IU in 2008, I served as Dean of the Frederick Pardee RAND Graduate School in Santa Monica California (2006–8), as Administrator of the White House Office of Information and Regulatory Affairs in the U.S. Office of Management and Budget (2001–2006), and as tenured Professor of Policy and Decision Sciences at the Harvard School of Public Health (1985–2001). For twenty-five years, I have taught the analytic tools of risk analysis and benefit-cost analysis in the classroom and published research on the application of these tools to health, safety and environmental issues. In fact, my doctoral dissertation at Carnegie-Mellon University (1983) was a benefit-cost evaluation of automobile airbag technology. While my testimony today draws on my academic expertise, it also draws on my experience at OMB, where I supervised a staff of fifty career policy analysts as they reviewed benefit-cost analyses performed by Cabinet agencies such as the Department of Labor, the Environmental Protection Agency, the Department of Homeland Security and the Department of Transportation. I am honored to have the opportunity to express my opinions on how benefit-cost analysis can be used more effectively to improve the federal rulemaking process. The views I express are strictly me own, and do not necessarily represent the views of SPEA or Indiana University.

TERMINOLOGY

With respect to terminology, the phrases "cost-benefit analysis" (CBA) and "benefit-cost analysis" (BCA) are synonyms and thus can be used interchangeably. I prefer the phrase BCA because it reminds students and policy makers that this analytic tool is aimed at increasing the benefits of regulations as well as reducing unnecessary costs. (B also has the alphabetical advantage over C!) When regulatory options are compared, a BCA tells us which option produces the largest surplus of benefits minus costs (assuming all benefits and costs can be quantified in monetary units). When only some benefits and costs can be quantified (or monetized), the net-benefit surplus (or deficit) is reported but the decision maker is also informed of any important benefits and costs that could not be quantified. After considering both benefits and costs (quantitative and qualitative), OMB instructs agencies to make a determination as to whether the benefits of a rule justify the costs, compared to doing nothing and compared to other viable regulatory options.

The phrase "cost-effectiveness analysis" (CEA) refers to a close analytic cousin of BCA. With CEA, the measure of effectiveness is expressed in physical units (e.g., lives saved or tons of pollution prevented), and the outcome of a CEA is the best option indicated by "bang for the buck" (e.g., the regulatory alternative that saves the most lives given a budget constraint, or the alternative that achieves an environmental goal at minimum cost to society). It is sometimes useful for agency analysts to conduct a CEA in addition (or instead of) a BCA, especially if the benefits of the rule are difficult to quantify in monetary units.

BIPARTISAN SUPPORT FOR REGULATION INFORMED BY BCA

The origins of BCA in federal regulatory policy are a matter of some academic debate but the push for cost-justified regulations goes back at least to the administration of President Jimmy Carter. As a small businessman, President Carter knew that the costs of regulation were a serious national problem and he deployed White House economists in a determined effort to reign in business regulations that were too costly. President Reagan went further and placed OMB in the driver seat during interagency reviews of the BCAs or CEAs prepared by federal agencies. President Clinton reaffirmed the legitimate role of benefit-cost analysis in regulatory decision making while focusing OMB's efforts on a smaller sample of significant rules and recognizing the primacy of agency policy discretion. President George W. Bush largely reaffirmed the benefit-cost language in the Clinton Executive Order and I interpret President Obama's position on BCA in regulatory policy to be largely consistent with the positions espoused by previous presidents of both parties. Thus, al-

though there are some advocacy groups and legal academics who oppose the use of BCA in federal regulatory policy, I think it is fair to say that recent Presidents of both parties have expected agencies to prepare benefit-cost analyses and use the insights from those analyses when making regulatory decisions.

I would also like to point out that leading members of Congress from both political parties have been consistent advocates of a stronger role for BCA in federal regulatory policy. For example, Senator Carl Levin (D–Michigan) and Senator Orrin Hatch (R–Utah) have been pioneers of BCA proposals in the Senate. Much can be learned by reviewing the relevant speeches and legislative proposals of these members for the last twenty years.

MYTHS ABOUT BCA

In my testimony today I would like to dispel some popular misconceptions about BCA. Much of my testimony about myths draws on a comprehensive article, "Saving Lives through Administrative Law and Economics," University of Pennsylvania Law Review, 157(2), December 2008, 395–540 that I have made available to subcommittee staff and would like to have inserted in the record of this hearing.

Myth #1: It is not feasible to quantify the benefits of public health, safety or environmental regulations.

Due to thirty years of progress in public health science, environmental science, risk assessment, and health/environmental economics, it is now feasible to produce (at least approximate) estimates of the benefits of federal health, safety and environmental regulations. The validity of benefit estimates varies depending on the quality of science used by federal agencies. For example, the projected number of lives saved by DOT's mandatory airbag regulation (1977) was estimated based on laboratory crash tests with cadavers, observed rates of safety belt use, injury surveillance data from police reports and hospital records, and engineering judgment. Based on more than 30 years of real-world experience with the airbag regulation, we now know that the safety benefits are smaller than projected by regulatory analysts but benefits are still large enough to justify the extra investment in airbag technology. In contrast, EPA's air pollution regulations have been shown to have higher public health benefits than previously thought due to better understanding of how the rate of premature death rises in a community due to the inhalation of soot and smog. As rates of urban air pollution have declined, the trends in mortality rates from chronic diseases (age adjusted) have been downward. Today, some of the best analytic work on the benefits of federal regulations is performed by analysts at the U.S. Environmental Protection Agency. While the benefits of federal regulations are sometimes overestimated and sometimes underestimated, there is no evidence that use of BCA causes any systematic bias in the estimates of benefits prepared by federal agencies.

Myth #2: It is unethical to consider costs when making regulatory decisions about medicine, public health, safety, and environmental protection.

The notion that "safety" or "protection" from harm is an absolute right, regardless of costs, is not defensible on either philosophical or practical grounds. Philosophically, complete safety (also called "zero risk") is an illusion because well-informed citizens choose, on a daily basis, to assume many risks in life in exchange for a variety of benefits (e.g., we reduce travel time by driving faster on four-lane highways than we do on two-lane roads). When risks are imposed on citizens without their explicit consent (e.g., when a pedestrian inhales pollution emitted by a car), the philosophical analysis is more difficult but the ethical solution is not necessarily a mandate for zero risk. A more compelling resolution is that regulators should protect citizens from imposed risks to whatever extent the affected citizens would prefer, assuming those affected citizens were to experience both the benefits and costs of the regulation. Philosophically, this is a standard of hypothetical informed consent, and it forms the ethical foundation of BCA. To reject the informed preferences of citizens in favor of absolute safety is a form of authoritarianism—an ill-considered rejection of the ideals of personal freedom and consumer sovereignty that are at the heart of democratic capitalism. The practical objections to zero risk are even more compelling. If regulators go so far in the pursuit of complete safety that they make families poorer (e.g., through higher prices for regulated, zero-risk products), there may be more imposed risk from the induced poverty than from the target risk that regulators seek to eliminate. For example, many regulations in the energy sector have the practical effect of raising the prices of gasoline at the pump. For many low-income households, rising gasoline prices have adverse ramifications for all aspects of welfare (including health). Thus, practical considerations favor some form of benefit-cost determination rather than blind pursuit of zero risk.

Myth #3: BCA is a mathematical straight jacket that prevents consideration of important qualitative values such as fairness and special concern for the welfare of children.

The falsehood here is the assumption that a benefit-cost determination may be based only on a numerical comparison, without consideration of qualitative values such as fairness and the special needs of children. It is well-accepted in the field of BCA that, while many benefits and costs can be quantified, some valid considerations are essentially intangible. BCA textbooks call for intangible benefits and costs to be disclosed by analysts and considered by regulators. For example, suppose that a federal regulation will reduce the rate of lead poisoning among children in poor urban communities. Assume further that the quantified benefits and costs of this regulation are roughly equal, without considering the fact that low-income children are the primary beneficiaries. A fairness argument can be made that a tie-breaking, intangible consideration favors the regulation: the notion that the federal government owes a special sense of fairness to low-income children who are less able than middle-class or wealthy adults to protect their own interests. Notice that this legitimate, fairness consideration may not be as compelling if the costs of the regulation are also borne by low-income families. In other words, a benefit-cost determination is not a mathematical straight jacket the prevents analysts and regulators from giving weight to compelling intangible considerations.

Myth #4: BCA of business regulations is biased against regulation because the costs of regulations are exaggerated and the benefits of regulation are understated.

For a variety of reasons, it is sometimes asserted that analysis of business regulations is biased because costs are exaggerated and benefits are under-valued. The literature now includes several dozen regulations where the ex post estimates of benefit and cost are compared to the ex-ante estimates made by agency analysts before regulations were issued. While many of these estimates have been shown to have errors, there is no universal pattern that costs are exaggerated and benefits are underestimated. Indeed, my summary of this literature is that it shows no systematic bias in the quantitative estimates of benefits and costs by federal agencies.

Myth #5: BCA is so complicated and time consuming that it slows the regulatory process to a halt.

There is a theory in the legal literature that the federal regulatory process has become so "ossified" by procedural and judicial requirements that the pace of federal rulemaking is now at a snail's pace. A related concern is that the addition of BCA requirements will exacerbate the ossification, and slow down the issuance of necessary regulations. Based on the available empirical literature and my five years of experience at OMB, I can assure you that federal agencies have no difficulty issuing numerous regulations, including highly expensive ones, when there is a political desire to do so. Consider, for example, the rapid flow of homeland security rules after the tragic events of 9/11. Anyone who has been following the Obama administration is aware that numerous new regulations are being proposed and finalized, despite the BCA requirement and other procedural requirements on agencies. And since most important regulations are already litigated by a wide range of stakeholders, and federal judges are already considering the findings of BCA, it is hard to see how a well-crafted statutory requirement for BCA could lead to more ossification or judicial delays.

Now that I have addressed some of the myths about BCA in federal regulation, I turn to some constructive suggestions for legislation in this arena.

SUGGESTIONS FOR STATUTORY REFORM

First, I recommend that Congress pass a simple statutory requirement that regulators conduct and use BCA (and related tools) when issuing significant federal rules. Reasonable people can disagree over how the benefit-cost mandate should be framed but I think it is sensible to start from the principles in the Clinton-Gore executive order (1993). I believe it may also be useful to review the legislative language that Senators Carl Levin and Fred Thompson crafted almost fifteen years ago, including some of the refinements made in consultation with the Clinton-Gore administration. I am very pleased that President Obama has recently reaffirmed presidential commitment to BCA as a valuable tool in rulemaking.

Basically, there needs to be a statutory requirement that regulators perform BCA, a requirement that a preferred regulatory option have benefits that justify costs, and some safeguards to ensure that the BCA is performed with a high degree of quality. For example, the agency should be required to analyze at least one option that is less expensive and one option that is more expensive than the agency's preferred option. In other words, analyses that simply compare one regulatory option to "doing nothing" should not be considered adequate. Since presidents and agencies

do not always adhere to the provisions in presidential executive orders, it is imperative that judicial review of the new statutory requirements be authorized. The benefits-justify-costs test should be applicable to each significant regulation, unless the agency's authorizing statute has explicitly prohibited consideration of BCA.

Second, I recommend that Congress require OMB to issue guidance on the proper conduct of BCA, and that this guidance be updated periodically (e.g., at least every ten years or as soon as there is significant change in the state of the art of BCA). OMB currently uses a guidance document called Circular A–4 that was issued in 2003 after public comment, interagency deliberation, and expert peer review. I recommend that Congress require a similar process in the future, placing OMB in the lead in consultation with the White House Council of Economic Advisors and other agencies. In order to better ensure that the data and models used by agencies are valid and appropriate, the new statutory mandate should reference the information-quality and peer-review guidelines that have been issued by OMB, and provide stakeholders an opportunity for judicial review in cases where these well-developed guidelines are not followed by agencies.

Third, I recommend that Congress expand the scope of the statutory mandate to include significant guidance documents as well as legislative rules, at least in cases where the agency's action to issue a guidance document has the same practical effect on regulated parties as a regulation. Senator Collins (R–Maine) has already proposed a bill in the Senate to apply BCA to guidance documents, and I urge the subcommittee to take a careful look at her guidance-related provisions.

Finally, Congress should consider adding a distributional arm of the "benefits-justify-costs" test that ensures that the welfare of low-income Americans is considered before a significant rule is issued. Thus, even if a regulation passes the benefit-cost test for society as a whole, it may not be advisable if low-income Americans are likely to incur more costs than benefits. For example, energy-related regulations that increase the price of gasoline at the pump have a disproportionately harmful effect on low-income families, especially those families living in small towns and rural areas where alternatives to automobile travel are not available. The benefit side of the ledger also needs to be considered, since some regulations offer significant benefits to low-income families while others do not. As a matter of fairness, regulators owe it to the most economically disadvantaged families in society to explore whether a proposed rule will make these families better off or worse off. My 2008 article in the Pennsylvania Law Review provides a more complete discussion of the philosophical and practical aspects of this recommendation.

In summary, it has been accepted by U.S. presidents for at least 30 years that BCA should play an important role in federal rulemaking. While OMB and federal agencies have made significant progress in this direction, it is well known that OMB and federal agencies do not implement this policy with consistency and a high degree of quality. Congress should build on the logic of the recent presidential orders by passing a simple statutory requirement that is backed by the force of judicial review. If OMB and federal agencies know that federal courts are authorized to review the role of BCA in federal regulation, they will take their BCA-related responsibilities much more seriously than they do today.

Mr. GOWDY. Thank you, Dr. Graham. Let me ask you a couple of questions, and then I will recognize the gentleman from Tennessee.

Is it fair that some benefits are not quantifiable? Is that a fair statement to say? And how would you address that in a cost-benefit analysis if some benefits are not easily quantifiable?

Mr. GRAHAM. Let me start by saying basic textbooks in benefit-cost analysis acknowledge that not all costs and benefits will be quantifiable, or, even if they can be quantified in the physical units, like tons of pollution prevented, for example, they may not be quantifiable in dollar terms. So, clearly a good cost-benefit analysis lays out—think of it as the advantages and the disadvantages of the regulation, and quantifies those that can be quantified. But there is no point in forcing agency analysts to try to quantify things that cannot be quantified.

So, in the final analysis, the decision about whether the benefits justify the costs is a policy judgment made by a regulator. That does not mean that the regulator can do anything, but they do have to make a judgment.

Mr. GOWDY. Dr. Graham, the best argument for codification, is it the political whims and caprices that change with Administrations? Is it judicial review? What are the three best, strongest arguments for codification in your judgment?

Mr. GRAHAM. Well, I think the first thing to keep in mind is that at the career level, the staff members in the regulatory agencies, whether it be the Labor Department or Homeland Security, if they know that their regulation is going to be subject to judicial review for its benefit cost justification, they will devote more serious effort to the benefit-cost analysis. I think that is a very important thing. Without that codification, you are not going to get that type of judicial review on the benefit-cost analysis implementation.

And then the second reason is, various Presidents—we can all pick our examples—they have called them political or policy preferences or campaign commitments in particular areas that they are going to want to proceed with, even though in some cases they really do not have a very good justification based upon benefits and costs. And the people who would be harmed by those regulations, they need the ability—the safeguards of the courts to ensure that those commitments and political commitments are not imposed on them without careful analysis of benefit and cost.

Those would be my two primary reasons.

Mr. GOWDY. All right. You said it is important to apply cost-benefit analysis to agency guidance documents because they have the same practical effect on regulated parties as a regulation. How can this happen? And, secondarily, does this mean that an agency can avoid the notice and comment process by just issuing guidance documents?

Mr. GRAHAM. Well, the short answer is yes. But there are a couple of good lawyers on this panel sitting next to me, and they can describe to you in better detail than I do the creative ways that agencies work to basically impose a burden on, say, a business without actually ever writing a regulation. They simply issue a guidance document and say, it would be a good idea if your plant was designed in this way or if it operated in that way. And then in addition, they say we might have visits or enforcement actions at your facility at some point in the future, and it is all kind of informal. But as a practical effect, the agency is saying you better do what this guidance document says.

That is, I think, is a very serious problem. And agencies, because rulemaking is more expensive, it takes longer, they like to do as much as they can through these guidance documents.

Mr. GOWDY. Can codification force agencies to quantify factors they might otherwise say are not quantifiable?

Mr. GRAHAM. I am not sure. I think the most important factor in the process of quantification is the peer review process where scientists, engineers, and economists from universities and from non-profit organizations, they review the analyses that are prepared by agencies. And they may say in certain cases, you know, there are data available that allow you to quantify this benefit or

this cost. Or they may say, you are trying to quantify this, but the data you have are not adequate to support that. It is that technical peer review process which needs to be part of this legislation that I think is the best assurance that the quantification process is proceeding in a valid manner.

Mr. GOWDY. Thank you, Dr. Graham. At this point I would recognize the distinguished gentleman from Tennessee and biggest fan of the Memphis Grizzlies in Congress, Mr. Cohen?

Mr. COHEN. Thank you. Thank you. And even though they lost yesterday, they are still very much alive. They will come back.

Mr. Graham, of the Atlantic Coast Conference, which also plays basketball on a different level, when you worked with the Bush Administration and you had these regulations come up on Homeland Security, how did you determine what we should do on a cost-benefit analysis when you are talking about people's lives and unknowns, such as Al-Qaeda?

Mr. GRAHAM. Well, I think that is a great question. And remember, I am talking about this period, maybe the first 18 months after 9/11 where there is a lot of emotional concern in the country about trying to do things to protect the next 9/11.

