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Panel I: A Fresh Look at Federal Regulatory Strategies

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Panel I:

**A FRESH LOOK AT FEDERAL
REGULATORY STRATEGIES**

Richard B. Smith
Moderator

Mr. Grenier: It gives me real pleasure to introduce the moderator of our first session, Richard B. Smith of the law firm of Davis, Polk & Wardwell in New York. Dick has served as vice-chairman of the Commission on Law and the Economy and played a very great role in putting this program together. He is a member of the Council of the Section on Corporation, Banking, and Business Law of the ABA. He is a former commissioner of the Securities and Exchange Commission and a former member of the Council of the Administrative Conference of the United States. Mr. Smith, I'll turn the program over to you.

Richard B. Smith: Thank you, Ed. The subject of our panel will be Chapters 3 and 4 of the Commission's report, which is among the material that has been given to you. Chapters 3 and 4 produce two recommendations which are reflected in the front of your book, and I hope that as we go through the panel you'll look at Recommendations 1 and 2.

Our panel's discussion, you will find, will also relate to Recommendation 4, dealing with regulatory analyses. That recommendation will also be discussed in this afternoon's program in conjunction with Recommendations 3 and 5. Those three recommendations grow out of Chapter 5, the subject of the program which Lloyd Cutler will moderate this afternoon. Let me introduce the panel quickly for you.

Steve Breyer, sitting to my right, was retained by the Commission as a consultant during its work, and his work really was a basis for

Chapters 3 and 4 of the Commission's report. Steve is a professor of law at Harvard and little did we know at the time we were working with him that he would occupy his present eminent position as Chief Counsel to the Senate Judiciary Committee.

Also on the program is Mike Baram, a lawyer in Boston. Mike did a very interesting paper for the Administrative Conference of the United States on cost-benefit analysis, a portion of which is included in the material that you have.

Paul MacAvoy, who is a member of the Commission and former member of the Council of Economic Advisers in President Ford's administration, is with us too. He is a professor at the School of Organization and Management at Yale.

With us also is Roberta Karmel, a Commissioner of the SEC and formerly a practicing lawyer in New York, who is exhibiting the kind of independence that practitioners before that agency admire.

Randy Thrower, who is a member of the Commission, former Commissioner of Internal Revenue, former chairman of the Tax Section of the ABA, and an attorney in Atlanta, is with us.

And Bill Kennedy, counsel for the General Electric Company and a former member of the Council of the ABA Business Law Section, is with us.

And, unrecorded on your program but very much with us, is Peter Aranson, a professor at the University of Miami, who has contributed a major critique of the Commission's report.

Some members of the panel will have views quite different from that reflected in the Commission's report. Since those recommendations were adopted by the American Bar Association, they reflect the policy of the ABA. While you are hearing these discussions and considering the cases, I hope you will keep in mind that the 26 members of the Commission debated long and hard and through a number of meetings and years to reach the balanced judgment that they did, and which the report and the recommendations reflect.

I'm first going to ask Steve Breyer to articulate some of the thinking and analysis that went into the first two recommendations of the Commission, which are perhaps the most conceptual.

Stephen Breyer: In the next twelve minutes I am going to try to outline an approach to regulatory reform. Whose approach is it? It is certainly consistent broadly with the Commission's approach, but I don't want to take everything I say as being precisely what everyone on the Commission thinks.

It is certainly generally consistent with my own approach. It is certainly broadly consistent with the philosophy of Senator Kennedy, who is now the Chairman of the Judiciary Committee of which I am Chief Counsel.

I say that because I want you to see that this approach really began, I think, having some practical effect with airline deregulation. I worked on that for Senator Kennedy five years ago, 1974-75. And Paul MacAvoy was working for President Ford.

And I think that President Ford's work on that, Senator Kennedy's work on that at that time, and then President Carter's work on that have all revealed the same thing. If you want regulatory reform, you take one agency, you look at it in extreme, exhausting detail, and then you produce major change within that one agency.

That was the approach that we took in airlines and that is the approach which Senator Kennedy and the administration are now taking with trucks. Let's call that the step-by-step approach. First, you take one agency. Then you take the next agency. Then you take the agency after that.

Now if that's a step-by-step approach, what more is there to say? There is more to say because the risk in taking one agency at a time is that whoever does it would just say, "All right. Let's look at the agency. Now let's do the right thing."

But what is the right thing? At that point I think you may see some practical value in the type of framework that the Commission has tried to articulate. What we are trying to do is work out a loose general system that will be useful to those who are involved in step-by-step agency regulatory reform. The framework will suggest a point of view for Congress or the Administration or those within the agency who are interested in severe, serious, meaningful regulatory reform. It will also be broadly suggestive of the worst areas of excessive or inefficient regulation.

The bottom line, as you can see it in the recommendation, is to approach agency regulation with a broad, procompetitive point of view. That's one way of describing the recommendation. A second way would be an antitrust point of view; that is, look for the least restrictive alternative.

A third slogan would be, regulation as a last resort. Now contrast those slogans with those who believe in regulation or those who believe in total deregulation. All three are slogans, but I think the first that I mentioned, the procompetitive outlook, captures the essence of what is needed for meaningful reform.

Now let me go a step further into detail. How can we begin to sketch out what this procompetitive point of view is? How can we make it meaningful? Moving down a level of abstraction, what we have tried to do in the Commission's work is to provide a framework, a framework that is basically procompetitive. It will suggest where deregulation is appropriate; where it may be appropriate to have incentives such as taxes or marketable rights, bubbles, bargaining; where those incentive approaches are most likely to work and where one might have to continue with classical, regular command and control regulation.