The Administration had the authority, emergency authority, to do a wide range of things without any cost-benefit analysis whatsoever. If they had had the kind of basis that was necessary to declare an emergency, they could have done so without any of the analysis I am talking about.

The Administration knew they did not have that as a matter of intelligence and as a matter of the situation at the time. So, they proceeded with these regulations through normal rulemaking process. When they made that decision, they were implicitly saying that we really ought to follow the same kinds of procedures that would normally apply for the rulemaking.

And in the case of these Homeland Security regulations, what I thought was the most interesting was the requirements as they are implemented in the United States and around the world are actually quite different. All of us travel to go through airports. Have you ever noticed how much variation there is between the specific requirements when you actually go through screening? Do each of these differences have a justification? Sometimes your shoes are off, sometimes they are on. Sometimes your belt is off, sometimes it is on. And it varies.

And I do not think there, frankly, is a really good, sound justification for a lot of this variation, and that tells me that the evidential basis for what is being required is somewhat thin. Does that mean we should not have any of these regulations? No. But I think a little more thought to how they are designed in the first place is probably a good idea.

Mr. COHEN. I agree with you, and I do not know that much about the regs, and I thought about them this week when in Memphis they said you had to take off your belt. They have never said that before, and sometimes they say it in D.C., and sometimes they do not. But we never said you had to take off your tennis shoes or your shoes, and then comes this guy with the material in his shoes. I mean, how do you quantify that type of regulation when 200 lives

would have been in the balance if the guy had a better lighter or BIC or whatever?

Mr. GRAHAM. You actually just did a little bit of quantification. And it does not require much in terms of number of lives saved, even potentially, to justify a significant regulation. So, the real question is, do they have the basis for these different types of distinctions and why they are requiring passengers to engage in this type of screening versus another type of screening. If they have that basis, even on a qualitative basis, I think you could potentially justify these types of regulations.

I am just trying to be candid with you and be honest with you that I have tire tracks on my chest from rules after 9/11 that rolled through this Federal Government. You know, it probably would be a good idea right now to go back and look at some of those and see whether all of them are still really necessary.

Mr. COHEN. Yeah, well, I do not disagree with you, and it is an interesting subject. I need to spend some more time on it. But some of the stuff is absurd, and I think we go overboard on some of the things. But nevertheless, safety, it is very difficult to do that in terms of dollars and cents. And some of it just seems like whether or not it makes sense, and sometimes we get into these regulations, like on the belt and all. We have really created an industry and we cannot get rid of it because their jobs are there, and there are companies that sell that equipment, and so they have become ones that push forward because, even though it really does not do us any good. So, I do not how you get around that.

But the President has said some things about fairness, and he has talked about equity, and he has been criticized for that when considering rules with lead poisoning among poor children. Would you agree that the President has probably got something appropriate when he is dealing with fairness and equity or dealing with poor children and lead poisoning, and that maybe the criticism is not fair?

Mr. GRAHAM. I have not seen the details of the criticism that the President made. But I do cite in my testimony what I think is an important role that fairness considerations play in a reasoned development of a regulation. And sometimes, for example, when you take energy regulations that increase fuel prices at the pump, those regulations have a disproportionate adverse impact on lower income Americans, particularly Americans who live in rural areas and in small towns where alternative transportation is not available. In that kind of a case, even if the benefits of that regulation would be somewhat greater than the cost, a fairness consideration might say, well, really this is not a very good time to impose this kind of burden on the lower income elements of our population.

So, I am a firm believer that fairness considerations, particularly as related to low income populations, do have an important role in a benefit cost framework. But I would have to look in more detail at exactly what President Obama said to understand his particular claim.

Mr. COHEN. So, if the Chairman would allow me for just 20 seconds, could you be willing to give me and/or the Chair and the Committee some of those tracks that you have got and tell us

which of those regulations you think we should not have passed and an explanation so that we may look at that?

Mr. GRAHAM. It will be easy because my boss at the time was Mitch Daniels, the current governor of Indiana. And he allowed me in 2004 to actually publish an annual report from OMB that listed all of these Homeland Security regulations, what was estimated as to their cost, and what their rationale was. And we allow readers to make their own determination.

Mr. COHEN. Do you have a Cliff's Note of that?

Mr. GRAHAM. Yeah, and it is on the website. It is a nice table actually, just maybe a two-page table that lays it all out. So, I will get you a copy of that.

Mr. COHEN. Thank you, Mr. Chairman. Thank you, sir.

Mr. GOWDY. Yes, sir, Mr. Cohen. Dr. Graham, that buzzer, I think, means something, but I am going to recognize the distinguished gentleman from the great state of California, Mr. Gallegly, for his questioning. And then with the indulgence of the other three panelists, we aspire to go vote and then return.

Mr. Gallegly?

Mr. GALLEGLY. Thank you, Mr. Chairman. I would just like to make a quick observation, and I know you have a flight to catch, and we have votes to take, and we are behind a couple of hours already.

But in follow-up to Mr. Cohen, relative to airport security and so on, you know, we all do a lot of traveling. In fact, I have accumulated over 1,700 trips from one coast to the other because I commute every week to California. And you do get familiar with that process all too well.

But the regulations, and I would like to know a little bit about maybe the flexibility in some of these regulations, because you mentioned, you know, you go into one airport, they require a belt, you go in another airport, it is taking your laptop out of the case, or your iPad or whatever, and then the next week it is different.

Well, an observation that I have made for some time, and I happen to know a little bit about the rationale behind it, and it has to do with flexibility sometimes is important, because when you are dealing with terrorists, the most important thing you can do is keep them flat footed and off guard. And every time you move a guard from one corner today to the next corner the next day, they never know which corner the guard is going to be on. So, if everybody is in the same place doing the same thing every hour with a belt or with a laptop or whatever, it has a strategic benefit. Could you maybe respond to that a little bit and how regulations impact on the importance of flexibility?

Mr. GRAHAM. Well, first of all, I think you make a really excellent point, that in order to have an effective strategy in counterterrorism through these kinds of regulations, you would have to have some changes over time that keep the terrorists off balance in terms of their targeting.

The examples I was referring to were not changes in practices at the same location. It is that when you are in this airport, they do it this way, and when you are at that airport, they do it that way. And to me, it is just not obvious that that is confusing many terror-

ists. It just seems to be kind of an unexplained variation in what this practice is.

But I agree with you. In fact, one of the things I noticed when I was at OMB and we were issuing all these rules, so many of the rules that we were issuing were trying to go back and prevent the incident that had already occurred. But surely a perceptive and shrewd terrorist, for their next couple of instances, would not necessarily be replicating the same pathway and the same targets that were used the time before. But how many regulations were we doing on all the other targets? Not very many.

So, I am just trying to admit that the whole process of regulation in a situation where you have a lot of political, you know, saliency on an issue like that, it can benefit from some evidence, some analysis, some benefits and costs.

Mr. GALLEGLY. The one thing that has certainly become abundantly clear is you have a very simple and unchallenging job. [Laughter.]

I appreciate your testimony, and I do know the tremendous challenges, and they are changing every day. So, but yet we do have to have regulations.

Mr. GRAHAM. We certainly do.

Mr. GALLEGLY. But we need to learn how to best prioritize, and that is why we have the experts out there hopefully that are doing the right thing. And I feel confident you are. Thank you.

Mr. GRAHAM. Thank you, sir.

Mr. GOWDY. Thank the gentleman from California. It is the fervent hope of all three of us that you will make it through TSA with your shoes and your belt on. Thank you for your patience.

To the three remaining witnesses, we continue to thank you for your indulgence. We are grateful for your patience. Mr. Cohen did much better in math than I did. He added up the number of minutes that we may be gone, and I am going to let Judiciary staff and our three witnesses decide how much of their lives they would like to be imposed on today. So, this could be a long series.

But you have got a plane to catch. You have lives to live. I will let higher ranking people than me make the decisions. But if I see you again, I will look forward to it. If I see you again another day, thank you for your patience.

We will be adjourned pending votes.

[Recess.]

Mr. GOWDY. We will reconvene. And, again, on behalf of Mr. Cohen and myself and everyone else involved in the process, we want to thank you again for your patience and understanding the vagaries of votes.

Without further ado, it is my pleasure to introduce our three witnesses.

Jeffrey Holmstead is one of the Nation's leading air quality attorneys and leads the Environmental Strategies Group at the law firm of Bracewell and Giuliani. Did I pronounce it correct?

As the head of the Environmental Protection Agency's Office of Air and Radiation from 2001 to 2005, Mr. Holmstead saw firsthand how regulatory agencies conduct and use cost-benefit analysis. Between 1989 and 1993, Mr. Holmstead served on the White House staff as associate counsel. In that capacity, he was involved in the

passage of the Clean Air Act amendments of 1990 and the key steps taken to implement that law.

He is a graduate of Yale Law School. He earned his bachelor's degree, summa cum laude, from Brigham Young University.

Sally Katzen has enjoyed a distinguished career in legal practice, government service, and academia. The first female partner of the law firm Wilmer, Cutler & Pickering, Ms. Katzen also served as the Section Chair of the American Bar Association's Administrative Law and Regulatory Practice Group. She served for 8 years in the Clinton Administration, including 5 years as administrator for the Office of Information and Regulatory Affairs in the Office of Management and Budget.

She has a bachelor's degree from Smith College and a J.D. from the University of Michigan School of Law. She has taught at George Washington University, the University of Michigan, University of Pennsylvania, and Georgetown, and is a visiting professor at New York University School of Law.

Mr. Harold Furchtgott-Roth. Have I pronounced that close to correct? All right. From 1997 to 2001, Dr. Furchtgott-Roth served as the commissioner of the FCC. Before his appointment to the FCC, he was chief economist for the House Committee on Commerce and the principal staff member on the Telecommunications Act of 1996.

He is a professional economist, the president of Furchtgott-Roth Economic Enterprises, the author of dozens of publications, and has authored or co-authored four books, which means he has written more books than we have read, right?

Mr. COHEN. You can say whatever you want to say about yourself. [Laughter.]

Mr. GOWDY. Dr. Furchtgott-Roth received his Ph.D. in economics from Stanford University and a bachelor of science degree in economics from MIT.

We would like to thank all three witnesses for joining us, and we will recognize each of you from my left to right, your right to left, starting with Mr. Holmstead, for 5 minutes and your opening statement?

TESTIMONY OF JEFFREY HOLMSTEAD, PARTNER, BRACEWELL & GIULIANI, LLP

Mr. HOLMSTEAD. Well, thank you. I am happy to be here. I wanted to be somewhat informal like Dr. Graham was and just say, to begin with, I like to think I have a somewhat unique perspective having seen the regulatory review process both from the White House and then from EPA and also from the private sector.

And having done this now for 20 years, worked on cost-benefit analysis and regulatory review, I want to say this. I know from my own experience that a lot of the career staff folks at EPA take cost-benefit analysis seriously and they try to use it to make regulatory decisions. But I have also seen that Federal officials sometimes use cost-benefit analysis not to inform their regulations, but to justify the regulations that they want to do for other reasons.

Cost benefit analysis is an important regulatory tool, but it can be done in properly, it can be done poorly, and in some cases it can actually be misused. And for this reason, I do think it is important to have some sort of meaningful oversight of the type of regulatory

analysis conducted by regulatory agencies. And I am enthusiastic that this Subcommittee is considering these types of enforcement mechanisms that would make sure that there is a meaningful cost-benefit analysis.

I want to just start with a quick example of what I consider to be the misuse of cost-benefit analysis. And this may sound like I am down in the weeds; I do not mean to be. But there has been a lot of research done over the past seven or 8 years, and Dr. Graham is one of the people doing this research, showing that reducing fine particle pollution is by far the most important thing EPA has ever done under any of its statutes. And, you know, there are arguments about all the EPA statutes, but I do not think any serious researcher disagrees that most of the benefits to our society achieved by EPA have come from reducing these fine particles, which we refer to as PM2.5.

You would think, and in fact a proper cost-benefit analysis would say, well, what is the most cost effective way that we can achieve these benefits? Unfortunately, some EPA officials have come to use the benefits of reducing fine particles as a way to justify almost anything they want to do. Again, a proper cost-benefit analysis, one that actually adheres to the principles that President Obama has in his executive order and certainly comes from the prior executive orders, would say, well, let us look at the most cost effective way of achieving these benefits. But unfortunately, it has come to be, as I said, used as a way to justify almost anything.

A particularly egregious example is something that we refer to as the Utility MACT Rule. This rule is supposed to be designed anyway to reduce mercury emissions from power plants. The sole basis for this rule was a determination back in the year 2000 by then administrator Carol Browner, that mercury emissions from coal-fired power plants needed to be reduced. So, they come up with this rule. The rule, as proposed, would be the most costly rule ever issued by EPA if they finalize it. And EPA's analysis says it is about $11 billion a year of costs. But then they say this is still a good deal for society because it will achieve benefits somewhere between $50 billion and $100 billion, so this seems like a good deal.

You get into the details, though, and EPA says, well, we did look at the benefits of mercury, reducing mercury from power plants, and we have quantified those benefits, and we estimate those benefits to be somewhere in the range of $500,000 to $6.1 million. So, benefits of half a million to no more than $6.1 million, and the costs are $11 billion. And they say, but that is okay because we are going to get all these PM2.5 reductions. But what they do not do is say, are there other ways that would be much more cost effective to achieve these reductions? And the answer is, there are, and Congress has specifically adopted a program to deal with these. It provides much more flexibility, a very different role for EPA. But EPA has chosen to use this benefits analysis to justify what it really wants to do anyway, which is to impose very costly regulations on coal.

I see that my time is running out. I will mention my last two points. One are, there are other ways that agencies have learned to avoid oversight. In some cases, and I am sure Ms. Katzen will probably agree that she has seen this. Two, is that there are

friendly lawsuits that set deadlines on agencies that effectively prevent OMB from exercising any kind of regulatory oversight. I would be happy to give you many examples of that where, again, in the Environmental Protection Agency they will go into court and come up with a settlement agreement with an environmental group, and that will compel the Agency to issue a rule on a certain schedule, a schedule which prevents OMB from being involved in the process. And I think it is important for this Committee to at least think about mechanisms to ensure that there is an opportunity for meaningful regulatory oversight by the Office of Management and Budget. And I also believe that the kind of enforcement mechanism that Dr. Graham talked about where there could be some judicial oversight would also be a very helpful thing for the process.

Thank you.

[The prepared statement of Mr. Holmstead follows:]

Prepared Statement of Jeffrey R. Holmstead, Partner,
Bracewell & Giuliani, LLP

My name is Jeff Holmstead. I am a partner in the law firm of Bracewell and Giuliani and the head of the firm's Environmental Strategies Group. This afternoon, however, I am not appearing on behalf of my law firm or any of my firm's clients. I am here as a former official in both the Environmental Protection Agency (EPA) and the White House who has spent more than 20 years working on the development of federal regulations.

I served as the head of EPA's Air Office for more than four years (from 2001 to 2005) and as an Associate Counsel to the President for almost four years (from 1989 to 2003). During my time in the White House, I was very involved in the regulatory review process. I have also been an environmental attorney in private practice for many years. In both government and the private sector, I have spent many years thinking about and dealing with cost-benefit analysis as both a conceptual and practical matter. Thank you for the opportunity to address the subcommittee on the important issue of presidential and judicial review of regulations and the role that should be played by cost-benefit analysis (CBA), which is sometimes referred as benefits-cost analysis (BCA). Both terms (and both acronyms) mean the same thing.

It is increasingly clear that we are in an age of unprecedented federal regulation over many aspects of the Nation's economy. I am most familiar with the regulations that EPA has issued over the last two years, but Susan Dudley, the former head of the White House Office of Information and Regulatory Affairs ("OIRA"), has noted that the Obama Administration has issued a total of 132 "economically significant" rules (i.e. rules whose costs or benefits exceed $100 million per year) in the two years it has been in office. To put this total in perspective, this total is approximately 40 percent higher than the annual rate under Presidents Bill Clinton and George W. Bush.

While it is tempting to draw conclusions by simply looking at these totals, each rule or set of rules that affect the same entities should be evaluated by looking at its costs and the benefits it provides to society—and how these costs and benefits are distributed. Everyone agrees that many of these rules will impose very substantial costs, but the rules may still be justified if they provide even greater benefits to our society. On the other hand, if the cost of a rule exceeds its benefits, our economy suffers the consequences. Proponents of greater regulation often pretend that the costs are simply imposed on industry or "big business," but they also affect—sometimes quite substantially—workers, consumers, ratepayers, and all Americans who have privately-funded pension plans or are otherwise invested in stocks, bonds, or mutual funds.

I can say from my own experience that many career officials at EPA take cost-benefit analysis seriously and try to use it as much as possible to make regulatory decisions. Other federal agencies also do CBA, but perhaps to a lesser extent. I have also seen, however, that federal agencies sometimes do not use CBA to *inform* their regulatory decision, but rather to *justify* actions they may want to take for other reasons. CBA is simply a analytical tool that can be used properly or poorly or even misused. For this reason, it is important to have appropriate oversight of the analysis conducted by regulatory agencies—to ensure that regulatory decisions are con-

sistent with the principles of CBA and with the underlying statutory scheme created by Congress.

I support this Subcommittee's efforts to consider legislation that will ensure proper presidential and judicial review of the justification underlying Federal regulations. To further your efforts, I would like to focus attention on three key issues relating to problems with the current system of cost-benefit analysis and areas of focus for any potential solution.

BACKGROUND

Before evaluating the current use (or misuse) of cost-benefit analyses and the need for legislative action, it may be helpful to briefly review the mandates placed upon all Federal agencies when issuing regulations. First, under Executive Order 12866, issued by President Clinton in 1993, when an agency determines that a regulation is the best method of achieving a regulatory objective it must, among other things:

- (1) "design its regulations in ***the most cost-effective manner*** to achieve the regulatory objective;"
- (2) "propose or ***adopt a regulation only upon a reasoned determination that the benefits of the intended regulation justify its costs;"***
- (3) "***identify and assess alternative forms of regulation*** and . . . specify performance objectives, rather than specifying the behavior or manner of compliance that regulated entities adopt;"
- (4) "tailor its regulations to impose the ***least burden on society*** . . . taking into account . . . the ***costs of cumulative regulations."***

In Executive Order 13563, issued on January 18, 2011, President Obama reaffirmed these regulatory principles under an overarching instruction to Federal agencies to protect public health and our environment "while promoting economic growth, innovation, competitiveness, and job creation."

MISUSE OF COST-BENEFIT ANALYSES

Having spent many years looking at the benefits of different environmental regulations, I agree with the many researchers who believe that reducing levels of fine particles in the air is the most important and beneficial thing that the federal government can do in the environmental arena. The vast majority of the benefits that EPA has ever achieved under all the federal environmental statutes come from reducing ambient levels of fine particles, which are often referred to as PM2.5.

There are two major areas of uncertainty about the benefits of reducing PM2.5: (1) whether all the different components in PM2.5 should be regulated equally; and (2) whether there are benefits of reducing such pollution in areas where levels are already low. I believe that the EPA and other agencies should pay more attention to addressing these areas of uncertainty, but I will not discuss them here.

My concern is that, rather than using cost-benefit analysis to develop the most effective way to reduce PM2.5, some EPA officials have come to view CBA—and the benefits of reducing PM2.5—as a way to justify virtually anything that they may want to do. All too often in recent years, EPA has understood the instruction to issue the "most" cost-effective regulation to mean that it may issue "any" regulation where it can show benefits exceeding costs. Unfortunately, this is a serious misuse of the type of cost-benefit assessment that is required by Executive Orders 12866 and 13563. Proper CBA should identify the most effective way to regulate—and not be used simply to justify any regulation that can be claimed to provide benefits that exceed costs.

A CASE STUDY: THE PROPOSED UTILITY MACT

EPA has recently issued a proposed rule to reduce emissions of so-called "hazardous air pollutants" (or HAPs) from coal- and oil-fired power plants. This rule is generally referred to as the Utility MACT because it was developed under a section of the Clean Air Act that calls for EPA to develop standards based on the "maximum achievable control technology" (MACT) that can be used to control HAP emissions from different type of industrial facilities.

As proposed, the Utility MACT would be the most expensive rule in EPA history. Some experts believe that EPA has actually understated its likely costs, but even EPA acknowledges that it would impose costs of about $11 billion a year on the U.S. economy. Yet EPA has also gone to great lengths to argue that the benefits of this rule will greatly exceed the costs. Under the requirements of the two Executive Or-

ders cited above, EPA prepared a cost-benefit analysis which suggests that annual benefits will be in the range of $48 to $130 billion. If the annual costs of the rule are only $11 billion, then "the benefits of the proposed [Utility MACT] far outweigh the costs," as EPA argues.

The Agency's sole basis for issuing this proposal is a regulatory determination that then-EPA Administrator Carol Browner made in December 2000 that it was "appropriate and necessary" to regulate certain HAPs from power plants This determination was based almost entirely on the Administrator's concern about mercury emissions from coal-fired power plants. Not surprisingly, the majority of the proposed rule deals with mercury reduction requirements for coal-fired power plants.

It stands to reason that the vast majority of benefits claimed by EPA to justify the proposed rule must be the result of reductions in mercury emissions. But the Agency's cost-benefit analysis tells a very different story. According to EPA, the benefits to society of the mercury-reduction requirements are in the range of $500,000 to a ***maximum*** of $6.1 ***million*** in total (i.e. not even annual) benefits. In other words, in a rule estimated by EPA to cost $11 ***billion*** annually, the maximum total benefit of reducing emissions of mercury—the emissions of which serve as the primary basis for the rule—is $6.1 ***million.***

EPA asserts, however, that it's proposal is justified based on cost-benefit analysis because the rule will provide benefits of up to $130 billion ever year. Yet virtually all these benefits come from reducing PM2.5.

Although mercury is the Agency's legal justification for the Utility MACT, EPA argues that it must also regulate non-mercury HAPs such as certain metals (e.g. nickel, selenium, etc.) emitted in trace amounts and acid gases (e.g. hydrogen chloride and hydrogen fluoride) that, according to EPA, do not pose a meaningful risk to public health. While some health risks from emissions of non-mercury HAPs are discussed in the proposed rule and the CBA (presumably implying health benefits from reducing such emissions), EPA does not make any attempt to evaluate the benefits that will be achieved by reducing these emissions. What is discussed at some length is that control technologies for non-mercury HAPs included in the proposed MACT standard result in reductions of emissions of PM2.5 and SO2. In fact, EPA's analysis admits that virtually all (i.e. 99+ percent) of the estimated $42 to $130 billion in annual benefits are due to reductions in PM 2.5.

Nowhere does EPA explain whether there is a less costly way to achieve these benefits, which is puzzling because Congress has created a whole separate program to regulate PM2.5—and it is very different from the MACT approach that EPA is now proposing. Although EPA is aggressively implementing the program that Congress created to regulate PM2.5, this program is much more flexible than the MACT program and would be a much more cost-effective way of regulating PM2.5 from power plants.

Why should this matter to the public? I have explained part of the answer above: EPA is mandated to find the most cost-effective solution for the regulatory priority (here: controlling mercury emissions from power plants) How can the Agency possibly conclude that it is a good deal for society to impose an annual cost of $10.9 billion to achieve benefits of $6.1 million?

The other reason this type of analysis matters is that EPA has ***already*** controlled emissions of PM2.5 by setting a national ambient air quality standard ("NAAQS") under section 108 of the Clean Air Act. In doing so, EPA has set a level of PM2.5 that it has found to be sufficient to public health and welfare with an adequate margin of safety. Areas of the country that already have attained this level of PM2.5 (i.e., that are in "attainment") are presumably therefore already safe from any health risks; Other areas that have not yet reached this level (i.e. are in "non-attainment") are ***already*** required to implement market-wide reductions in PM2.5 to get into attainment.

In explaining how it developed the baseline for its benefits analysis, EPA's RIA states that "EPA did not consider actions states may take in the future to implement the existing ozone and PM2.5 NAAQS standards[.]" Of course, as it did for the Utility MACT, EPA's proposed NAAQS for PM2.5 contained an estimated analysis of the benefits of PM2.5 reductions. By not including these benefits in the baseline of the Utility MACT, EPA is essentially claiming these same benefits a second time to justify another regulation. Put a different way, the only way EPA can possibly claim more benefits from reductions in PM2.5 is to go beyond the controls it has already put in place under the PM2.5 NAAQS. Doing so, however, is completely contrary to Congress' intent to regulate PM2.5 under a different section of the Clean Air Act and contrary to EPA's own claims that the PM2.5 NAAQS is sufficient to protect public health and welfare.

USING "FRIENDLY" LAWSUITS TO AVOID OVERSIGHT

Currently, the only check on an agency's use of cost-benefits principles to make regulatory decisions is the interagency review process overseen by OIRA, which is part of the White House Office of Management and Budget (OMB). I have great respect for ORIA officials and staff, who are seasoned and dedicated economists and analysts with years of experience analyzing the costs and benefits of innumerable types of regulations. Unfortunately, OIRA officials are often unable to perform effective oversight due to factors outside of their control. EPA's proposed Utility MACT is, once again, a useful illustration.

In April 2009, after being sued by several environmental organizations for its failure to issue emission standards for HAPs from power plants, EPA ***voluntarily*** agreed to a consent decree. Under this consent decree, EPA agreed to an extraordinarily ambitious schedule that almost guarantees that there will not be enough time to do serious regulatory analysis. The consent decree requires EPA to issue the proposed Utility MACT by March 16, 2011 (which it has already done) and then to issue a final rule by November 16, 2011. It is not clear that the environmental organizations had a valid legal claim that EPA was required to issue the Utility MACT on any particular schedule, but there was certainly no legal justification for a schedule like this one. Some observers have suggested that EPA may have wanted to be "required" to issue the rule well in advance of the next presidential election.

To gather data for the proposed rule, EPA issued an information collection request ("ICR") to utility companies in December 2009. This ICR required these companies to conduct extensive testing and analysis that cost almost $200 million to produce. This data was not even available until late 2010, so neither EPA nor any other interested party had more than four months to review it before the proposed rule was issued. Putting aside the question of whether four months is an adequate timeframe in which to perform the required technical and cost-benefit analyses, EPA only submitted its proposed Utility MACT to OMB for the regulatory review process on February 19, 2011. Accordingly, OIRA and OMB officials, as well as officials at other affected agencies, had a total of ***thirty*** days to review, analyze, submit and resolve comments on the 946-page rule and the 496-page cost-benefit analysis before EPA was required to publish the proposed rule. It goes without saying that thirty days to perform the type of careful analysis and provide the meaningful input intended by the Executive Orders is beyond the skills of even the most dedicated and hard-working public officials.

This is just one example (a particularly glaring one, to be sure) of a consent decree having the effect, if not the intention, of cutting off meaningful regulatory review. But it highlights the need for Congress to ensure that agencies cannot make voluntary arrangements with outside entities which result in an end-run around the regulatory review process. I urge the Subcommittee to develop a legal, enforceable mechanism to ensure that there is sufficient time for meaningful interagency review.

ENSURING PROPER REVIEW AND ANALYSIS OF GUIDANCE DOCUMENTS

I also recommend that the Subcommittee go beyond just rules and regulations to require that significant guidance documents are subject to analysis and interagency review. Informal guidance is a very important part of the regulatory and compliance process, and it would be a mistake to do anything that would prevent agencies from developing guidance that is helpful to outside parties. But some guidance documents can have major impacts on regulated entities, even though they are not formally designated as "rules" that must go through the normal rulemaking procedures and interagency review. The Subcommittee should expand the scope of its inquiry to ensure than such guidance is analyzed and reviewed like rules that have the same practical effect on regulated parties as a regulation.

* * * * *

It has been widely accepted for many years that cost-benefit analysis should play an important role in federal rulemaking. Although OMB and some other federal agencies have used CBA as an important tool in regulatory development, this requirement is not always done well. Congress should build on the work that has been done over the last 30 years to ensure that agency do not avoid or misuse this type of analysis.

Mr. GOWDY. Thank you, Mr. Holmstead.

Ms. Katzen?

TESTIMONY OF SALLY KATZEN, SENIOR ADVISOR, PODESTA GROUP, VISITING PROFESSOR, NEW YORK UNIVERSITY SCHOOL OF LAW

Ms. KATZEN. Thank you, Mr. Gowdy and Mr. Cohen. I appreciate the opportunity to appear today.

I think all of the witnesses are in agreement to a point. We all support the use of economic analysis by regulatory agencies, and that would include the independent regulatory commissions, like the FCC and the SEC, the CFTC, and the Fed. And in my written statement, I provided several paths that Congress could take if it wishes to pursue this, and I would like to discuss that further in the question period if you are interested.

I also think it is wholly appropriate for Congress, using hearings like this one or other oversight tools, to monitor agency activity, evaluate current practices, spotlight deficiencies, and bring public pressure to bear to improve agency performance, if that is what is called for.

Now, where I disagree with my colleagues is whether Congress should codify the requirements that exist for the executive branch agencies, including centralized review, and provide for judicial review of that process. I think not.

Before regulating, we ask agencies to identify the problem it intends to address and explain how the proposed regulation would fix that problem in an efficient and effective way. Those same questions should be asked before Congress acts. What is the compelling need to codify pieces or all of the executive order? The foundational principles have been in effect for over 30 years, endorsed and implemented by Presidents of both political parties, and recently reaffirmed by President Obama. And over the years, the benefits of regulations have consistently exceeded the costs. This was true during the Obama Administration, during the Bush Administration, during the Clinton Administration.

I cannot and will not say that all executive branch agencies do a great job of economic analysis and always incorporate the results in rule development. While strikingly better than the IRCs, the record is mixed, which should not surprise anyone given that agencies have different cultures and different resources. The latter is important because economic analysis, at least thoughtful, careful, comprehensive analysis, is not cost free. It takes time and resources. And the more significant the proposed regulatory action, the more time and resources it should consume. Regrettably, some of the very people who call for more analysis are the first to suggest straight lining or reducing the agency's budgets.

But even if the agencies were not consistently doing and using high quality analysis, and that case has not been made, would legislating pieces or all of the executive order bring about significant change?

Over the past 30 years, Congress has imposed a series of analytical requirements on the agencies—the Paper Reduction Act, Reg Flex Act, NEPA, the Unfunded Mandates Act, just to name a few—without substantially increasing the funding for the agencies to carry out the tasks that they were assigned. So, before adding another requirement, Congress might want to rationalize the current set of analytical requirements and/or provide more resources to

OIRA to review them. If there is an implementation problem, Congress should address the source of that problem directly and not just add another requirement.

Second, executive orders are, after all, orders of the President, to those who report to him and for whom he is constitutionally responsible. Those who profess support for the unitary executive should pause before crossing the separation of powers line to codify an executive order despite its universal appeal. And the history of this particular line of executive orders, from 12291, to 12866, to 13422, to 13653—do we not love all the numbers—shows that while many of the concepts are the same from one Administration to the next, different Presidents choose to emphasize different things—openness and transparency, market failure as a basis for regulating, public participation. These differences may be subtle, but are nonetheless important indicators of Administration policies and preferences.

Third, if Congress were to codify the analytical requirements of the EO, it would be amending a host of previously enacted statutes dating back over half a century. At this point, it is totally unclear how many statutes and which ones would be amended, and what the implications of such an amendment would be, both for the regulated entities and intended beneficiaries of those statutes.

A number of pieces of legislation are silent on the question of the role of cost, and others explicitly do not permit the consideration of cost. For that reason, the executive order says repeatedly that it will prescribe certain practices "to the extent permitted by law." However, if you were to codify the executive order, that would become the law, and as a result, a proposed regulation, even under a statute that does not permit the consideration of costs, could not become effective unless, among other things, the benefits justify the costs.

Now, Dr. Graham referred to the host of regulations coming through after 9/11 and was worried that they had not been cost-benefit analysis. I recall explicitly that one of those was a DoT rule to reinforce the steel in the cockpit doors. That was what Congress told DoT to do. It was not just that the President, for some political reason, wanted to get these things through. Congress said to do that. Agencies are not free agents. They have to do what the Congress has told them to do.

Now, you could amend all these acts. You can amend the Clean Air Act, the OSHA Act, and any other authorizing act. But I would urge you then to do it directly and not indirectly by creating decisional criteria.

Lastly, I would like to say that the idea of judicial review here leaves me in a very difficult position. I am a lawyer who greatly respects our judicial system, and I am talking to the Judiciary Committee. I would ask you whether the Federal courts is really the proper forum for sifting through cost-benefit analysis and deciding whether or not it has been properly used in formulating rules. Dr. Graham talked about the non-quantified aspects. Fairness was one. Justice might be another. Disparate impacts. How do you have Federal courts deciding? So, that in addition to having an army of lawyers who will be battling out whether or not the decisional criteria here has amended the underlying act, you are

going to have armies of economists who will be doing battle as well. With all due respect, I do not think that is the way to promote economic growth and job creation, except perhaps for lawyers or economists.

With that, I thank you very much for your patience.

[The prepared statement of Ms. Katzen follows:]

Statement of Sally Katzen

Visiting Professor NYU School of Law and Senior Advisor of the Podesta Group

before the

Subcommittee on Courts, Commercial and Administrative Law
of the
House Committee on the Judiciary

on

"Cost Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"

May 4, 2011

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May 4, 2011

Chairman Coble, Ranking Member Cohen, Members of the Subcommittee. Thank you for inviting me to testify today. I have been privileged to appear before this Committee on a number of occasions, both as a government official and as a private citizen. The Committee's oversight activities in the field of administrative law make an important contribution to the public's understanding of our nation's regulatory system and help frame the issues for both the legislative and the executive branches.

As you know, I served as the Administrator of the Office of Information and Regulatory Affairs (OIRA) at the Office of Management and Budget (OMB) for the first five years of the Clinton Administration, then as the Deputy Assistant to the President for Economic Policy and Deputy Director of the National Economic Council, and then as the Deputy Director for Management of OMB. After leaving government service in January 2001, I taught administrative law courses at the University of Michigan Law School, George Washington University Law School, George Mason University Law School, and the University of Pennsylvania Law School, and also taught American Government courses to undergraduates at Smith College, Johns Hopkins University, and the University of Michigan in Washington Program; this semester, I am teaching a seminar in advanced administrative law at NYU School of Law and am a Senior Advisor at the Podesta Group here in Washington. Before entering government service, I was the Chair of the ABA Section on Administrative Law and Regulatory Practice (1988-89), and during my government service, I was the Vice Chair (and Acting Chair) of the

Administrative Conference of the United States (ACUS). I have written articles for scholarly publications and have frequently been asked to speak on administrative law in general and rulemaking in particular.

The subject of today's hearing is "Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits." I understand the Committee wants to focus on several things: Cost/Benefit Analysis (CBA) in developing proposed and final regulations, Presidential (or centralized regulatory) Review of the economic analysis underlying those regulations, and Judicial Review. I support – strongly support – the use of economic analysis in developing regulations and the centralized review of those regulations, but I have reservations – serious reservations – about codifying the requirements for economic analysis and centralized review and providing for judicial review of that process.