Now you can read what that framework basically is, but I'll briefly describe the approach. First, let's step back and pretend that we are regulators or congressmen or people in the Administration who are not interested in politics but interested in doing what is right.

We'll start with that point of view, and we can add political considerations later. Now what type of framework might a person want? Well, let's first have a list—a list of the basic types of problems that arguably justify regulation—primarily an economic list.

Let's look at five or six basic types of economic justification for regulation. First, there is the classical justification that we must regulate because the firm, like the telephone company or the electric company, has monopoly power.

Second, there is a quite different justification which often gets confused with the first. That is the justification that the firms are earning windfall profits or monopoly rents. An example will demonstrate how this differs from the first justification.

Suppose you bought some coffee in 1973 and hid it under your bed. It would be stale, but suppose it was in vacuum tins. Now you go and sell it today. You will discover that you could, if it is still fresh, earn a huge profit on that coffee.

Why? Because the price of coffee has gone way up. Does that mean you are a monopolist? It doesn't mean that at all. You are simply a person who bought coffee and put it under his bed. Although I am using an example to capture your attention, that may be essentially the problem of oil regulation or natural gas regulation; there are huge rents that have been earned and some people feel the owners are no more deserving of \$150 billion rent than you are because you kept coffee under your bed. Some people say, "Why should the producers have that? Let us transfer that to the consumers or the taxpayer."

Now one can argue whether that is good or bad but it is important to note that it is quite a different problem than the problem of monopoly power.

Three, there are justifications for regulations in what economists often refer to as externalities or spillovers, and we see that justification in environmental regulation and sometimes in safety regulation.

Four, there are justifications for regulation where there are informational defects. SEC regulation is a good example of what has been called forth to cure possible informational defects in the market.

Five, we are seeing more and more justification for what is called the moral hazard problem. That is Kenneth Arrow's reference to "I buy it. He pays for it. If I buy it and he pays for it, that's great. I have no reason not to buy as much as I want." That is called moral hazard and we see that occurring frequently in the health area.

And, finally, there is the great rationale from the 1930s called excessive competition. That was the rationale that was used for airlines, used for trucks, possibly used for ocean shipping.

Now I call that rationale the empty box, because it isn't at all clear that it is still meaningful today, but it is used.

That is List I. It contains the basic problems and into that set of boxes I think you can put most justifications for the regulatory programs in existence today. Now let's get a second list called opening up the black box which has the label "regulation."

People say "regulation" as if it were one thing, or alternatively they talk of it as if it were a million things. But it is partly our job to say, "It is neither one thing nor is it a million things." Can we get a few boxes into which we can put most regulatory programs in order to describe them and in order to describe the major problems with them?

We have tried to come up with some boxes. Cost of service rate-making is a classical box, and it is a classical system. What else? Historically based price setting.

Now what is the value of having two boxes, one called "cost of service ratemaking," another called "historically based price setting"? The value, I think, is if people recognize when they want to set prices in a new program, that whether they like it or not, given history, given the problems of bureaucracy, given the problems of the world, they are going to find that they are in either Box A or Box B.

And if they are in Box A, they will have to face certain discrete problems. And if they are in Box B, they will have to face other discrete problems. And I will tell them in advance, those who want to set hospital prices or any other kind of price, that they will have to face either the one or the other and they are going to have to solve them.

That doesn't mean you shouldn't do it, but it does mean you should be aware that you are not going to create a totally new system out of

whole cloth, and you should be prepared to meet the resulting problems. That is the virtue of the box. There are still other boxes.

Those who want to allocate goods—such as allocating routes in the CAB, allocating trucking routes, allocating television licenses—also better be aware that they will probably fall within Box C or Box D. That is the system which we have called “public interest allocation.”

That is what the FCC uses to hand out television licenses and it is very similar to what the CAB used to hand out airline rates or what the ICC uses to hand out trucking rates. The alternative to public interest allocation is D, “historically based allocation.”

That is rather like historical price allocation and it is what, in fact, is used to allocate oil. And if we are in a shortage again and we go to an allocation scheme, it, or some variation, will be used, and people will face the problems that are described within that category.

There are a couple of other major regulatory activities, one of which we have called “standard setting.” That is vast and huge, but there still are certain typical problems that are faced whenever people use it.

And, finally, there is “individualized screening which is what the drug agency does when it screens drugs or when you try to screen food additives or when the ABA tries to screen lawyers. Weed out the bad ones, it is called, and it is quite different from public interest allocation.

Public interest allocation is you're all in this room and we try to choose the best. The main problem is that everyone thinks he is the best. So you hire lawyers to make arguments as to who really is the best and it goes on for a very long time.

The other system is quite different. The other system is called “screen out the worst.” That is different. There are still lawyers. There are still long hearings, but the problems are different. It is a little bit easier, in fact, if you are prepared to have rather loose standards for what is the worst.

I am trying to give you a rough flavor of the system. We have lists of problems. We now open up the box a little bit about what classical regulation is and it says at least six things, not one. Now let's list some alternatives on our third list to classical regulation.

What kind of alternatives? Less restrictive alternatives for the most part, such as antitrust. A second alternative is disclosure. The SEC uses that frequently. Third, taxes may be used directly for regulatory purposes in order to provide certain incentives or disincentives.