When someone says "Cost/Benefit Analysis," people tend to look away or their eyes glaze over. The analysis itself – that is, the actual work product -- may be complicated, highly technical and often difficult to follow, but the concept is quite simple. It is a way to think about the consequences of a proposed action and then try to translate quite diverse consequences into the same metric -- typically money – so we can evaluate whether the proposal is, on the whole, good for us or not. We do this every day of our lives, whether it be for something trivial (walk or take a taxi) or significant (purchase a home or launch a new business), with the extent of the analysis roughly commensurate with the importance of the decision we are trying to make.

Requirements for economic analysis to inform, or in support of, important regulatory proposals adopted through rulemaking -- typically proceedings under Section 553 of the Administrative Procedure Act -- have been around at least since President Nixon established a "Quality of Life Review" program for certain high-profile regulations. Beginning in 1981 with President Reagan's Executive Order 12291, all Presidents (both Republicans and Democrats) have required regulatory agencies within

the Executive Branch to assess the costs and benefits of proposed actions, and, among other things, to the extent permitted by the laws that you enact, ensure that the benefits of the intended regulations justify the costs. The requirement to undertake this economic analysis and to submit it along with a draft proposed or final rule to OIRA was designed to make sure that the agency has thought through, in a disciplined and rigorous way, the obvious and the less obvious costs and benefits that are likely to occur if the proposal is adopted and has the force and effect of law. It is a significant undertaking. Consider the description of the overview of the analysis to be developed by regulatory agencies under Executive Order 12866:

> "An assessment . . . of benefits anticipated from the regulatory action (such as, but not limited to, the promotion of the efficient functioning of the economy and private markets, the enhancement of health and safety, the protection of the natural environment, and the elimination or reduction in discrimination or bias), together with, to the extent feasible, a quantification of those benefits;
>
> "An assessment . . . of costs anticipated from the regulatory action (such as, but not limited to, the direct cost both to the government in administering the regulation and to businesses and others in complying with the regulation, and any adverse effects on the efficient functioning of the economy, private markets (including productivity, employment, and competitiveness), health, safety and the natural environment), together with, to the extent feasible, a quantification of those costs . . . [and]
>
> "An assessment . . . of costs and benefits of potentially effective and reasonably feasible alternatives to the planned regulation . . . ."

And for those who thirst for a detailed description of how to do all of the above, I would refer you to OMB Circular A-4, which I require my students to read--with profuse apologies.

There are some items in the calculus, such as the costs of new equipment, the time it will take to install that equipment and train employees to use it, or savings from fewer

trips to the hospital or less employee time off to recuperate from workplace injuries that are relatively easy to quantify and monetize. There are other factors that are more difficult to quantify and monetize, such as being able to see across the Grand Canyon, increased protection from invasions of privacy, or peace of mind that food in the stores is free of e-coli. There are many economists working on ways to use samples or surrogates to provide relatively accurate data, such as willingness to pay, etc., and a literature that is full of commendations and critiques from their proponents and detractors. The theories and practices are evolving and are not without controversy, on the cost side as well as on the benefit side. But with benefits as with costs, thinking through the consequences and seeking to quantify and value them in a serious way is itself highly informative.

Indeed, gathering the data and structuring the analysis help the agency staff refine its thinking in drafting the proposal; the presentation of the analysis to the agency decision-makers can reinforce existing assumptions or cause rethinking of conventional wisdom; the review of the analysis by the staff of OIRA provides a dispassionate second opinion and quality control for the analysis; and the availability of the data and the analysis throughout the process enables the various stakeholders, their elected officials and the public generally to evaluate in a more objective way the merits of the regulatory action – what is at stake and for whom?

In a word, undertaking economic analysis in the course of developing regulations provides important information that often affects, for the better, the shape or scope of a proposed regulatory action. It is an input; it is useful; it is instructive. Indeed, I cannot imagine making regulatory choices (or legislative choices for that matter) without a systematic consideration of the intended (and unintended) consequences of a proposed action. But such economic analysis, carried out by the most eminent economists according to tried and true methodology, is not and cannot be dispositive; it is not precise on its own terms, and I believe it was Professor Einstein who supposedly had a sign over his desk at Princeton saying: "Not everything that can be counted counts and not everything that counts can be counted." CBA (and economic analysis generally) is

valuable, but hardly a silver bullet to resolve all issues – you can't just turn it on and declare the job is done.

There are other aspects of CBA that may become relevant if the Congress seeks to codify the Executive Order and/or provide for judicial review of that process that I will turn to in a moment. But first it is important to recognize that while regulatory agencies in the Executive Branch have been required to prepare Regulatory Impact Analyses (RIA), including analyses of costs and benefits, since at least 1981, there is no similar requirement for Independent Regulatory Commissions (IRCs) – those multi-headed commissions, such as the SEC, FCC, FTC, FEC, CFTC and the Federal Reserve, whose Members do not serve at the pleasure of the President and can be removed from office only for cause.

I raised this anomaly when I testified before this Committee on July 27, 2010, on "Federal Rulemaking and the Regulatory Process." Among other things, I noted that there was no legal barrier to the President's extending the requirement for economic analysis and centralized review to the IRCs, and that both President Reagan and President Clinton declined to do so for political reasons – namely, out of deference to the Congress -- rather than a lack of constitutional authority. The result, however, is that IRCs do not typically engage in the analysis that has come to be expected for Executive Branch agencies; in the 2010 OMB Report to Congress, it appears that roughly half of the rules developed by the IRCs over a ten-year period have no information on either costs or benefits, and those that do have very little monetization of benefits and costs. This is not a good sign because we are about to see a large increase in regulations from the IRCs; in Dodd-Frank alone, there are over 300 provisions saying that agencies shall or may issue rules, most of them directed at IRCs.

Support for requiring IRCs to engage in economic analysis in developing their rules has come from a number of commentators across the political spectrum. Several months ago (February 28, 2011), this Committee held a hearing on "The Administrative Procedure Act at 65," and all three witnesses (from both sides of the aisle) concurred in

the suggestion. Last month (April 7, 2011), Resources for the Future (a centrist think tank) held an all-day conference here in Washington, where various scholars and former government officials from five different IRCs (again, from both sides of the aisle) explored the status of IRC analysis in rulemaking and the agencies' potential to do more. The materials compiled for that conference would provide a solid foundation for your further consideration of this issue.

To be sure, the quality of the work done by Executive Branch agencies -- how solid or sophisticated is the economic analysis -- is mixed but has improved over the years. Some scholars have studied selected agencies and given them mediocre (or even failing) grades, but others have been generally complimentary while suggesting areas for improvement. This should not be surprising because agencies are very different from one to the next, with different cultures and different resources. The latter is important because economic analysis (at least thoughtful, careful, comprehensive analysis) takes time and resources, and the more significant the proposed regulatory action, the more time and resources it should consume. Yet some of the very people who call for more analysis are the first to suggest straight-lining or reducing the agencies' budgets.

An important incentive for Executive Branch agencies to provide high quality analysis is that their work is reviewed and critiqued by OIRA (and other agencies during the inter-agency process) under Executive Order 12866, and ultimately made available to the public. Nothing focuses the mind like knowing that someone will be reading (or listening) to your paper (or presentation). With Executive Branch agencies, OIRA staff regularly review the RIAs that accompany important draft proposed and final rules before they are officially signed by the issuing agency and published in the Federal Register. The OIRA staff communicates its views concerning the RIAs, formally or informally, to the agency staff, who generally pay attention to, and usually heed, the critiques/suggestions from OIRA; if there is disagreement, there is an informal process for "elevating the issue" to the more senior staff or even to the political appointees, where ultimately there is a meeting of the minds.

While the way Executive Branch agencies and IRCs conduct rulemaking is for all practical purposes the same, the differences between the two types of agencies in terms of their structure and their relationship to the President suggests that the review process or the "enforcement" of any requirement for economic analysis should not – possibly, cannot -- be the same without compromising the independence of the IRCs when they do not acquiesce in OIRA's assessment. Congress confronted this very question in the Paperwork Reduction Act, where it provided for OIRA review of information collection requests (i.e., government forms) from all agencies, Executive Branch and IRCs. OIRA was authorized to approve or disapprove paperwork from Executive Branch agencies directly, but when it disapproved paperwork from an IRC, the IRC is able to void any disapproval by majority vote, explaining the reasons for its decision to do so. A variation on that approach for review of the analysis underlying IRC rulemakings could be that OIRA would provide its views in writing to the IRC, and that document would be presented to the Commission (presumably in a public meeting), where the critiques/suggestions could be discussed and disposed of (accepted or dismissed) per the will of the Commission before final approval of the regulatory action.

As noted above, past presidents have been reluctant to extend OIRA's role to the IRCS out of deference to Congress. A Sense of the Congress that such a course would be desirable would go a long way to ameliorate any concerns in that regard. Or Congress could designate an entity outside the Executive Branch as the reviewer of the economic analysis undertaken by the IRCs. Two obvious candidates are the Government Accountability Office (GAO) and the Congressional Budget Office (CBO). The former was given a limited (check the box) role in reviewing and commenting (to Congress) on the regulations issued by IRCs under the Congressional Review Act, and the latter already has analytical capacity that could be directed to this effort. Neither of these entities has the expertise or experience that OIRA has with reviewing economic analyses, but both have the "virtue" of being identified with Congress rather than the President, which may be important to those who read "independent regulatory commission" as independent of only one and not the other political player.

In any event, I am a staunch supporter of requiring regulatory agencies to do economic analysis and of having their work reviewed by OIRA. These are two of the most important foundational principles in Executive Order 12866 (carried over with significant modifications from Executive Order 12291) and recently reaffirmed by President Obama in Executive Order 13653. As noted earlier, Presidents of both political parties have endorsed these principles by incorporating them in their own executive orders and/or implementing them under their predecessor's executive orders. Nonetheless, and with respect, I do not believe that the Congress should seek to codify these principles in legislation.

One of the first provisions in Executive Order 12866 is that "agencies should promulgate only such regulations as are required by law, are necessary to interpret the law, or are made necessary by compelling need . . . ." The agency should then "identify the problem it intends to address (including, where applicable, the failures of . . . public institutions that warrant new . . . action) as well as assess the significance of that problem"; it should "examine whether existing regulations (or other law) have created, or contributed to, the problem . . . and whether those regulations (or other law) should be modified to achieve the intended goal . . ."; and it should "identify and assess available alternatives to direct regulation . . . ." These are the standards that should be met when an agency intends to act. I would suggest that these same standards should be met before Congress takes action.

Given the recent reaffirmation of the salient principles in Executive Order 13653, and the now almost 30-year implementation of these provisions, what is the compelling need to be addressed by legislation? The Executive Branch agencies undertake economic analysis as part of the process of developing rules, and if further analysis is needed, OIRA works with the agency to accomplish that. Moreover, all indications are that the rules being developed by Executive Branch agencies generally meet the "benefits justify costs" standard of the Executive Order. For example, in OMB's 2010 Report to Congress, OMB included data on the cost ($43-$55 billion) and the benefits ($128-$616 billon) of major rules issued by Executive Branch agencies over the most recent ten-year

period (FY 1999-2009). Even if one uses the highest estimate of costs and the lowest estimate of benefits, the regulations issued over the past ten years have produced net benefits of $73 billion to our society. [This cannot be dismissed as a partisan report by the current administration, because OMB issued reports with similar results (benefits greatly exceeding costs) throughout the George W. Bush Administration (e.g., for FY 1998-2008, major regulations cost between $51 and $60 billion, with benefits estimated to be $126 to $663 billion dollars).]

Even if the Executive Branch agencies are not undertaking economic analyses when they should, or are not conducting them with sufficient rigor or proficiency, or are not adequately reflecting those analyses in the framing of regulations as required under the Executive Order – and, again, that case has not been made – would legislating pieces or all of the Executive Oder likely bring about significant change? And are there not alternatives to legislation that would likely have the same or similar salutary effect? Congress has imposed a series of analytical requirements on the agencies over the last 30 years, from the Paperwork Reduction Act, to the Regulatory Flexibility Act, to the National Environmental Policy Act, to the Unfunded Mandates Reform Act, to name just a few, without substantially increasing agency funding to carry out the tasks assigned in those statutes. Before adding another requirement, Congress might rationalize the current set of analytical requirements and/or provide more resources to the agencies to do the analyses and more resources to OIRA to review them. If there is an implementation problem, Congress should address the source of that directly and not just add another requirement that also cannot be implemented. Surely, Congress has a host of alternatives to legislation, including hearings such as this one, by which to monitor agency activity, evaluate current practices, spotlight any deficiencies, and bring public pressure to improve agency performance if that is what is called for.

Second, one of the last provisions in Executive Order 12866 is the statement: "This Executive order is intended only to improve the internal management of the Federal Government . . . ." This statement appears in virtually all executive orders from all administrations. It is not a throw-away clause but rather reflects the nature of

executive orders – that is, orders by the Executive (the President) to those who report to him and for whom he is constitutionally responsible. Executive orders are traditionally the prerogative of the President; they are not subject to notice-and-comment or any other form of public participation in their formulation or to any judicial interpretation or enforcement in their implementation. The history of this particular line of executive orders, from EO 12291 to EO 12866 to EO 13422 to EO 13653, shows that while many of the concepts are the same from one administration to the next, different presidents choose to emphasize different things – e.g., costs and the effects on the economy, openness and transparency, market failure as a basis for regulating, public participation, etc. The differences may be subtle but are nonetheless important indicators of administration policies and preferences, which would likely be lost if the President's prerogatives were preempted by legislation (which is much more difficult to modify than an executive order).

Third, if Congress were to codify the analytical requirements of the Executive Order, it would be amending a host of previously enacted statutes (dating back over half a century or more). At this point, it is unclear how many and which statutes would be amended and what the implications of such an amendment would be, for both the regulated entities and the intended beneficiaries of these statutes. I am referring to the fact that under the Executive Order, agencies are required to conduct economic analysis, but in developing regulations the agencies are, in the first instance, bound by their authorizing legislation. Some legislation is silent on the question of the role of costs in the formulation of regulations; others do not permit consideration of such factors. For example, Section 109(b)(1) of the Clean Air Act provides that the Administrator should set standards for certain pollutants at a level "requisite to protect the public health" with "an adequate margin of safety." The Supreme Court (in a unanimous decision written by Justice Scalia) was emphatic that the Administrator cannot lawfully take account of costs in setting the standards. Whitman v American Trucking Associations, 531 US 457 (2001). For that reason, the Executive Order repeatedly prescribes certain practices "to the extent permitted by law."

However, if provisions of the Executive Order were codified, they would become decisional criteria. As a result, a proposed regulation -- even a regulation under a statute that does not permit the consideration of costs – could not become effective unless, among other things, the "benefits of the intended regulation justify its costs." And, notwithstanding the terms of the underlying statute, the agency would be required "in choosing among alternative regulatory approaches, [to choose] those approaches that maximize net benefits." Such a super mandate would effectively abrogate previously enacted Congressional decisions; one example that comes to mind is the requirement after 9/11 that airlines reinforce the steel in their cockpit doors. And such a super mandate might well delay such time-sensitive rules as those implementing the Migratory Bird Treaty, which must be issued on an annual basis and for which cost data has never been collected or analyzed. Congress can, of course, rewrite the Clean Air Act or the Occupational Health and Safety Act, or the National Traffic and Motor Safety Act, or any other existing authorizing legislation. But it should do so directly, not indirectly by creating a super mandate in the guise of promoting cost/benefit analysis and the consideration of that analysis in developing regulations.

It is important to emphasize that implementation of the Executive Order entails a great deal of judgment, even in those circumstances when costs and benefits are appropriate factors for consideration. As noted above, not all costs and benefits can be quantified and monetized. Yet those that cannot be are, according to the Executive Order (and common sense), "essential to consider." And there are not infrequently questions of disparate effects that should be taken into account, as well as other considerations that should properly come into play. With codification, the easily applied tests will inevitably take precedence over the judgment calls, which are more difficult to explain and document (especially in terms of the weight they are given). This becomes especially problematic if any such codification carries with it judicial review.

The issue of judicial review is difficult for me because I am a lawyer (who greatly respects our judicial system) and I am appearing before the Judiciary Committee. But I

must question whether the federal courts are the proper place to sort through cost/benefit analysis and its role in developing regulations. We are, as you know, a very litigious nation, and there is little disincentive for those who are disappointed at the agency level to take the matter to court. Judicial review of economic analysis will become yet another issue on appeal. Along with the lawyers debating whether the new decisional criteria trump the authorizing legislation, we can expect armies of competing economists with various theories about how to quantify or monetize the diverse direct and indirect effects of a proposed regulation. With Chevron and the hard look doctrine framing the inquiry, one would expect substantial deference to the agency's determinations, but there will nonetheless be substantial time and money (and the ensuing uncertainty) devoted to litigating whether benefits justify the costs and whether the alternative selected is the one that maximizes net benefits, among other concepts that will be placed before the court.

Thank you again for giving me an opportunity to speak to these issues. I look forward to any comments or questions you may have.

Mr. GOWDY. Yes, ma'am. Thank you.
Mr. Furchtgott-Roth, we recognize you for 5 minutes?

TESTIMONY OF HAROLD FURCHTGOTT-ROTH, PRESIDENT, FURCHTGOTT-ROTH ECONOMIC ENTERPRISES

Mr. FURCHTGOTT-ROTH. Thank you, Mr. Gowdy. It is a great honor for me to be here today.

Mr. GOWDY. I might implore you to turn on the——

Mr. FURCHTGOTT-ROTH. I am sorry. Mr. Gowdy, Mr. Cohen, it is a very great honor for me to be here today before this Committee. I have to mention to Mr. Cohen that I was born in Tennessee, and I have noticed the color of your tie today, sir. Thank you very much.

I am aware of the substantial effort that goes into preparing a hearing, an effort on the part of the Members and the staff, and I thank you for those efforts.

I have a written statement that I would like to have entered into the record.

I am trained as an economist and have spent my entire career as an economist, both inside and outside of government, except for three and a half years when I had the honor to serve as a commissioner on the Federal Communications Commission. I bring to this panel not only the perspective of an economist, but also the perspective of an independent agency, one that falls outside of the scope of executive orders, such as 12866 and 13563. I am not saying that those orders are perfect, but the value of those orders is all too apparent in agencies not covered by them, agencies such as the FCC.

The FCC promulgates dozens of rules every year. I regret to tell you that for not a single one of them can we say with any certainty that the benefits exceed the costs because they are never documented.

I can tell you from the perspective of an agency that has never been under these executive orders that Ms. Katzen described, there is a lot that is lost. There is a lot of process that is lost. It is a process that is not there simply for the purpose of process or for the purpose of providing paper. Those are processes that are there for the end result, which is more sensible regulation or rational regulation, and regulation that not just the government officials, but the American public can have some sense that the benefits exceed the costs.

I will summarize my testimony in just a few areas.

The public and our economy benefit substantially from the careful consideration of costs and benefits of regulation. Federal agencies have substantial legal and regulatory requirements, including executive orders, to document their consideration of the costs and benefits that are proposed in new regulations, but those do not apply to independent regulatory agencies. The executive orders are not sufficient, even in Federal agencies, to ensure recent rulemaking, in part because they are not always enforced, and because the public cannot go to the courts to ensure that they are enforced.

I have noticed that the FCC, which has an independent statutory requirement to review its rules every 2 years and ensure that they continue to be necessary, that that provision of law has never been applied. It has been around since the '96 Act, and in the past 15 years I can assure you the commission has never reviewed its rules even once. And the reason is that the commission knows that no

court is going to compel it to do so. Without the ability of court review, I have very great doubts that there will be any enforcement of any statutory requirement for cost and benefit analysis.

I am quite optimistic that the regulatory decisions that would be made if Federal agencies, such as the FCC, would substantially improve if there were requirement to do careful cost-benefit analyses. The results without it are all too apparent. I think even this Committee is going to have a hearing in the coming days on network neutrality. Regardless of your views of whether those rules were good or bad, the fact that those rules were promulgated without a cost-benefit analysis, without some documentation that the commission can say, the benefits of this rule are greater than the cost, I think puts the commission in a very weak position. And had the commission been compelled to go through the type of cost-benefit analysis that Ms. Katzen described, I think the rules probably would have been better, and I think that the commission would have been in a stronger position to defend those rules to the public.

I know the hour is late, and so in the interest of time, I will end my comments at this point.

Thank you very much.

[The prepared statement of Mr. Furchtgott-Roth follows:]

Prepared Statement of Harold Furchtgott-Roth, President,
Furchtgott-Roth Economic Enterprises

I. INTRODUCTION

A. Qualifications

I am president of Furchtgott-Roth Economic Enterprises, an economic consulting firm in Washington, DC. I was a commissioner of the Federal Communications Commission from November 1997 through May 2001.

From June 2001 through March of 2003, I was a visiting fellow at the American Enterprise Institute for Public Policy Research in Washington, DC. In 2007, I was a senior fellow at the Hudson Institute, another policy research organization.

I have worked for many years as an economist. From 1995 to 1997, I was chief economist of the House Committee on Commerce where one of my responsibilities was to work on regulatory reform issues.

My academic research concerns economics and regulation. I am the author or co-author of four books: *A Tough Act to Follow?: The Telecommunications Act of 1996 and the Separation of Powers* (Washington, DC: American Enterprise Institute), 2006; *Cable TV: Regulation or Competition,* with R.W. Crandall, (Washington, DC: The Brookings Institution), 1996; *Economics of A Disaster: The Exxon Valdez Oil Spill,* with B.M. Owen, D.A. Argue, G.J. Hurdle, and G.R. Mosteller, (Westport, Connecticut: Quorum books), 1995; and *International Trade in Computer Software,* with S.E. Siwek, (Westport, Connecticut: Quorum Books), 1993. I received a Ph.D. in economics from Stanford University and an undergraduate degree in economics from M.I.T.

B. Summary of opinions

Based on my years of experience both in government and in the private sector, and based on my training as an economist, I find the following:

- The public and our economy would benefit substantially from the careful consideration of the costs and benefits of regulations.
- Federal agencies have substantial legal and regulatory requirements, including Executive Orders 12866 and 13563, to document their consideration of the costs and benefits of proposed and new regulations
- The executive orders are not sufficient to ensure reasoned rulemaking.
- The FCC does not effectively document or weigh the benefits and costs of its rulemakings.

- Outside parties that participate in FCC proceedings do not insist that the agency consider costs and benefits of regulations because of the lack of judicial review.
- FCC regulatory decisions would likely improve with greater consideration of costs and benefits.
- Assigning to a federal agency the responsibility for reviewing the compliance of all agencies—including independent agencies—with requirements for cost-benefit analyses could help standardize practices and give the public a more predictable standard of analysis.

II. THE PUBLIC AND OUR ECONOMY WOULD BENEFIT SUBSTANTIALLY FROM THE CAREFUL CONSIDERATION OF THE COSTS AND BENEFITS OF REGULATIONS

Evaluating the costs and benefits of an activity is not an idle academic exercise. As individuals, as families, as businesses, and as other organizations, we constantly evaluate activities. We are reluctant to delegate to others those decisions about which activities we engage in. We reject those activities whose costs are too high for the possible benefits. We engage in those whose benefits exceed our estimate of costs.

We make these cost-benefit analyses with varying degrees of formality. Individuals and families are informal. We reflect on those decisions that we make for ourselves as individuals. We may explain to our families decisions about why we make certain decisions, such as reducing our driving as gasoline prices increase.

Businesses make decisions supported by documents. Woe be to the vice president of a company who proposes an investment without documents explaining the possible returns, examining them in detail, and reviewing possible alternative investments. Civic organizations do the same.

A publicly traded company that makes major decisions without documentation is reckless. A privately held company making such decisions would have difficulty attracting investors. Investors insist on some documentation of decisions not because they are obsessed with process but rather because they are obsessed with results.

Good documentation helps lead to good results. Good documentation leads to rational decisions— decisions that can be reviewed and vetted, decisions that can be replicated if they yield positive results, and decisions that can be avoided in the future if the results are negative.

We insist on documentation and rational decision-making with benefits expected to exceed costs by our private companies and civic organizations. Yet, in government, we all too often insist on documenting practically everything except the common-sense requirement that the benefits of our federal agency decisions should exceed their costs.

It may well be that many—or hypothetically even all—federal rules have benefits that exceed their costs. But such a statement today would be an unverifiable expression of faith rather than verifiable fact. We cannot possibly know which federal rules have benefits that exceed their costs because our government agencies too often fail to document such benefits and costs.

The net result almost certainly is that we have some rules whose costs exceed their benefits. Perhaps even worse, we cannot identify those harmful rules and distinguish them from those that are beneficial.

Bad government regulation harms America. It weakens our economy, lessens incentives to invest in America, destroys American jobs, and makes less productive the jobs that remain. It reduces the choices we have as consumers taking many options away from us and unnecessarily raising the prices of the choices that remain. It robs us and our children of the belief that our government is always in the right. We are a poorer country as a result of harmful regulation, regulation that we cannot even begin to identify.

This result is not a surprise to the American public. Your constituents see it every day. We see it in our daily lives in toilets that do not work well as the result of government regulation. We see it in manufacturing plants that have gone elsewhere because of government regulations. We see it in security screening at airports. We see it in employment rules that ordinary Americans cannot understand.

Ask your constituents about bad federal regulations, and you will hear an earful. Many if not most Americans have their favorite stories about a bad federal regulation. Some of the stories don't even pertain to federal rules—such as automatic dish washing detergents that no longer work. Washington regulation has become so discredited in the eyes of many Americans that it is the presumed source of much that ails America, whether it is the actual culprit or not.

Americans don't understand Washington regulation, and Washington refuses to explain it. The result is not merely bad regulation that harms our country but a corrosive mistrust of Washington and our government in general.

We are a better country than this. America deserves regulation that is accountable. We can do a much better job, and it begins with having better documentation of the benefits and costs of each regulation.

Let me describe the value of documented cost-benefit analyses in at least two different stages in the regulatory process:

1. *Notices of proposed rulemaking*—One of the most important aspects of the Notice of Proposed Rulemaking process is to obtain guidance from the public about how best to craft a rule. A federal agency should solicit ideas from the public first rather than develop a predetermined rule before seeking public comment. An agency that can articulate in detail the possible costs and benefits to various segments of our economy of each proposed rule and alternatives to it demonstrates some thoughtful analysis behind the proposed rule. And the agency can explain other forms of the rule, including no new rule, that can be considered. Part of the reason to make these cost-benefit analyses public at the NPRM stage is to enable the public to vet the analyses. Can the analyses withstand public scrutiny? Are they internally consistent? Do the numbers make sense? Here is what the federal agency identifies as the likely benefits and costs of the regulation. Here is what federal agency identifies as the likely distribution of those benefits and costs.

2. *Final rules*—After it has received comments on the reasonableness of the cost-benefit analyses for a proposed rule, an agency can modify not only the proposed rule but modify the cost-benefit analyses as well. The final cost-benefit analyses should present in some detail the expected levels and the expected distributions of the expected benefits and expected costs of the final rule. The final cost-benefit analyses should review the comments the agency received on the initial cost-benefit analyses and should explain how and why the final cost-benefit analyses were modified to accommodate the comments, or why certain comments were disregarded. As important, the final costs-benefit analyses should present milestones that the agency expects the rule to accomplish, milestones by which the rule can be reviewed in the future. If the rule is intended to reach goal Y in two years, the agency should be willing to have the rule evaluated in 2 years based on whether or not goal Y was in fact reached or not. In much the same way, a business makes an investment and projects that it will be cash-flow positive in two years. In two years, the board and the shareholders can evaluate both whether the investment met its targets and also whether management had good business acumen in the past and is worthy of being trusted to make decisions in the future.

III. FEDERAL AGENCIES HAVE SUBSTANTIAL LEGAL AND REGULATORY REQUIREMENTS, INCLUDING EXECUTIVE ORDERS 12866 AND 13563, TO DOCUMENT THEIR CONSIDERATION OF THE COSTS AND BENEFITS OF PROPOSED AND NEW REGULATIONS

The processes that I describe above are not academic exercises. The assessments of costs and benefits for both proposed and final rules are required by Executive Order 12866. The review is to be comprehensive, consider all alternatives, including not regulating: "In deciding whether and how to regulate, agencies should assess all costs and benefits of available regulatory alternatives, including the alternative of not regulating."[1] The objective is to ensure that benefits not only exceed costs, but that benefits exceed costs by as much as possible: "Further, in choosing among alternative regulatory approaches, agencies should select those approaches that maximize net benefits (including potential economic, environmental, public health and safety, and other advantages; distributive impacts; and equity), unless a statute requires another regulatory approach."[2]

Moreover, the Executive Orders instruct federal agencies to evaluate not only new rules but existing rules as well. Executive Order 12866 requires agencies to consider whether existing rules may contribute to a problem that new rules are intended to correct: "Each agency shall examine whether existing regulations (or other law) have created, or contributed to, the problem that a new regulation is intended to

[1] Executive Order 12866, Section 1.
[2] Ibid.

correct and whether those regulations (or other law) should be modified to achieve the intended goal of regulation more effectively."[3]

Executive Order 13563 goes further and requires federal agencies to have periodic reviews of existing "significant" rules:

> Within 120 days of the date of this order, each agency shall develop and submit to the Office of Information and Regulatory Affairs a preliminary plan, consistent with law and its resources and regulatory priorities, under which the agency will periodically review its existing significant regulations to determine whether any such regulations should be modified, streamlined, expanded, or repealed so as to make the agency's regulatory program more effective or less burdensome in achieving the regulatory objectives.[4]

Each agency may have additional cost-benefit analysis requirements under its organic statutes. Section 11 of the Communications Act, for example, requires the Federal Communications Commission periodically to review all of its rules every two years and eliminate those that are no longer necessary.

IV. THE EXECUTIVE ORDERS ARE NOT SUFFICIENT TO ENSURE REASONED RULEMAKING

If fully implemented and enforced, Executive Orders 12866 and 13563 would go far towards ensuring reasoned regulation in the federal government. At least two limitations have prevented the full implementation of these Orders.

First, as executive orders, these documents are not laws or rules under which interested parties can seek compliance or enforcement either through the executive branch agencies themselves or through the courts.

Second, the Orders apply only to executive branch agencies, not independent federal agencies. The executive orders do not cover the Federal Communications Commission, on which I served, and other independent agencies.

V. THE FCC DOES NOT EFFECTIVELY DOCUMENT OR WEIGH THE BENEFITS AND COSTS OF ITS RULEMAKINGS

While the Executive Orders 12866 and 13563 are insufficient, they provide a framework for the evaluation of regulation that is entirely absent at independent agencies. It would help the quality of regulatory-decision making at the independent agencies to be required to comply with the executive agencies.

Perhaps partly because it is not covered by the executive orders, the FCC does not directly weigh or even itemize the benefits and costs of a particular regulation. The FCC does not systematically consider alternative forms of regulation including no regulation. The FCC certainly does not focus on the alternative with the greatest net benefit. The only presentation of the costs and benefits of a regulation is an appendix for the Regulatory Flexibility Act. This appendix is at best an afterthought: a short, rarely read boilerplate passage that is outside the deliberative process. Sometimes it is forgotten altogether. I have seen little change in the regulatory analyses at the FCC since I left the Commission.

I have seen even less attention at the FCC to the biennial review of all regulations under Section 11 of the Communications Act. After 15 years of Section 11 being in the statute, the FCC has yet to review meaningfully all of its rules even once. Indeed, many if not most of its rules have never been formally reviewed at all. Those that have been reviewed have not documented cost-benefit analyses.

Of course, the FCC, like every other federal agency, implicitly considers the costs and benefits of proposed and final rules. But the costs and benefits are rarely if ever formally presented. Rather than explain exactly how and why benefits would be greater than costs, and rather than explain the distribution and level of those benefits and costs, the Commission routinely recites the magic words—"the public interest"—as if it were possible for rules which plausibly had costs in excess of benefits to be in the public interest.

VI. OUTSIDE PARTIES THAT PARTICIPATE IN FCC PROCEEDINGS DO NOT INSIST THAT THE AGENCY CONSIDER COSTS AND BENEFITS OF REGULATIONS BECAUSE OF THE LACK OF JUDICIAL REVIEW

The absence of judicial review of the regulatory process means that both the federal agency and the outside parties do not take the regulatory process seriously. If Congress were to alter the regulatory process, it would be important to have mechanisms whereby courts can review federal agency decisions.

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[3] Ibid., Section 1 (b) (2).

[4] Executive Order 13563, Section 6(b).

Absent the prospect of meaningful judicial revision, outside parties that participate in FCC proceedings do not insist that the agency fully comply with either the Regulatory Flexibility Act or Section 11 of the Communications Act. Outside parties are reluctant to invest in an effort that will annoy a federal agency but have little prospect of a judicial remedy. Consequently, few if any parties bother to review either the initial and final regulatory flexibility analyses, much less comment on them.

VII. FCC REGULATORY DECISIONS WOULD LIKELY IMPROVE WITH GREATER CONSIDERATION OF COSTS AND BENEFITS

Careful and thoughtful consideration of costs and benefits of regulation could substantially improve the regulatory decision-making process at the Federal Communications Commission. Whether one agrees or disagrees with the new rules, it is impossible to determine from the Commission's record whether the benefits of the new rule exceed the cost. The Commission provided no cost-benefit analysis for the new rule, nor did it explicitly consider and calculate the benefits and costs of alternative rules, including no regulation.

The Commission is currently considering a wide range of new rules, some dealing with compensation among telecommunications companies, some dealing with spectrum, and still others dealing with the future of the broadcast industry. None of the proposed rules under consideration has a meaningful cost-benefit analysis. Nor do the proposed rules have a range of specific alternatives, including the option of no regulation. Based on documents that the FCC has provided the public, it is impossible to determine for each rule what the Commission considers to be either the range of benefits or the range of costs—and who will pay for those costs. The public has no basis to comment on whether the Commission's assessment of benefits and costs of regulation are accurate because there is no such assessment.

Not infrequently, Congress itself is alerted to new rules at the Federal Communications Commission that raise public concern. Late last year, the FCC adopted new rules for network neutrality. The FCC provided no meaningful assessment of costs and benefits in the final rules, nor specific consideration of alternative forms of regulation including no regulation. The FCC has not helped its cause by failing to provide at various stages of the regulatory process clear statements about the assessment of benefits and costs of its network neutrality rules. Had the Commission presented to the public such an assessment of the costs and benefits of these rules, and had the Commission accepted and incorporated comments on such an assessment, the Commission would today be in a much stronger position to defend those rules.

Instead, the Commission is in the weak position of asking Congress and the public to trust its judgment to regulate sensibly. It cannot point to a document that lists the benefits and costs of the new rules and explains in straightforward terms how the benefits and costs were assessed, who will likely receive the benefits, and who will likely pay the costs. Nor can the Commission point to such a document that has been vetted by the public and modified to reflect public comment.

The Commission's neglect of accounting for costs and benefits of regulation is not limited to network neutrality. The Commission proposes and promulgates dozens of new rules each year, some more controversial than others. For none of the rules, controversial or otherwise, does the Commission prepare a document that either an economist or an ordinary citizen would consider a full accounting of the costs and benefits of each of the proposed or new rules.