Fourth, there is the cousin of the tax, cold marketable rights, which EPA is now introducing in realistic form under the name of the bubble. Five, we can use liability rules. Six, systems of bargaining,

either as supplements to or substitutes for certain classical regulation in certain areas, can be adapted.

And, finally, there is the nationalization system which isn't used much here, but is used in Europe. Now what we have are three lists and the trick is to match them up; given the problems with regulation on the second list and given our objectives from the third list, what type of alternative—classical regulations or one from the third list—should be used?

Now that sounds complicated in ten minutes, but, in fact, airline regulation took five years. And so it is worth spending time on the intellectual framework and going into it in detail if we are going to target the right agencies, have a framework—a procompetitive framework—for going after them, and then bringing that into play.

You see the basic idea of the system. It generates a few results. It generates a few possible examples of worst cases. That is, if you really see room for a major change, it immediately would pick out, and did pick out, airlines as a place to go after regulation because one can make a major improvement through deregulation.

It has picked out trucking and Senator Kennedy and the Administration are indeed pursuing trucking reform. It picks out others. For example, it suggests the use of taxes instead of classical regulation in some instances, such as windfall profits, possibly oil, possibly natural gas.

And we do see legislative proposals embodying that idea. In other words, there are at least some practical results you can get from it. What I am suggesting is that this framework helps to provide a beginning point for a reasonably sophisticated analysis that will identify a program as a major candidate for reform.

It at least gives you a place to begin. Now once you have begun, you had better get involved in the five years of work and that really means looking at it in serious detail. Now let me conclude by putting a problem to you and I'll suggest the answer that you will have followed.

Suppose you believe in step-by-step reform. Suppose that is your basic premise, that it is the way to get meaningful reform. Suppose, second, you start with a procompetitive point of view which can be fleshed out through this analysis.

Then the problem is to sit down and draft a statute, a generic statute, a statute that deals with regulation in general and that will further the step-by-step process with the precompetitive point of view.

Can you draft such a statute? Why is it difficult? Because, you see, the very notion of step-by-step says generic really won't work all that well. Can you do something to help? I'll tell you the answer we have

come up with so far, which is one of Senator Kennedy's parts of this legislation he has introduced, and maybe you can, in fact, help improve that.

What does it do? It says what you have to do is encourage people to take the step-by-step approach. Who do you want to encourage and how do you do it? You want to encourage the President of the United States and you want to encourage the people in Congress. They have the power to change the laws.

How? First, let's have a schedule of agencies that will be given a serious look. We can generate such a schedule. But how do you know those agencies will really get a serious look or is it going to be just a report on the shelf?

Second, let's have a trigger, and the trigger will force the problem to be taken seriously at a high level because people at high levels see that real action is going to take place. The trigger that we have put in the bill is not a Sunset trigger.

Sunset can be viewed as a trigger device. But the trigger we have put in the bill is not Sunset because we were afraid of the argument—it sounded like a good one—that once you Sunset an agency, a minority in Congress, through various procedural devices, will be able to prevent its resurrection.

So we did not choose that trigger. Rather, we chose a trigger which says, "The President must make a report to Congress. It must go to committee and within one year the committee's proposals or the President's proposals will be automatically discharged to the floor for a vote."

Now the prospect of a real vote on the floor is meaningful to those who work in Congress. Finally, how do you assure or how do you suggest or how do you encourage a procompetitive point of view? The way that we've done that is to suggest that the people who do the study and advise the President are people who will basically have a procompetitive outlook; for example, the Chairman of the Council of Economic Advisers, the Attorney General, the Chairman of the Federal Trade Commission, the Chairman of the Council on Wage and Price Stability, possibly someone from labor and other such representatives.

I am leaving you with the problem, not the solution. What I want you to see is (1) the step-by-step approach, (2) the effort to develop an intellectual framework that will help identify the worst candidates and achieve meaningful reform within agencies and through serious dealing with major agency programs, and then (3) to leave you with the problem of how you embody that type of approach in generic legislation.

Mr. Smith: Thank you, Steve. At the end, of course, Steve was describing S. 1291's provisions and the Sunset-High Noon alternatives, which, I am sure, will be a subject to be discussed on the next panel.

Let me turn back to the first two stages which represent the framework for analysis and the thought that (a) one should look to regulation as the last alternative and (b) if you do turn to any form of regulation, that it be the least restrictive alternative. The premise, of course, is that one can and should rely upon the market and market forces to the extent social policy objectives would permit. And I would like to turn now to Paul MacAvoy. Paul, what is this market? There is only a sense of what a market is and what a market can do, so is the market a better alternative?

Paul MacAvoy: Richard Smith's question is answerable in terms of another Mr. Smith, perhaps one of Dick's illustrious ancestors. The professor of moral philosophy in the late eighteenth century at the University of Glasgow, Adam Smith, in his long book—a book almost as long as the one that Stephen Breyer promises will divulge the real truth here—he told us that a market is essentially any kind of organizational device or institution by which individuals can exchange property.

Now that need not be a location where the five largest corporations in the country conspire on setting the price of salt or whatever. The varieties of markets are almost infinite. One could create a market—and I am almost disposed to do so—by which I sell a good part of my time for the next twelve minutes to Roberta. She has much more to say. She has a higher level of income, my being only a professor and she being a commissioner, and we could re-allocate the scarce time here on the basis of a little bit of money as a medium of exchange.