VIII. ASSIGNING TO A FEDERAL AGENCY THE RESPONSIBILITY FOR REVIEWING THE COMPLIANCE OF ALL AGENCIES—INCLUDING INDEPENDENT AGENCIES—WITH REQUIREMENTS FOR COST-BENEFIT ANALYSES COULD HELP STANDARDIZE PRACTICES AND GIVE THE PUBLIC A MORE PREDICTABLE STANDARD OF ANALYSIS

It would be useful to designate a federal agency with responsibility for ensuring the uniform application of cost-benefit analyses across different agencies so that the public can more easily interpret agency findings.

Mr. GOWDY. Thank you. I will ask a series of questions, and then recognize the gentleman from Tennessee.

Mr. Furchtgott-Roth, picking up on what you said toward the end, why is it that no President to date has included a cost-benefit

analysis in the executive orders for independent agencies? They could have done so, right?

Mr. FURCHTGOTT-ROTH. I believe they could have. I believe that one of the limitations is that most independent agencies, certainly when I was at an independent agency, I would have been reluctant to feel guided by an executive order. And that is, I think, one of the benefits of having a statutory remedy, that a statute definitely applies to an independent agency. It is an open question as to which executive orders apply to independent agencies. And the string of executive orders on cost-benefit analysis explicitly do not apply to independent agencies.

Mr. GOWDY. What do you think the result of a cost-benefit analysis would be with respect to net neutrality? Walk me through what that analysis would be like.

Mr. FURCHTGOTT-ROTH. The agency would have been required to at least put on paper what it views as the benefits of the rule and what it views as the cost of the rule. And it would have had to explain those benefits and costs.

The commission does not have to do that, and what it does is it has other statutory requirements. I am not saying that it does not follow those. It does, but the net result we do not know because no one has ever, at least the commission has never done that. And it might have come up with a very different set of rules had it been required to have that benefit-cost analysis.

Mr. GOWDY. Mr. Holmstead, toward the end of your testimony, you made a reference to friendly lawsuits allowing folks to skirt oversight. Can you give an example of that or extrapolate on that some?

Mr. HOLMSTEAD. There are a couple of recent examples where an environmental group brings a lawsuit trying to argue that EPA should have issued a regulation. In at least two recent cases, it is far from clear whether EPA did have that obligation, if anybody had been kind of litigating that straight up, that the environmental groups did not really have much of a case. Notwithstanding that fact, EPA entered into a consent decree in one case to issue something called new source performance standards to reduce greenhouses gases from coal-fired power plants and from refineries, which had been a big target of regulation. There is no legal basis for that suit, especially to get them to issue the greenhouse gases. Notwithstanding that fact, they entered into a consent decree. They went to the court to get that consent decree blessed, and the consent decree includes a schedule which is extremely aggressive. And as a result, because the consent decree has a date that has to be met by court order, OMB might get 2 weeks to review a rule that is going to cost several billion dollars. And it completely prevents the kind of normal interaction and analysis that would go on.

And I could give you a number of examples for the record, but they are, you know, allies of the agencies that enter into these lawsuits and certainly have the results, if not the intention, of avoiding regulatory oversight.

Mr. GOWDY. Are there instances where you can cite agencies double counting the benefits, single counting the cost?

Mr. HOLMSTEAD. And, again, I keep coming back to the Utility MACT Rule because it is a particularly egregious example. The

heart of the Clean Air Act is designed to force states to regulate, to meet these standards. And so, there are regulations on the books today that require states to reduce flying particles. And now, EPA has done this Mercury MACT Rule, which is supposed to be about mercury, but EPA says, well, we are going to get all these benefits from flight particles. And they take credit, again, for benefits that they are taking for in this other regulatory program. So, that may be not a very good way of explaining, but, yes, there are cases where EPA does double count the benefits in justifying different rules.

Mr. GOWDY. Ms. Katzen, Cass Sunstein, I believe, I know he wrote a book on judicial review. I think he was a law professor and now currently with the current Administration. If my research is correct, he supports an executive order that allows judicial review?

Ms. KATZEN. I would be reluctant to speak for him now. But I would say——

Mr. GOWDY. I was going to ask you for yourself on whether or not you think that is a good idea.

Ms. KATZEN. No. I mean, I will speak to it, and, no, I think it is a very bad idea. During the Clinton administration and during the Bush administration, George W. Bush administration, there were attempts to provide for judicial review of those processes. And in both instances, both the Democratic and the Republican administrations, took the position that it would not be productive. As I said, it is a question of where is the proper forum to have that kind of analysis reviewed. There are issues whether, it be forum shopping to find the right court that will stop something or other issues. It is another level as part of the process.

But judicial review does exist. If there are problems with the regulation, it will be challenged in court. And one of the basic tenants of administrative law is that it has to pass the arbitrary and capricious standard. It has to have substantial evidence. That material is in the record. But to have an additional clause that goes to the cost-benefit study and whether the benefits justify the costs, when you have part of the benefits being qualitative, not quantitative, I find it just mind blowing. And I have been practicing law for over 40 years. To ask a Federal judge to go through that, it strikes me as being really quite an extension.

If I may, Mr. Gowdy, I would like to answer your very first question because——

Mr. GOWDY. I will ask permission from Mr. Cohen because I am 2 minutes over my time limit. So, I will——

Mr. COHEN. Permission not granted.

Mr. GOWDY. Permission not granted, so I am going to recognize the gentleman from the great state of Tennessee, Mr. Cohen?

Mr. COHEN. Thank you. Ms. Katzen, answer the first question?

Ms. KATZEN. President Reagan was the first one to write the executive order. His advisers asked the Office of Legal Counsel at the Department of Justice whether the President had the authority to extend the economic requirements and centralized review to the independent regulatory commissions. He was told yes. He declined to do so for political reasons, not legal reasons. He declined to do so because he did not want to offend Congress.

When we drafted the executive order for President Clinton in 1993, we went back to OLC. We asked them the exact same question. They gave us the same answer. They said, yes, he has the authority to do it. The President chose not to extend it for political reasons, not legal reasons. He did not want to offend Congress.

It is for that reason that in my written testimony I give you several routes that you could take to achieve this, whether it be a sense of the Congress that the President could do it, or you self-designate an entity. It is there. It is possible.

Mr. COHEN. Well, if Congress did it, little chance of offending Congress.

Ms. KATZEN. If Congress did it for the IRCs, there would be little chance of offending Congress, particularly if the entity was who was going to review it was OIRA.

Mr. COHEN. Let me ask you this. It does seem a bit, Ms. Katzen, in your testimony, and then, gentleman, if you all would like to add your comments. If you give the courts the right to make these decisions on the cost-benefits analysis, I do not know what their standard would be and how they would do it. And since of it is qualitative, are you not letting the courts then legislate and take value judgments that they have and make them law? And is that not somewhat antithetical to kind of the idea that you are supposed to interpret the law and not make the law?

Mr. HOLMSTEAD. Can I answer?

Ms. KATZEN. Well——

Mr. COHEN. Please, Mr. Holmstead?

Mr. HOLMSTEAD. We are not asking courts to make those judgments. As I understand it, we are asking them to review whether the agency made a good faith effort to do that. That is a much easier inquiry for the courts than many of the things that they view today. I mean, if you look at the statutory provisions that judges deal with under the Clean Air Act, under the Clean Water Act, under the FCC, all sorts of things, there are much more complicated questions than whether the agency made a showing that the benefits justify the costs.

So, I do not think it is a meaningful change. What I do think, though, is that agencies would take the requirement much more seriously if it were enforceable. So, it seems odd to me to say, well, we believe in these principles; we just do not want them to be enforced.

Ms. COHEN. Ms. Katzen?

Ms. KATZEN. If you read Dr. Graham's testimony, he says that judicial review should extend to whether the agency has followed the guidelines set out by OMB in Circular A-4. I invite you, if you have insomnia, to read Circular A-4. It is 50 pages single spaced of alternative ways of calculating everything under the sun and throughout it says, "where appropriate," "where appropriate, where appropriate."

Mr. Holmstead sas the inquiry is did they do it? I have not heard good faith. Has the agency met the requirements? Do the benefits justify the costs? Has the agency chosen the alternative that maximizes net social benefits? Those are result questions, not process questions.

Mr. COHEN. And that seems like, as I said—Mr. Furchtgott-Roth, if you would like to comment. It just seems to me that it does give a lot of discretion to the judge to make policy, which the Congress should be doing?

Mr. FURCHTGOTT-ROTH. Mr. Cohen, the FCC is challenged in court on its rules on a routine basis. Many of those challenges have to do with compliance with the APA. Was there adequate public notice? Did the findings reflect the comments that were provided to the agency?

The commission candidly has a very poor track record in court. The courts deal with that agency all the time, and I do not think it is the case that the courts necessarily get involved in legislating as you described it. A lot of times they simply say, you know, this is not in your statutory authority to make this judgment.

I think right now, parties can and do go to courts on everything from they did not provide adequate notice in the NPRM, they did not do this, they did not do that. But if someone came to a court and said, this agency did not put on paper that the benefits of the rule exceeded the cost, the court would say, well, you know, they are not required to.

Candidly, as a citizen, I find that result to be so profoundly disturbing for a government that requires agencies to document practically everything under the sun, but to say they are not required to demonstrate to the American public that the benefits of a rule are greater than the cost, I do not get it.

Mr. COHEN. Well, I have a plethora of additional questions, but my time has expired. I yield back to the Chair.

Mr. GOWDY. I am sure Mr. Cohen joins me in expressing the frustration of having such a distinguished and learned panel fall on an afternoon where our vote schedule impacted your schedule and our ability to have this hearing in a timely fashion. So, it was a treat to hear from each of you. I compliment you on your acumen, your professionalism, and, frankly, your civility toward one another.

Without objection, all Members will have 5 legislative days to submit to the Chair additional written questions for the witnesses, which we will forward and ask the witnesses to respond as promptly as they can so their answers may be made pat of the record.

With that, again, my apologies to all for disrupting more of your afternoon than we were originally planning on doing. And we thank you.

[Whereupon, at 6:02 p.m., the Subcommittee was adjourned.]

APPENDIX

Material Submitted for the Hearing Record

OPENING STATEMENT: CONGRESSMAN GOWDY

Each week I hear from my constituents in the Fourth District of South Carolina about the impact of agency regulations on their lives and businesses. Regulations have the power to create or destroy American jobs and American economic growth, and as a result, regulatory agencies must be careful not to issue regulations that will impede our country's economic recovery.

One way to promote reasonable, beneficial agency regulations is to require agencies by statute to follow common sense requirements that Presidents of both parties have prescribed by executive order. These include, for example, requirements to search for the least burdensome regulatory alternative, to assure that the benefits of a regulation outweigh the costs, and to determine whether defects in *existing* regulations are actually causing the problem the agency thinks it needs to solve.

President Reagan, both Presidents George H.W. Bush and George W. Bush, President Clinton and President Obama all have embraced one formulation or another of good-government

regulatory principles like these. Such principles add substantial meat to the bones of the basic rulemaking procedures set forth in the Administrative Procedure Act.

By codifying these principles in the APA, Congress could make them permanent features of the regulatory landscape. This would assure consistency and good practice across all federal agencies – including independent agencies that executive orders have not reached.

Codification of these principles also could assure judicial review. Under the past executive orders, judicial review of these requirements has been specifically excluded. As a result, the ability of the judicial branch to provide effective checks and balances on overreaching agency power has been substantially limited.

Our witnesses today have tremendous knowledge about the requirements of the rulemaking executive orders, the usefulness of executive orders for regular and independent agencies, and the potential for codification and judicial review to contribute to good government in the rulemaking process. They also can help us vet which of these requirements would be most suitable for

codification. Finally, they can help us to identify which additional statutory concepts, if any, we should introduce to prevent agencies from "gaming" the requirements to evade their spirit while seeming to follow their letter.

As a result, today's hearing should help us to frame legislation that will improve the rulemaking process based on bi-partisan, time-tested principles. Such legislation has the potential to encourage the economic growth and job creation that our citizens need.

I look forward to our witnesses' testimony and reserve the balance of my time.

Statement of the Honorable Steve Cohen
For the Hearing on "Cost-Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"
Before the Subcommittee on Courts, Commercial and Administrative Law

Wednesday, May 4, 2011 at 1:30 p.m.
2141 Rayburn House Office Building

Today we consider three issues concerning agencies' use of cost-benefit analysis. First, should Executive Orders 12866 and 13563, which outline requirements for cost-benefit analysis by agencies and Presidential review of agency rules, be codified? Second, should Congress provide for judicial review of agencies' compliance with the cost-benefit analysis requirements of those executive orders? Third, should the cost-benefit analysis requirements of these executive orders apply to independent agencies?

As we will hear, there are some concerns about codifying the executive orders that currently outline the requirement that federal agencies engage in cost-benefit analysis.

For one thing, it is not entirely clear why there is a need for codification. While it is true that executive orders can be revoked at any time, a bipartisan consensus appears to have arisen over the last 40 years that some form of cost-benefit analysis is useful to the rulemaking process, and the basic contours of such analysis have remained largely the same for the last generation. Therefore, the risk that future administrations will simply abandon cost-benefit analysis seems remote.

That being said, it is also true that every administration has tried to refine existing cost-benefit analysis criteria, either to reflect changing circumstances or its own particular views on cost-benefit analysis. It seems healthy for the regulatory system to retain this type of flexibility. Codification may threaten to take away that flexibility.

Additionally, although I am a firm believer in Congress's role in overseeing and shaping the regulatory system, I appreciate that there may be legitimate separation of powers concerns with simply codifying the language of executive orders governing Presidential review of agency performance. Congress should be cautious in treading on the President's ability to oversee executive branch functions.

Regarding the question of whether Congress should make available judicial review of agencies' compliance with cost-benefit analysis criteria, there seems to be a real risk that this would simply open the door to frivolous lawsuits by industry as a means of slowing down rulemaking and ultimately defeating rules that may be perfectly valid and which maximize net benefits.

Despite its appearance of mathematical precision, I think all of our witnesses would agree that cost-benefit analysis involves a considerable level of subjective judgment when quantifying certain costs and benefits. I can easily see these types of judgment calls by agencies leading to endless arguments in court over whether cost-benefit analysis was conducted properly in a given case. Courts' second-guessing of such judgment calls also seems to fly in the face of the traditional deference that courts have shown to agency decision-making.

The potential for the manipulation of a judicial review process to instigate expensive, time-consuming litigation that slows down rulemaking without necessarily improving it also worries me.

As to the proposal for extending the existing cost-benefit analysis requirements of Executive Orders 12866 and 13563 to independent agencies, on its face it strikes me as a reasonable and logical idea. Of course, I would need to know how such agencies' independence will be protected if such a move were made. I would also reserve final judgment until I see a more specific proposal – whether legislative or not – before committing firmly to supporting it.

I welcome our witnesses and look forward to learning their insights on these issues.

**Statement of the Honorable John Conyers, Jr.
for the Hearing on "Cost-Justifying Regulations: Protecting
Jobs and the Economy by Presidential and
Judicial Review of Costs and Benefits"
Before the Subcommittee on Courts,
Commercial and Administrative Law**

**Wednesday, May 4, 2011, at 1:30 p.m.
2141 Rayburn House Office Building**

By my count, today's hearing will be the *sixth* that this Subcommittee has held on the subject of regulatory reform.

I note, however, that this Subcommittee has not held a *single* hearing this Congress on the ongoing home foreclosure crisis that is ravaging communities across our Nation.

Nor, has the Subcommittee spent any time at all examining what could very well be the next subprime mortgage crisis, namely, the tremendous educational loan debt that students are being saddled with in an a recessionary economy.

Rather, this Subcommittee appears to be steadfastly committed to finding ways to promote the interests of big business by hobbling and slowing down the administrative rulemaking process.

And, what would be the impact of slowing down the rulemaking process? It means that rules intended to protect the health and safety of American citizens will take longer to promulgate and become effective.

We are talking about rules that protect the quality of the air we breathe, the water we drink, and the food we consume.

And, we are also talking about rules that ensure the safety of the cars we drive, the airplanes that convey us, and the places where we work.

Slowing down the promulgation of these rules would only serve to put Americans at greater risk, while allowing polluters, makers of dangerous toys, and manufacturers of tainted drugs more time to avoid regulation.

While admittedly the rulemaking process is probably not perfect, some of the proposals we will be discussing today will make that process much worse, not better.

I start, however, with a proposal that I may be open to supporting, namely,

the extension of cost-benefit analysis requirements to independent agencies. This may possibly be appropriate given the fact that other federal agencies are already required to conduct cost-benefit analysis.

If these requirements are extended to independent agencies, however, Congress must continue to ensure that these agencies remain independent.

These agencies are accorded their independent status by Congress to insulate them from the political whims of a particular Administration.

Extending cost-benefit analysis requirements should not be used to undermine the independence of these entities.

I also sincerely hope that this proposal is not being pushed simply as a way to slow down or undermine the implementation of major reform legislation, such as the Dodd-Frank Wall Street Reform Act. If I detect even a hint of that being the true motivation for this proposal, I will feel compelled to oppose it.

Turning to the two more problematic proposals, one of these proposals would codify the cost-benefit analysis requirements outlined in Executive Orders 12866 and 13563.

As we noted during prior hearings on the administrative rulemaking process, this proposal purports to offer a solution in search of a problem based on faulty assumptions and conclusions.

As all of today's witnesses acknowledge, Administrations of both political parties over the last 40 years have endorsed Presidential review of rulemaking and the application of cost-benefit analysis as part of that review process.