We won't do that. The institutions are not present. But the underlying thrust of this report that is the center of our attention today is a very insidious argument that, in effect, institutions can and should be developed to replicate market-like devices to a much greater extent in regulation than has occurred in the last twenty-five years.

The most insidious of the thrusts is towards more such marketlike devices in the area of regulation that has grown the most rapidly—and that is in health and safety regulation. Obviously the commissioners, and obviously our colleagues here today, would not spend this time arguing about the importance of the institution of deregulation in airlines; first, because the evidence is not all in; second, because it may have already occurred before the formal deregulation acts that

Steve had mentioned were passed; so that we should let that go until next year or the year after.

Attention should center on where ultimately, in the next five years, the thrust of this report will go. And I believe that the invocation of Adam Smith's words for more marketlike institutions goes to making fundamental changes in the way in which we regulate health, safety, and the quality of the environment. This is because the evidence did indicate that the present non-market systems that are operating in health and safety regulation are working very, very poorly. These are not market mechanisms in that there is no exchange device available by which all parties to the controversy can gain from a change in operations with respect to health or safety.

There is no means by which the Smithian maxim can really apply—the maxim that individuals engaged in economic activities, out of self-interest, can within a rule of law be brought to the point whereby they maximize the social and economic welfare of the community. There are no individual economic incentives—self-interest incentives—in the present health, safety, or environmental standards setting in regulations that do drive us towards the conclusions that are sought to be reached by the legislation that sets up this regulation.

We use almost entirely equipment and design standards in EPA, OSHA and NHTSA which are for the purpose of command and control. They are for the purpose of providing retribution against violation rather than for providing incentives to improve the quality of the environment.

As the research literature now widely indicates, these command and control procedures do not produce the benefits for which the regulations are designed. One need not have been in Los Angeles, as I was Sunday, to have heard the head of the air pollution control agency there decry the fact that we have superb design standards for automotive emissions which, when put into effect in actual driving conditions, have no perceptible effect on the quality of the environment in Los Angeles. A third of the cars are so far out of compliance with the engineering design for that piece of equipment that they produce by themselves as much pollution as was expected to have come from the entire population of automobiles. That is because there is no incentive for the owner of that piece of equipment to somehow or other internalize the social benefits and costs from his emissions.

And the design standard approach of NHTSA or of EPA does not provide mechanisms by which we get the operating results that are hoped to be achieved in the regulations. The accident rates in factories have not been in any way affected by the Occupational Safety and

Health Administration. Automotive equipment standards have not reduced accidents. They may have changed the incidence of the effects from accidents to better protect drivers and worse protect pedestrians. These conditions have been widely found in engineering, economic and political science research literature to be, in effect, an intellectual default of the design standard mechanisms that use command and control procedures.

All well and good! That is where we are now. We have had a decade of this kind of regulation and I believe that the thrust of the ABA Commission approach is because we are doing so poorly—only because we are doing so poorly with the approach we now have in place—the traditional command and control approach—we have no alternative but to go to market-like mechanisms because they can certainly do no worse and they may do better.

These mechanisms are fraught with great danger. The use of—as Stephen mentions first—a taxation device has been widely bandied about. We considered it very seriously. We propose it in a most timid fashion. These devices do produce Smithian market mechanisms.

By taxing a polluter, one provides costs against which he then has to operate to make profit. This will reduce the rate of his output. It will internalize the social cost in the way that raised prices and reduced quantities of those socially disadvantageous goods. The market mechanism works. There are terrible problems with this potential alternative regulatory device of taxing polluters or unhealthy perpetrators of one kind or other.

Randy Thrower will discuss these in detail, but for one that would be to put an additional, conflicting goal on the tax system which may make it administratively unmanageable. The use of damage claim systems in litigation whereby the collective individuals that are harmed by health and safety—poor health and safety conditions—can sue those that perpetrate the conditions to the point where their harms are compensated for is widely regarded as a market-like mechanism that could have possible gains in the efficiency of operation of our economy.

This is widely believed to be highly costly and to lead to an even greater explosion of litigious behavior, an explosion you may hardly recognize given that the sky is already afire with litigious behavior. And it may be that we are dulled to some of these cost elements and, indeed, this would be a very large step backward to open the courts to collective damage claims in ways that produce economic-like results.

So we are very concerned here. Deregulation is a marketlike proposal; that is, to roll back part of the health, safety, and environmental law that calls for all these goods that we are not receiving—simply

saying that the market can do no worse and we can save a good part of the cost that Mr. Neustadt mentioned that seems to be following from the administrative system in place—is sending us back into the world of Adam Smith in terms of not having any protective devices whatsoever. It is risky to be that naked in terms of a legal frame of reference. Indeed these marketlike devices all have terrible problems.

Their remaining virtue, however, is that the present system is working alarmingly poorly and that if you take our approach seriously, you must begin to say the unsayable which is that there may have to be a movement to another kind of device besides EPA, OSHA and NHTSA to achieve the goals that they need to achieve.

This is no argument about social benefits versus economic costs, about the value of a human life saved against unemployment created by an EPA rule. It is an argument that the goals that are being sought by the great three, by the triad of EPA, OSHA and NHTSA, are valid goals. Many of them cannot be measured in economic terms and none of them are being achieved and that we must go to market mechanisms in order to begin to have a substantial social effect. Adam Smith would be smiling at this point in my discussion so I think I'll quit.

Mr. Smith: Thank you. Paul MacAvoy has indicated that while he thought this was a step in the right direction, we ought to recognize before we travel down this road, which he thinks we should travel, that there are a number of problems with some of the alternative approaches. I would like to turn to Peter Aranson now to develop this theme, which I know is in his thinking. If this matching of goals and tools that Steve Breyer so eloquently described is such a good idea, and it is not that unobvious, then why hasn't it been done long before this? Peter?

Peter H. Aranson: I will resist the very obvious answer that Steve Breyer didn't look at it soon enough. Having done that, let me provide a very modest demurrer. As some people in the Commission know, I have taken exception to certain parts of the report. However, in terms of matching regulatory strategies to regulatory goals, I believe this document has moved us from about 1935 to 1965. And that is absolutely remarkable, especially considering the political realities within which the Commission is operating.

But what we have here is an interesting question and that is, here are several social problems, and here are some obviously superior ways to handle them. Why hasn't the Congress or the Administration or the

agencies themselves—or, for that matter, the electorate—risen up in arms and adopted these superior ways immediately? Why have we gone along as we have been for so long without these things being adopted? The importance of the answer to that question is that any proposal to solve certain problems of the present regulatory regime must face the cold light of political reality.

For example, why has the EPA used standards instead of some kind of a tax system, an effluent charge system? Why was its original legislation written as it was? Why is it that antitrust policy has evolved incoherently? The answers to these questions can be found in a burgeoning literature on the frontier between political science and economics, variously called public choice, law and economics, and property rights theory. This literature has not been brought together in one place at one time, and therefore many of its findings have been ignored. It has not been summarized and it leaves many questions unanswered but we have begun to get a grasp on the answer to the question, “Why haven’t we had a more sensible regulatory regime at an earlier date?”

The answer public choice offers to this question is that the present regime is about the way the members of Congress want it and their incentives dovetail very, very nicely with those of the members of regulatory agencies. Even when congressmen kick and scream, they are making points with the electorate. If they didn’t have the regulatory agencies to kick occasionally, they would have to find a less inviting target.

Now why do I say that? Much research has gone into the question of what happens in the Congress and the nature of the legislation it enacts. All of the problems that Steve Breyer has talked about involve in one interpretation or another the production of public goods. When you are suppressing a public bad, such as air pollution, you are producing a public good called clear air. When you are suppressing the public bad of monopoly power, you are producing the public good of more goods at a lower price for consumers generally. The same thing holds true, although with certain modifications, of the market for information. Information is very much like a public good. These are goods that are available to anybody once they are provided and if one more person consumes them, this in no way detracts from anybody else’s ability to consume them.

This is Basic Economics 101. The problem with such goods is to get them to be produced. The members of the economics profession for many years said, “Well, when you have public goods, you have market failure and, therefore, you need government.”

They never looked at government. But some hard, cold economic analysis has been brought to bear on the public sector and the result, we find, is that the members of Congress have absolutely no incentive to produce public goods and their legislation will reflect that.

For example, a congressman really cannot credibly claim to have reduced the cost of living by a tenth of one percent. But he can credibly claim to have brought a particular dam, post office, or a public works project into his constituency. That is a private good for that constituency vis-à-vis the entire nation.

This incentive to enact private interest legislation—private good legislation—pervades the entire legislative process and the regulatory agencies.

Agencies cartelize industries. They give private benefits to particular sectors and segments of the economy at the expense of everyone else. The question we must answer is in what way can we get around this process. In what way, if we can respond to Professor Breyer's question, can we write legislation that somehow brings about a good matching of strategies to goals?

I am not sure what the answer to that question is. I have severe doubts about giving Congress more control over that which they have already created. I have severe doubts about writing legislation that requires regulatory analyses, cost benefit studies, which is going to result in an expansion of the agencies themselves, because agency incentives dovetail with those of the Congress.

They want bigger budgets or to maintain their budgets. They want larger jurisdictions or to maintain their jurisdictions, and they want to maximize the probability of not making a detectable error as opposed to making undetectable errors. So you get over-regulation in safety and drugs and the result is that instead of killing drivers, we are now killing pedestrians. There is no net benefit in terms of lives saved, but there is a lot of equipment added to automobiles, which some argue has driven Chrysler to the brink of bankruptcy, and that has certain anticompetitive effects.

So in all of this I am not certain that we have arrived at the point yet where we are prepared to make a legislative leap. But there are two things that have not been considered that ought to be. One of them is a return to regulation by the common law rather than by agency. The efficiency of the common law is a newly discovered area in law and economics, and one that shows great promise. The second possibility that might be considered is regulatory decentralization. Most regulatory schemes now carried out at the federal level might be done more properly and adequately at the local level. There are several problems

with that. But if the people of Oregon, for example, want higher environmental standards than, say, the people of Alabama, they ought to be able to enact them and the people of Alabama ought not to be made to bear the social choice of the people of Oregon. While there may be errors made at the local level, the amount of damage done to those not in a particular jurisdiction might be minimized.

Mr. Smith: Thank you, Peter. As a resident of Manhattan, I'm not sure that I would like New Jersey alone to decide how much pollution over New Jersey is to float over Manhattan.

Mr. Aranson: Yes, but you can always move to Coral Gables.

Mr. Smith: All right. Let me now shift the focus a bit. We have exposed you to at least some of the conceptual framework for our approach to questions of governmental interventions in the economy, a structure of analysis for it.

Most of this is directed to analysis at the congressional level, the legislative level, where decisions are being made on whether or not to intervene in the economy and if the government is to intervene—because there is a compelling social objective that the majority of the Congress decides has to be served and is not being served by the market—then they have to select a form of intervention. Most of the congressional decisions about regulatory interventions have given to administrative agencies or executive departments a great deal of discretion couched in public interest or public convenience and necessity language.