This strongly suggests that we have a system in place that is not broken and that does not need to be fixed.

In contrast, the proposed fix would hamstring future Administrations from being able to tweak cost-benefit analysis requirements to meet changing circumstances or to respond to new findings about the administrative process, as every President since Richard Nixon has done.

Codification will deny the Executive Branch the flexibility it needs to properly oversee agency rulemaking.

If we really want to improve the rulemaking process, we should be considering whether agencies need more resources to better perform their

rulemaking functions, rather than simply adding requirements for analysis.

Moreover, given the numerous regulatory analyses that agencies are already required to perform by statute, we should be considering whether to *reduce*, rather than increase, regulatory analysis requirements.

Another proposal that we will consider today – mandating judicial review of agency compliance with their cost-benefit analysis criteria – is equally problematic.

Again, if we truly are concerned with streamlining the rulemaking process, mandating judicial review of agencies' use of cost-benefit analysis will achieve the opposite.

I have tremendous respect for the federal courts and have often been at the forefront of increasing judges' pay and of giving judges more authority to decide questions that they are capable of deciding.

And, I do not share the knee-jerk hostility that many of my colleagues, especially those in the Majority, have towards judges and judicial decision-making.

The courtroom, however, may not be the best forum for reviewing agencies' application of cost-benefit analysis requirements.

Many of the cost-benefit analysis criteria that are required by Executive Order 12866 are deliberately broad and require substantial judgment calls by agencies.

Additionally, quantifying benefits and costs of regulation can be difficult, even for those with the requisite background in economics and in the agency's substantive policy areas.

While agencies are required to quantify benefits and costs or to explain why it cannot do so, a judge – who lacks the agencies' expertise both in economics and in the substantive policy area of the rule at issue – would not be in a position to review meaningfully an agency's conclusions.

Additionally, providing for judicial review opens the door to abusive litigation by well-funded business entities and others who oppose regulations generally, which would make rulemaking more costly and expensive without maximizing the benefits or minimizing the costs of regulation.

Congressman Henry C. "Hank" Johnson, Jr.

Statement for the Hearing on "Cost-Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"

May 4, 2011

Mr. Chairman, with all due respect, I take issue with the attack on regulations. Regulations are not the enemy. My colleagues on the other side of the aisle want to rein in government regulations because of cost.

However, in many instances, the protections we receive from regulations outweigh the costs. They have guarded us against risks like lead in paint and poisons in our drinking water.

The majority purports that the purpose of this hearing is to consider whether to codify cost-benefit analysis requirements, whether cost-benefit analysis should be subject to judicial review, and whether cost-benefit analysis requirements should apply to independent regulatory agencies.

I have some serious concerns about imposing codification and judicial review requirements. Codification and judicial review could result in the unintended consequence of hampering the regulatory process. As a former magistrate judge, I know first-hand that our courts are facing tremendous back-logs.

Are our courts really equipped to handle this, especially in a time when the Republican controlled House is obsessed with cutting costs? Adding a judicial review requirement could also lead to abusive litigation with individuals bringing suit solely to slow down the rule-making process.

I am anxious to hear from our witnesses today about how we can strike the proper balance that is needed to protect the health and safety of all Americans and grow our economy and create jobs. These concepts are not mutually exclusive of each other.

Thank you and I yield back the balance of my time.

COALITION FOR SENSIBLE SAFEGUARDS

May 4, 2011

The Honorable Lamar Smith, Chairman
The Honorable John Conyers, Ranking Member
U.S. House Judiciary Committee
U.S. House of Representatives
Washington, DC 20515

The Honorable Howard Coble, Chairman
The Honorable Steve Cohen, Ranking Member
U.S. House Judiciary Committee, Subcommittee on Courts, Commercial and Administrative Law
U.S. House of Representatives
Washington, DC 20515

RE: Hearing on "Cost-Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"

Dear Mr. Smith, Mr. Conyers, Mr. Coble, and Mr. Cohen:

As the Subcommittee on Courts, Commercial and Administrative Law continues to examine the value of federal regulations during today's hearing, the Coalition for Sensible Safeguards cautions Congress against acting to weaken the existing regulatory system that has served American families and consumers well.

The Coalition for Sensible Safeguards is a coalition of consumer, labor, scientific, faith, research, public health, public interest, and environmental groups, joined in the belief that our country's system of regulatory safeguards provides a stable framework that secures our quality of life and paves the way for a sound economy that benefits us all.

Critics of existing regulations and the process for the promulgation of regulations have grossly distorted the facts in order to convince members of Congress that legislation is needed to further constrain agencies' ability to issue regulations in a timely manner. We believe that additional Congressional action to constrain agencies will endanger our economy as well as all Americans' health and safety.

For the following reasons there is no need to further constrain the ability of agencies to issue regulations:

The benefits of regulations consistently outweigh the costs.
Supporters of efforts to further slow the process of agencies promulgating rules frequently cite the cost of regulations. But they fail to note their benefits. Under existing law the OMB already is charged with

estimating the costs and benefits of proposed regulations. George W. Bush's OMB found that from FY 1998-2008 the costs of regulations ranged from $51 billion to $60 billion and the benefits ranged from $126 billion to $663 billion. Even if one assumes the high range of costs and the low range of benefits, the benefits outweighed the costs by more than $60 billion. Similarly, the regulations finalized by the Obama Administration over the past two years have had benefits far in excess of their costs, according to OMB.

Worker safety.

Regulations have helped to decrease deaths. Immediately prior to the creation of OSHA in 1970, an average of 14,000 workers died annually from occupational injuries. In 2009, despite a workforce that is twice as large, 4,340 workers were killed on the job.

More remains to be done. In addition to the more than 4,000 workers killed on the job every year, almost 50,000 Americans die every year from occupational illnesses and more than 4.1 million workers are injured. The cost of these injuries and illnesses is enormous—estimated at $159 billion to $318 billion a year for the direct and indirect costs of disabling injuries. Additional safeguards to prevent these injuries and illnesses, along with stronger enforcement of existing laws, would save thousands of lives and billions of dollars.

Clean Air.

In March 2011, the Environmental Protection Agency released a congressionally mandated report on the costs and benefits of the Clean Air Act Amendments of 1990. Its central estimate was that the costs of the amendments were $53 billion in 2010. However, the benefits in that same year were $1.3 trillion, or 25 times the costs. This is not surprising given the significant number of people who are sickened by airborne pollution and the costs imposed on our economy in the form of increased use of our health care system and lost work days. In 2010, an estimated 160,000 lives were saved by the Amendments.

Food Safety.

In 2010 Congress passed the FDA Food Safety Modernization Act in response to high-profile episodes of tainted spinach, peanut butter, and eggs. In 2010 the Centers for Disease Control estimated that 48 million Americans suffer from foodborne illnesses each year, which result in 128,000 hospitalizations and three thousand deaths. Far from being an unwelcome burden on industry, the food industry supported this legislation. On the day this legislation passed the Chairman of the Grocery Manufacturers Association said,

"I am proud of the food industry for its support of landmark food safety legislation and our efforts to protect consumers and provide them a safe food supply. This legislation will strengthen the safety of our nation's food supply, give FDA much needed resources to effectively monitor and regulate it, and increase consumer confidence in the food they eat."

Studies find environmental regulations increase total jobs somewhat.

Most studies of economy-wide impacts of environmental regulations actually find a net increase in jobs due to regulations. A review of the literature in 1994 by the Economic Policy Institute concluded that ". . .a majority of the available studies indicate that environmental spending has actually boosted aggregate employment

somewhat." A 2008 study by Bezdek et al in the Journal of Environmental Management finds that "Investments in EP [environmental protection], economic growth, and jobs creation are complementary and compatible. Investments in EP create jobs and displace jobs, but the net effect on employment is positive. The employment in environmental protection industries in the United States has increased from 700,000 jobs in 1970 to 5 million in 2003."

Extended mass layoffs are not related to regulation.
Since 2007 the U.S. Department of Labor has tracked the number of times that mass layoffs (layoffs of 50 or more employees) are due to "government regulations/intervention." The department reports that just 0.3 percent of all workers laid off between 2007 and 2009 were laid off because of government regulation. And this data is based on companies self-reporting the cause of layoffs. Indeed, weather events were a far larger cause of layoffs than regulations.

Flaws in Crain and Crain study.
One of the most often cited studies by the opponents of regulation was conducted by Crain and Crain for the Small Business Administration's Office of Advocacy. They find that the cost of regulations was $1.75 trillion in 2008 or $8,086 per worker. In April of this year, the Congressional Research Service published a lengthy critique of Crain and Crain's study entitled, "Analysis of an Estimate of the Total Costs of Federal Regulations." CRS noted the following flaws:

- **Crain and Crain fail to account for the benefits of regulations**. By only considering the costs of regulation Crain and Crain's analysis is one-sided.

- **Crain and Crain assume that "higher quality" regulations are necessarily less stringent**. Crain and Crain attempt to use a cross country comparison of regulatory quality to infer the impact of regulations on economic activity. This comparison forms the basis of 70 percent ($1.2 trillion) of their figure for the annual cost of regulation under their model. However, the authors of the study Crain and Crain cite do not assume, as Crain and Crain do, that a less stringent regulatory environment is by definition of "higher quality." This is a fundamental methodological flaw that calls into question, Crain and Crain's findings.

Sincerely,

The Coalition for Sensible Safeguards

Response to Post-Hearing Questions from John D. Graham, Ph.D.,
Dean of the School of Public and Environmental Affairs, Indiana University

Questions for the Record
Rep. Howard Coble
Chairman
Subcommittee on Courts, Commercial and Administrative Law
For the Hearing on "Cost-Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"
May 4, 2011

For John D. Graham:

From Mr. Coble

1. At this Subcommittee's hearing on March 29, 2011, we heard from Professor Robert Glicksman that cost-benefit analysis is unreliable because it over-values costs and under-values benefits of regulations. Is this true?

   I addressed the concerns raised by Professor Robert Glicksman in both my written testimony and in my 2008 article ("Saving Lives through Administrative Law and Economics") in the University of Pennsylvania Law Review. In short, while both benefit and cost estimates are imprecise, there is no evidentiary basis for the conclusion that the analytic tool systematically overstates costs and understates benefits.

From Mr. Cohen

2. Do you agree with Ms. Katzen that, whatever the value of applying cost-benefit analysis to proposed regulations, such analysis should not be dispositive of whether the regulation should go into effect?

   Regulators should be required to consider the findings of cost-benefit analyses, and explain how the benefits of the regulation justify the costs. Regulators should be permitted to proceed with a regulation, even though benefits do not justify costs, if a compelling justification -- supported by substantial evidence -- is provided.

3. Please clarify exactly how certain intangible benefits like "dignity" can be quantified and monetized.

   By definition, an "intangible" benefit or cost cannot be fully quantified and monetized. My initial reaction is the a regulation that protects human

dignity may have some quantifiable benefits (e.g., citizens are certainly willing to pay money to protect the dignity of their family and loved ones) but some aspects of dignity protection may not be fully quantifiable.

4. What is your response to the concerns that courts may not be well-suited to second-guessing agencies' use of cost-benefit analysis given the numerous judgment calls that cost-benefit analysis requires and that allowing judicial review of agencies' use of cost-benefit analysis will simply lead to abusive litigation by those who are unhappy with the substance of a given rule?

   The federal courts are already making extensive use of cost-benefit information in their review of federal regulations under the "arbitrary and capricious" test. It would certainly be ill-advised for federal judges to replace the agency's analysis with their own but the courts are in a good position to judge whether a cost-benefit analysis has been conducted by the agency, whether the analysis has any egregious flaws, and whether the agency has explained clearly how the findings of the analysis were used to inform the agency's decision.

5. While it may be too much to ask that all risk in life be eliminated, should government not strive to reduce as much risk as possible?

   Reducing risk to life "as much as possible" may sound like a good idea but, in reality, there are many feasible reductions in risk that are not a good idea. For example, it is possible to set the speed limit on Interstate Highways at 35 MPH (thereby reducing the severity of highway crashes) but the cost of additional travel time would be far too great.

6. What is your view of extending cost-benefit analysis requirements embodied in Executive Orders 12866 and 13563 to independent regulatory commissions?

   In general, I support extending cost-benefit requirements to independent regulatory commissions as well as to Cabinet agencies.

7. Do you agree that, whatever the feasibility of quantifying benefits, it is difficult to do so with precision, such that cost-benefit analysis may seem misleadingly precise?

In many cases, neither the costs nor the benefits of major federal regulations can be quantified with a high degree of precision. However, there are standard tools such as sensitivity analysis that can be used to inform regulators of the imprecision, and avoid the evils of misleading precision.

8. You recommend that Congress require OMB to issue guidance on the proper conduct of cost-benefit analysis and cite OMB Circular A-4 as a positive example of such guidance. Given that Circular A-4 remains in effect, why do you believe Congress should become involved? Why should Congress require what has already been done?

   OMB Circular A-4 is a guidance document issued by OMB for use by agencies. Currently, there is no enforceable, legal requirement that agencies follow the analytic guidance in A-4. Congress should offer legal relief to stakeholders who are harmed because an agency has failed to follow the guidance in A-4.

9. In your testimony, you said that it is well accepted in the field of cost-benefit analysis that "some valid considerations are essentially intangible," such as "airness" when considering a rule that would reduce the rate of lead poisoning among poor children. However, President Obama has recently been criticized by some for mentioning "fairness" and "equity" as values that should be taken into consideration when agencies do such analyses. Do you think those criticisms of President Obama on this issue are "fair?"

   I am not aware of the criticisms of President Obama that you are referring to. If you provide the precise context for the criticisms, I would be happy to indicate whether I agree or disagree with the criticisms. In general, I do believe that regulators should be permitted to consider values such as fairness and equity, as well as economy efficiency, when making a regulatory decision.

10. You mentioned that you do not believe that agencies' estimates of benefits and costs are pretty good, and that there is no evidence of "systematic bias" in those estimates. In a much-touted study issued by the Small Business Administration that concluded that regulations cost $1.75 trillion, however, the authors used only the highest possible agency estimates of regulatory costs because they believed that agencies systematically underestimated

costs. What do you think of that approach and the authors' overall conclusion?

I have no comment on the SBA study because I have not had an opportunity to study it.

11. In her testimony, Ms. Katzen expressed some concerns about codifying the requirement for cost-benefit analysis, noting that it could be interpreted as a "supermandate" that would trump previous statutes like the Clean Air Act and the Occupational Safety and Health Act. Do you share those concerns? Wouldn't any statutory requirement have to have the same caveat that is in the executive orders – i.e., "to the extent permitted by law?"

If a "benefits justify costs" test is properly crafted, I would have no objection to trumping all of the existing decision criteria in previous statutes. However, I am aware of only a few cases where a statute appears to explicitly prohibit cost-benefit considerations (e.g., the setting of primary ambient air quality standards under the Clean Air Act) and I can understand why Congress might be more reluctant to overturn such statutes with a "supermandate." Thus, I could support a more limited cost-benefit mandate that would apply only "to the extent permitted by law."

Response to Post-Hearing Questions from Jeffrey Holmstead, Partner, Bracewell & Giuliani, LLP

Questions for the Record
Rep. Howard Coble
Chairman
Subcommittee on Courts, Commercial and Administrative Law
For the Hearing on "Cost-Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"
May 4, 2011

For Jeffrey Holmstead:

(From the Majority)

1. **Based on your own personal experience serving in the executive branch, you suggest that agencies often use cost-benefit analysis to justify decisions that already have been made. Can agencies really twist the facts to fit the rule, instead of making a rule to fit the facts? What are some ways by which Congress can prevent this?**

Unfortunately, in some cases it is possible to "twist the facts to fit the rule." In my view, this has become a serious issue when it comes to air pollution regulations. Over the last 15 years, a significant amount of research has suggested that there are serious health risks associated with elevated levels of fine particles in the air. In the regulatory world, this type of air pollution is called PM2.5, which is shorthand for "particulate matter with a diameter of 2.5 micrometers or less." According to a number of studies, the vast majority of the benefits that EPA has ever achieved under all the federal environmental statutes come from reducing ambient levels of PM2.5.

PM2.5 is actually a very complicated mix of many different components, including black carbon, organic carbon, sulfates, nitrates, and soil particles. Most of these fine particles are so-called "secondary particles" that are formed through photochemical reactions in the ambient air. Any type of fuel combustion results in emissions that, to some extent, contribute to the formation of PM2.5. In fact, virtually every type of manufacturing or industrial activity contributes in some way to ambient levels of PM2.5. As a result, virtually any regulation that controls any type of emission does something to reduce concentrations of PM2.5.

Rather than using cost-benefit analysis to develop the most effective way to regulate PM2.5, some EPA officials have come to view cost-benefit analysis (CBA) – and the benefits of reducing PM2.5 – as a way to justify virtually anything that they may want to do. All too often in recent years, EPA has argued that any regulation is justified as long as its assumed benefits exceed its projected costs. Proper CBA should identify the most cost-effective way to regulate – and not be used simply to justify any regulation that can be claimed to provide benefits that exceed costs.

Moreover, Congress specifically designed certain CAA programs to deal with ambient levels of PM2.5 – programs that provide much more flexibility than the regulatory approaches that EPA has chosen to use in recent years. EPA should be required to address PM2.5 under the statutory framework that Congress created for this purpose, rather than using other, more prescriptive regulatory programs (such as "maximum achievable control technology" mandates) that Congress enacted to address other issues such as air toxics.

Moreover, there is considerable uncertainty as to whether all the different constituents in PM2.5 pose a risk to public health. Recent studies have suggested, for example, that regulators should focus on reducing black carbon rather than treating all the different constituents alike for purposes of regulation. Yet EPA has paid little attention to research that might find a more effective way to deal with the health risks that are now attributed to PM2.5. It has been suggested that it would not be in EPA's institutional interest to limit its focus on certain components, since the use of PM2.5 gives the Agency a justification for regulating virtually any type of industrial activity.

Congress could address these concerns by (1) requiring CBA to be used properly to identify the most cost-effective way to achieve an environmental objective; (2) requiring agencies to use the programs that Congress has created to address specific objectives; (3) requiring further research regarding the most effective ways to deal with the risks that are now attributed broadly PM2.5

2. **As I read your testimony, it seems like there are lots of ways for agencies to violate the spirit of cost-benefit analysis requirements while perhaps still following the letter of the requirements. What are some key elements Congress should include in a statute to prevent agencies from gaming the system?**

The most important element would be a statutory requirement (including a meaningful enforcement mechanism) that requires agencies to follow broadly accepted principles of cost-benefit analysis when developing regulations. As noted above, this should include a requirement that agencies identify the most cost-effective way of achieving the benefits that a regulation is supposed to achieve. It would also be helpful for Congress to establish an independent regulatory watchdog to review the costs and benefits of new federal regulations and also to recommend changes to existing regulations.

3. **Proponents of regulation often complain about the burden that a cost-benefit analysis requirement would place on agencies. Bnt what abont the burden that harmful and ill-considered regulations places on employers? Which should we be more concerned about, especially in an ailing economy?**

The cost of conducting even a comprehensive cost-benefit analysis is trivial compared to the cost imposed by a major rule. If a federal agency is given the power to develop regulatory requirements that may impose billions of dollars in costs on businesses and consumers, it should be required to conduct the type of analysis that will ensure that those requirements are justified.

(From the Minority)

1. **As a former Assistant Administrator of the United States Environmental Protection Agency for Air and Radiation and as an air-quality lawyer, do you agree with Dr. Graham's assessment of the role EPA's air pollution regulations have played in reducing mortality rates resulting from chronic diseases?**

Yes. Regulations issued under the Clean Air Act (CAA) have clearly provided very substantial public health benefits – far greater than the regulations issued under any other environmental law. I can also say with great certainty, however, that some air pollution regulations impose very large costs but provide very little in the way of benefits. Other CAA regulations result in benefits that exceed costs, but are still not cost effective because there are other less expensive ways of achieving the same results. There is no doubt that we could achieve the air quality benefits that we enjoy today at a much lower cost to U.S. consumers, businesses and ratepayers. Throughout my career in government and the private sector, I have worked to ensure that our country's environmental objectives are achieved in the most effective and efficient way possible, but I have not always been successful.

Do you think even stronger anti-pollution regulations would result in fewer deaths?

Depending on how they are designed and implemented, some stronger anti-pollution regulations would result in fewer deaths, but other stronger anti-pollution regulations could result in more deaths. In my view, it is a shame that some people automatically support any regulation as long as it is "stronger" or "more stringent" while other people automatically oppose all such regulations. American consumers, ratepayers, and businesses would be much better served if policymakers would engage in more thoughtful discussions about the true costs and benefits of environmental regulations and how we can achieve our environmental objectives in the most cost-effective way possible.

2. **You mentioned in your testimony that, based on data provided by Susan Dudley, the Obama Administration issued 132 "economically significant" rules in its first two years in office, which you said was much more than during the George W. Bush Administration. The official data provided by the Government Accountability Office, however, indicates that during the last full year of the Bush Administration, agencies issued 102 major rules, while during the first year of the Obama Administration, agencies issued only 79 major rules. During the last two years of the Bush Administration, there were 168 major rules, compared to 175 during the first two years of the Obama Administration -- about the same. Do these real**

numbers support the theory that there has been an "explosion" of rules issued during the Obama Administration, as some have claimed?

It is silly to judge any Administration's regulatory record simply by the number of "major rules" (or even total rules) that it has issued. In some cases, a single "major rule" can impose a much greater burden than 20 other major rules. On the other hand, even a very costly rule may be justified if (1) its benefits outweigh its costs and (2) the rule is designed to achieve those benefits in the most cost-effective way possible.

I am not qualified to evaluate all the rules and regulations that have been issued under the Obama Administration, but I can say with great certainty that EPA, under the first 2+ years of the Obama Administration, has imposed a much greater burden on the U.S. economy than the Agency had ever imposed in any other equivalent period in history. I believe that any independent analysis would show that the cost of the EPA rules that have been proposed or finalized thus far by the Obama Administration is substantially higher than the cost of the EPA rules issued under any other Administration, including the 8 years of the Clinton Administration, the 8 years of the George W. Bush Administration, and the 8 years of the Reagan Administration.

3. **You mentioned in your testimony that Congress should require significant guidance documents to be reviewed by OIRA. Pursuant to a March 2009 OMB memorandum, however, agencies are already required to send those guidance documents to OIRA for review. Why should Congress require what is already being done?**

The fact that something is required by an OMB memorandum does not mean that it is "already being done." As Dr. Graham pointed out in his original testimony, the "requirements" imposed by Executive Orders and OMB guidance documents are sometimes ignored for political or other reasons. If Congress were to impose the same requirements by statute, with a meaningful enforcement mechanism, then federal departments and agencies would be forced to take them much more seriously.

4. **What is the cost-benefit analysis of keeping a coal-powered utility operational when there are other sources of electric power that cause less pollution?**

There are clearly very substantial benefits to having a reliable and affordable source of electricity. Even with historically low natural gas prices -- and subsidies (as well as mandates) for wind, solar, and other politically favored but more expensive sources of electricity – coal-fired power plants still provide almost half of the electricity consumed in U.S. every year. I am not aware of any credible analysis that suggests it would be cost-beneficial to shut down existing coal-fired generation over the short or medium term.

5. According to the Polluter Watch website, you, during your time with the EPA, "worked internally to undermine the Clean Air Act" and "to weaken the new source review program, which ensures modified or upgraded power plants don't increase pollution after they are retrofitted." It also alleges that you "oversaw the development of the Bush Administration's Clear Skies Legislation, which would have allowed for increased utility pollution." What is your response to this description of your work?

I do not know of any serious policy analyst who considers the "Polluter Watch website" to be a credible source of information. Any legitimate analysis would show (quite clearly, I believe) that we would have significantly lower levels of pollution from power plants than we have today if Congress had adopted the Clear Skies Legislation that I helped to develop, with the strong support of EPA career staff, when I was at EPA. In addition, U.S. businesses and consumers would have lower power bills and much greater certainty about their future electricity costs and the reliability of their power supply. My views on the "new source review" (NSR) program are well known and supported by many economists and other policy analysts: Although well intentioned, it has been implemented in a way that has hindered investment in new power plants and industrial facilities and created a strong incentive for companies to extend the life of their existing plants beyond what would be economically or environmentally desirable. It is a shame that NSR has become such a political lightning rod. There are clearly much more effective and less costly ways to reduce air pollution, as the National Academy of Sciences concluded when, in response to a congressional request, it conducted a review of the NSR reforms adopted during my tenure at EPA.

6. Were you formally counsel for the Chemical Manufacturers Association?

Yes. When I joined Latham & Watkins in 1993, several partners in that firm were representing the Chemical Manufacturers Association (CMA) and were gracious enough to involve me in their work on behalf of CMA. The senior Latham lawyers representing CMA were Robert Sussman (who is now serving as the Senior Policy Counsel to EPA Administrator Lisa Jackson), and David Hayes (who is now serving as Deputy Secretary of the Interior).

7. Were you an adjunct scholar of the misnamed "Citizens for the Environment," an entity funded in part by the Koch family?

Yes. I am proud to have been an Adjunct Scholar for Citizens for the Environment, which was a non-profit group that worked to promote market-based solutions for environmental problems. I do not know whether CFE received any funding from the Koch family. Over the years, I have been associated with a number of non-profit groups and have never asked about the source of their funding. I believe that the best way to evaluate any such group is by the quality of its work.

8. As stated in a piece by Molly Ivins published in the Sarasota Herald-Tribune in 2002, did you represent agribusiness in a suit challenging a law requiring

assessment of the health effects of pesticide exposure on children? Was that law an example of a "burdensome" regulation?

I am not familiar with the 2002 piece referenced above, but I did have the opportunity to represent several companies and a trade association in challenging certain EPA rules related to the evaluation of pesticides. I assume that the law referenced above is the Food Quality Protection Act (FQPA) of 1996. This law is not an example of burdensome regulation. In the late 1990s, however, EPA attempted to use the FQPA to justify certain very burdensome regulations that were inconsistent with the law and would have imposed substantial and unnecessary costs on farmers and consumers, as well as companies that produce agricultural chemicals.

Response to Post-Hearing Questions from Sally Katzen, Senior Advisor, Podesta Group, Visiting Professor, New York University School of Law

Sally Katzen

1. **Q: What is your view of the suggestion that significant guidance documents be subjected to cost-benefit analyses and interagency review?**

   A: I am in favor of treating significance guidance documents like significant regulatory actions.

2. **Q: What is your view of Mr. Graham's suggestion that a "distributional arm of the 'benefits-justify-costs' test" should be added to cost-benefit analysis to ensure "that the welfare of low-income Americans is considered before a significant rule is adopted?"**

   A: I believe "a distributional arm" is already included in the formulation set forth in E.O. 12866 and E.O. 15363.

3. **Q: What is your response to Mr. Holmstead's contention that agencies often misuse cost-benefit analysis to justify regulations where benefits outweigh costs, rather than assessing whether regulations most effectively maximize benefits and minimize costs?**

   A: I disagree with such a generalization. It is possible that there are such occurrences, but I am not familiar with any from my tenure as Administrator of OIRA

4. **Q: What is your response to Mr. Holmstead's contention that the EPA enters into consent decrees with environmental groups as a way to cut off meaningful regulatory review by speeding up the time-frame within which a rule must be issued?**

   A. I cannot speak to EPA's motivation for entering into consent decrees, which is a common feature of litigation, with either environmental groups or regulated entities. Entering into such decrees does not necessarily limit regulatory review.

5. **Q: What is your response to the contention that executive orders are not sufficient to ensure proper cost-benefit analysis because they are not laws or rules under which interested parties can seek compliance or enforcement of cost-benefit analysis requirements?**

   A: On the whole, Executive Orders have far greater authority (and effectiveness) within the Executive Branch than the threat (or promise) of individuals' seeking compliance or enforcement by the judiciary. Even though there are occasional newsworthy stories of courts' remanding regulatory actions to the issuing agencies, for the most part courts defer to agency expertise so long as the basis for the decision is recorded and documented.

6. Q: In your view, would allowing for judicial review of cost-benefit analysis threaten to undermine the deference that the federal courts have generally displayed towards agency decisions concerning the substance of proposed rules?

A: The most adverse effect of affording judicial review of cost-benefit analyses that are required by an Executive Order but not by the authorizing statute, is that it would create a super-mandate by effectively amending a host (we do not now know how many or which ones) of previously enacted statutes, some dating back over half a century or more. We also do not know what the implications of creating these decisional criteria are for the regulated entities or the intended beneficiaries of the regulations. We do know, based on experience, that the number of petitions for review of regulations will increase, for there is little disincentive for those who are disappointed at the agency level to take the matter to court and this would provide yet another allegation in the complaint. Even with judicial deference to agency expertise, there will nonetheless be substantial time and money as well as extended uncertainty devoted to litigation – not the most productive use of our resources.

7. Q: What is your response to Mr. Furchtgott-Roth's claim that in the absence of judicial review, federal agencies and outside parties do not take the regulatory process seriously?

A: Mr. Furchtgott-Roth served at the Federal Communications Commission, an independent regulatory commission (IRC) that is not covered by the Executive Order and therefore not required to undertake economic analysis in its decision-making. In my written testimony (pp. 6-8), I urged that IRCs be covered by the Executive Order so that they will be required to engage in the rigorous economic analysis that has come to be expected for (and generally accomplished by) Executive Branch agencies. With respect to Executive Branch agencies, my experience is that, even without judicial review, federal agencies and outside parties take the economic analysis requirements very seriously.

8. Q: If the cost-benefit analysis requirements of E.O. 12866 and E.O. 13563 were extended to independent agencies, what entity would be the most appropriate one to review rules issued by such agencies while continuing to ensure that they remain independent?

A: I believe that OIRA is the entity most qualified to review rules issued by such agencies and could do so in a way that would not compromise the independence of the IRCs. In my written testimony, I provide a variation of the approach used by Congress to deal with the analogous issue of clearance of information collection requests by IRCs (p. 8).

9. **Q: Mr. Graham asserts that "regulators should protect citizens from imposed risks to whatever extent the affected citizens would prefer, assuming those affected citizens were to experience both the benefits and costs of the regulation." Do you agree?**

   A: Regulatory agencies are not free agents and can only do that which Congress has authorized. Assuming that there is a broad delegation of authority, the agencies should prioritize risks based on sound science and accurate data. Beyond that, I am not sure what Dr. Graham is referring to or the context of his assertion.

10. **Are you concerned at all that the extension of cost-benefit analysis requirements to independent agencies may be used as a back-door way of undermining the implementation of major reform efforts like the Dodd-Frank Wall Street Reform Act and the establishment of the Consumer Financial Protection Bureau by opponents of such measurers?**

    A: No. I believe that the end result would be better coordinated and coherent regulatory actions, and ultimately better decision making in implementing the major reform efforts.

11. **Q: You state in your written testimony that you "strongly support" the concept of cost-benefit analysis. At this Subcommittee's hearing on March 29, 2011, we heard from Professor Robert Glicksman "that cost-benefit analysis is itself a fl nawed technique for distinguishing between useful and counterproductive regulations." Is Professor Glicksman correct that cost-benefit analysis is a futile pursuit?**

    A: Cost-benefit analysis is not perfect, but it the best analytical tool available for assessing the consequences of a proposed regulation. It is particularly useful when it is done early in the process of developing proposals (and alternatives to those proposals) rather than after the fact to justify whatever proposal is selected.

Response to Post-Hearing Questions from Harold Furchtgott-Roth, President, Furchtgott-Roth Economic Enterprises

Questions for the Record
Rep. Howard Coble
Chairman
Subcommittee on Courts, Commercial and Administrative Law
For the Hearing on "Cost-Justifying Regulations: Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits"
May 4, 2011

Harold Furchtgott-Roth:

From Mr. Cohen:

1. You suggest that judicial review of agency regulatory analyses is necessary for the regulatory system to function properly. How would you prevent outside parties that oppose regulation generally - and not simply those that raise objections to particular regulatory analyses - from exploiting judicial review as a way simply to stall rulemaking?

   Judicial review of potential violations of the Administrative Procedures Act has developed in a manner such that outside parties have a predictable estimate of how courts will consider the facts in a particular proceeding. Where agencies clearly violate the APA, outside parties go to court, and a proceeding may be delayed; where agencies comply with the APA, proceedings are rarely delayed as a result of APA complaints. I see no reason to expect that judicial review of agency analyses of the costs and benefits of regulation would have different outcomes.

2. If Congress or the President were to extend cost-benefit analysis requirements to independent agencies, how would you safeguard the continued independence of such agencies?

   I do not believe that the President can unilaterally impose regulatory requirements on independent agencies. Congress, by passing bills that become law can impose requirements on independent agencies. I see no direct relationship between the analysis of costs and benefits and the independence of independent agencies.

3. You mentioned that independent regulatory agencies like the FCC should be required to do cost-benefit analysis, and that one agency should be made responsible for ensuring that they are done in a uniform manner. Should independent regulatory agencies, which were established to be independent of the President, be required to submit their rules to OIRA for review? If not OIRA, what agency would you recommend and why?

   Independent agencies, such as the FCC, currently submit some aspects of their rules to OMB for review, such as the requirements of the Paperwork Reduction Act. I do not see such requirements as lessening the independence of independent agencies.

4. You mentioned in your testimony that federal agencies have "substantial legal and regulatory requirements" to document their considerations of costs and benefits, yet you argue that there should be a statutory requirement for agencies covered by EO12866 so that interested parties can seek "compliance and enforcement." Compliance and enforcement, however, are only needed if there is a problem with agencies carrying out their responsibilities. Assuming that is true (which itself is not clear), why should Congress enact a law to fix what is essentially an implementation problem? Isn't better oversight the solution to the problem you identify, rather than enacting another law?

   Enhanced Congressional oversight is one possible solution, but Congress has limited oversight resources. Moreover, in many areas of law, the courts—not Congress—are the only remedy for mistakes by federal agencies.

5. During your time as a senior fellow at the Hudson Institute, who funded your research? Were Charles and David Koch among those who funded the Hudson Institute?

   The Hudson Institute funded my research as senior fellow, and I do not know the many sources of funding for Hudson.

6. Please identify your firm's clients.

My clients have no interest in this hearing, and I have not discussed the hearing with them.

7. Does your firm receive any funding from sources other than its clients? If so, please identify those sources.

No.

8. Is it too much to ask of independent regulatory agencies like the FCC to perform cost-benefit analyses before they make decisions that will directly affect the employment and quality of life of millions of Americans?

No.

9. Why is it important that independent agencies' cost-benefit analyses be judicially reviewable? In your experience as an FCC commissioner, would the mere prospect of judicial review improve the quality of the FCC's cost-benefit analysis, thereby relieving courts from having to review many cost-benefit analyses?

I believe that the mere prospect of judicial review will compel agencies to comply with their responsibilities including the conduct of cost-benefit analyses. If an agency complies with its responsibilities, few complaints regarding its conduct will be brought to court, and even fewer will proceed very far.

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