In an attempt to bring this kind of analytic approach to decisions at the agency or department level within the usually broadly worded regulatory statute, a lot of thought and attention has been given to a device called regulatory analysis. It is a device to bring the sort of thinking we are talking about into a formal process. Now this overlaps a bit with our fourth recommendation, but an important element in regulatory analysis thinking is something called cost-benefit analysis.

Mike Baram has given a good deal of systematic thought to cost-benefit analysis as a technique, and I would like to turn to Mike now to discuss with us what is meant by cost-benefit analysis. Is it different from regulatory analysis? How real is regulatory analysis as a way of decision making?

Michael S. Baram: As Dick Smith has said, the use of cost-benefit analysis or variants called regulatory analysis is the one real regulatory reform that is underway now. My infatuation with this subject began a few years ago when I served on a National Academy of Science Committee on Radiation Standards.

The Academy had been asked to review the radiation standards established by the Nuclear Regulatory Commission and to offer guidance to EPA. We had assembled before us all the economic, technical, health, and environmental data on the effects of radiation on human beings and on the environment and we were now wondering how all this data could be put together in some sort of balancing analysis.

One of the stumbling blocks was that there were no numbers or dollar values to associate with human life or human health. Fortunately the people from the Nuclear Regulatory Commission were there. As we struggled with the issues of how to value life and other unqualifiables in a cost-benefit type of analysis, we asked them how they dealt with the value of human life in their radiation standard setting.

And after a slight pause, we were told that "the value of a human life is \$1,000 a man-rem." This seemed to satisfy the analysts and the discussion immediately proceeded onto another subject. As a non-expert, I was shocked. This led me to inquire of the EPA people in the Radiation Programs office whether they used a dollar value for human life when they did their cost-benefit analyses in setting their environmental radiation standards, also dealing with human exposure to radiation.

Only after my persistent questioning was it revealed that the EPA Program director had determined that a \$500,000 cutoff was the highest value for human life that would be used by EPA in developing its radiation standards. My infatuation with this subject and its cavalier treatment by the analysts continued, and I spoke to people in other agencies and found out that a variety of dollar values for human life were being used by different economists and analysts in each of these agencies.

The point I'm trying to make is that our reliance on an analytic tool, cost-benefit analysis, which is the most easily usable form of regulatory analysis, runs into some very severe methodological problems, and raises institutional, legal, and ethical issues.

The regulatory analysis that is now prescribed by Executive Order 12,044 to be conducted by the agencies is described as a more flexible tool than the simple kind of cost-benefit analysis that I have described as being conducted at the NRC and EPA. Presumably regulatory analyses that would not involve quantification of unquantifiable factors would be permissible.

However, in actual practice and despite some of the comments of previous speakers this morning, the most common type of regulatory analysis that is being done today in the Office of the President, in

COWPS, CEA, OMB, in the Regulatory Analysis Review Group, and in the agencies that are doing their own regulatory analyses, are quantified cost-benefit analyses. The analysts in the agencies and their consultants that I have discussed this practice with have cynically referred to this new development as the game of "pushing the numbers" to reach predetermined outcomes.

There are methodological problems in economic analysis, particularly in the simplistic cost-benefit analysis approach. These include not only the quantification of unquantifiable factors, but also the discount rate.

What discount rate to use, for example, when dealing with future costs and benefits which an agency is trying to translate into present day dollars. The OMB has issued a guidance calling for use of a 10 percent discount rate. Yet another office in the Office of the President, the Council on Wage and Price Stability, uses other discount rates at its own discretion.

For example, in evaluating the proposed regulations for access of the handicapped to transportation systems that had been issued by DOT, the Council on Wage and Price Stability in one single regulatory analysis used two different discount rates, one for translating future costs and another for translating future benefits, 3.8 percent for future costs and some much higher figure for future benefits.

I find all of this analytic discretion mind-boggling. If economic analysts and decision people don't have answers to these methodological problems in the simplest form of economic analysis, cost-benefit analysis, then how much reliance can we place on their more sophisticated models and assertions about market behavior?

In doing my study for the Administrative Conference on "Regulation of Health, Safety and Environment and the Use of Cost-Benefit Analysis," I also found that the cost-benefit approach of the Executive Order is being practiced in many agencies which do not have statutory authority to consider economic factors in their decision making or to use economic frameworks for decision making.

Certainly the Environmental Protection Agency, OSHA, the Consumer Product Safety Commission, the FDA and others in the cluster of health-safety-environment agencies do not clearly have such statutory authority, and there are therefore various constitutional issues pertaining to the separation of powers which the ABA report recognizes, when such agencies are urged to use cost-benefit under Executive Order.

I want to make just a few more comments. What can be done about

this situation? If we are committed to introducing greater consideration of economics in agency decision making, how can one foster this responsibly? Is cost-benefit or other variations the route to follow?

I think certainly we can all agree that we want cost effectiveness in agency decision making. We want each agency to make the most cost-effective choice in reaching an explicit statutory goal. However, when the statutory goal is left to agency determination, do we really want these goals defined by the agency on the basis of an economic cost-benefit analysis of the type I have described?

The recommendations in the Administrative Conference Report, which is outlined in your notebook,* deal with the three sources of this problem—first, Congress. Through its unclear statutory delegation of authority, it is handing over the very important trade-off or balancing function to the agencies. Therefore, the report contains recommendations calling for Congress to try to better clarify its intent on health, safety, and environmental quality in many cases, to review the nature of the authority that it has given the agencies, and agency practice which involves the use of cost-benefit analysis, and to offer better guidance on how the societal trade-offs should be made, if at all, in light of the limitation of analysis.

The second set of recommendations deal with the Office of the President, and attempt to prevent ex parte contacts which usually are designed to get the agency to “push the numbers” to better achieve anti-inflationary goals, a process which is obstructing efficacious regulation of health hazards and environmental problems.

The third set of recommendations deal with the agencies themselves, and primarily try to force the agencies to do two things—to structure their discretion for decision making when cost-benefit is involved, and to articulate how they intend to deal with the mushy, subjective aspects of their analysis, aspects for which there is no expertise, aspects such as valuation and discount rates. After structuring their discretion, the recommendations call for the agency to articulate it in generic rules which will properly inform everybody as to how they are indeed conducting their balancing analyses. This is intended to prevent ad hoc “numbers games.”

Mr. Smith: Thank you very much. Let me turn now to Randy Thrower and Roberta Karmel. We have talked about using alternatives to classic command and control regulation. Prominent alternatives are utilization of the tax system and utilization of disclosure.

*Table of Contents and excerpt reprinted in Appendix A, *infra* page 194.

Roberta's agency's main function, we hope, is disclosure. Randy formerly headed the administration of the tax system. Randy, let me ask you whether you see any conflict in seeking to have the tax system in one way or another advance a social policy goal as distinct from being an equitable way of raising funds for the federal government.

Randolph W. Thrower: At our breakfast this morning I found myself restating a position that early in my administration as Commissioner I had discussed at some length with Dan Monahan and the White House and with the tax policymakers in the Treasury Department, mainly to the effect that the tax system was not the proper structure through which to undertake to introduce broad, experimental, exploratory, social programs.

The principal function of the tax system, of course, is, in as painless a manner as possible, to extract funds now at a rate approaching \$400 million a year from the populace. And the mission of the IRS should not be diffused of its efforts diverted through social programs.

The ideal income tax system, of course, is one with a very broad base, with few exceptions, with simple laws and low rates. But that's a beautiful thought that has been respected more by exception than by observance and, in fact, has been abused in many instances.

Recognizedly there are occasions where the system offers perhaps the best alternative for certain social objectives or economic objectives that are clearly desirable. One advantage, particularly where the provision is for an incentive to desirable conduct, is that it preserves freedom of choice and of election.

It provides for a decision made within a business context. It generally is readily administerable because of the very large staff in place with the national office of the Internal Revenue Service and the very large field organization, now about 30,000 revenue agents, revenue officers, and tax auditors in the field.

It does have some clear disadvantages, I think, principally if overused. This does abuse and diffuse the objectives of the system. Where the provisions are made elective, of course, the extent of the coverage cannot be known in advance. It is dependent upon the value of the incentive to follow the course that is desired, but there may be other market and financial incentives that divert and interfere with that.

I have mentioned that the tax system is better suited as an incentive device than as a disincentive. For example, take the area of pollution—it is within the ordinary course for the Internal Revenue to confirm an investment in certain machinery designed to accomplish a certain purpose.

Once confirmed, that cost can be amortized over a five-year period and that is the particular incentive involved here—similar incentive for rehabilitation of low income housing. It would be an entirely different thing for the IRS to administer a disincentive in terms of a penalty upon the performance or operations of a company which is polluting.

Another disadvantage of this use of the tax system is that cost is frequently overlooked. Congress seems much more ready to accept the cost of a loss in revenue rather than the cost of a direct appropriation. Since incentives or disincentives are being more frequently used in the revenue system, I think it would be highly desirable to develop methodologies and techniques, which would in a sense have to be specialized, to measure the total values and disadvantages in the use of the tax system in particular instances. There is a record of experience in this respect. It could be utilized.

With respect to the reference that has been made to the windfall tax on oil profits, such a tax, a tax on unjust enrichment so to speak, is not without precedent. Such taxes are very complex. They become more arbitrary with the passage of time because factors other than those that are measured and seen and perceived when the tax is imposed arise in later years and make the situation complex. However, they have been used where other alternatives were not readily available and, of course, that is the great debate going on at the present time.

Mr. Smith: Thank you, Randy. Roberta, much is made in our report that disclosure is about the least restrictive alternative as a form of regulation. Do you agree with that?

Roberta Karmel: I agree with the conclusion in the report that disclosure is a less restrictive regulatory alternative when it is compared, for example, to standard setting or what standard setting in my area of the law sometimes is called, merit regulation.

Probably one of the reasons that the SEC has been able to maintain a generally good reputation over the years is that the agency has engaged in disclosure regulation as opposed to merit regulation. Nevertheless the report seems to assume that disclosure regulation and standard setting are always totally separate and distinct. I think the experience of the SEC would indicate that the difference between disclosure regulation and standard setting is not always that easy to determine and disclosure regulation itself can be or can operate as a form of standard setting.

Let me give you two examples. One example, which is presently controversial, is the Securities and Exchange Commission requirement that persons who are asking the shareholders of their company to elect them Directors must enumerate all of their affiliations, some of which may be conflict of interest type affiliations, with the corporation.

That may very well have an impact on the composition of corporate boards. This kind of disclosure regulation has sometimes been criticized as an effort to change standards of corporate conduct in a way that go beyond disclosure.

But then I would like to give you a much more basic example which goes to the heart of the SEC's disclosure regulations. If public corporations have to provide shareholders before they come to the market with three years of audited financial statements, a form of disclosure about their financial affairs, corporations which are unable to do so are unable to come to the market.

Sometimes disclosure also can have anticompetitive results. And to the extent that the thrust of much of current regulatory reform thinking is to try and inject more competitive forces into the marketplace, that also has to be considered in the context of utilizing disclosure as a regulatory tool.

Mr. Smith: I suppose the intersection of standard setting and disclosure doesn't mean that disclosure is not a distinctly different concept, and less restrictive. For instance, your example about the statutory requirement of three years of audited financials to come to the market—that seems to be a standard setting requirement designed to motivate people to provide disclosure.

The interest or need in coming to the market is such that an issuer puts itself in a position to provide that form of disclosure, but there is no question that it is standard setting. The important thing about disclosure is that it doesn't matter what the balance sheet says. You can show negative net worth or whatever the balance sheet shows, but you can go to market so long as you produce the balance sheet. That's a big difference from saying, "You can't go to the market unless you have a net worth of umpty-ump million dollars."

Ms. Karmel: I would agree. Yes, that is a big difference. It does not prevent a business entity from engaging in a form of business activity. It only requires disclosure of that activity. I think in terms of what the government is required to do in order to enforce the regulation, there is also a difference which is important, because it is rela-

tively easier to administer a disclosure statute than it is to administer a standard setting statute.

The enforcement problems are somewhat simpler and I think that a much smaller bureaucracy is generated by that type of a regulatory scheme. And I would say that part of the evil that the committee's report is addressed to and that we have been discussing here this morning is not simply government regulation but bureaucracy.

This effort to search for the least intrusive type of regulatory mechanism in controlling what the private sector does is so government and business will operate for the overall public good. It is important to do that with a minimum of bureaucracy at the government level.*

Mr. Smith: Thank you, Roberta. Peter Aranson, I guess, would say that bureaucracy is the whole question. Let me turn to Bill Kennedy. Bill, you've done some heavy thinking about regulatory analyses and have had some experience with them. Is this a device to contain the kind of analysis that we're talking about in Chapters 3 and 4?

William F. Kennedy: Let me open by endorsing very emphatically the observations made first by Dick Neustadt and reiterated by Stephen Breyer and by others that there is no one sovereign technique of regulatory reform. There is no simple remedy to be adopted, either by agencies or by the White House or in four line measures by the Congress, that will provide a solution for all our woes.

Next let me endorse the observations of Mike Baram that regulatory analyses have some obvious limits. I don't know how you go about quantifying the value of human life or shortened life expectancy or a cleaner or more beautiful environment. I do think you can quantify, perhaps in a modest way, some other issues, such as the cost of alternative methods of attaining those goals and that that is a useful discipline to go to.

Finally, let me, if I may, turn to the concept of regulatory analysis embodied in some of the pending bills and make some observations about those concepts, a little bit at variance, perhaps more than a little on one point, with the recommendations of the ABA Commission.

The current congressional agenda for "regulatory reform," as reflected in the pending bills, includes proposals for:

- regulatory analyses (economic impact statements),
- competitive impact statements,
- expedited procedures, principally in licensing cases,

*Paper prepared by Ms. Karmel is reprinted as Appendix B, *infra*, page 206.

- periodic agency review of rules,
- legislative sunset reviews, and
- legislative vetoes of agency rules.

The bills contain additional provisions on regulatory planning and regulatory agendas, on deadlines for agency action, on administrative law judges, subpoenas, *ex parte* communications, and separation of functions, on Government funding of intervenors, and on restructuring of the Administrative Conference (ACUS) and expansion of its monitoring role.¹

Whatever else one may say of this agenda, it cannot fairly be characterized as modest. Yet I would like to use my brief time this morning, to suggest additional items, two of them based on recommendations of the American Bar Association's Commission on Law and the Economy.²

ISSUES TO BE ADDRESSED IN REGULATORY ANALYSES

If we are to introduce some meaningful economic discipline into the regulatory process it seems to me desirable to define as sharply as possible the issues to be addressed in any required regulatory analysis (economic impact statement). This to my mind suggests that these analyses should address not only the questions of benefits, of costs in the narrow sense, and of alternatives. It would also be desirable to require that the analyses address (where relevant):

- effects on investment and productivity,
- effects on competition, and
- specifically, effects on the capacity of U.S. based industry to respond to import competition, and to meet foreign challenges in export markets.

¹Two bills S. 262 (Ribicoff) and S. 755 (Carter Administration) deal with all the foregoing issues except sunset reviews, legislative vetoes, competitive impact statements, and *ex parte* communications. S. 1291 (Kennedy) deals among other things with competitive impact statements, procedure for periodic (high noon) review of regulatory agencies, and *ex parte* communications. Legislative veto proposals are embodied in S. 104 and H.R. 1776. Sunset proposals of varying scope are found in S. 2, S. 445, and H.R. 2. Congressman Derrick's "sunrise" bill H.R. 65 provides that "it shall not be in order" for Congress to consider any bill involving budget or spending authority or "tax expenditures" unless the bill states "specific objectives and planned annual accomplishments" and requires annual reporting as to achievement.

²Federal Regulation: Roads to Reform, Report by Commission on Law and the Economy, American Bar Association, Exposure Draft, August 5, 1978.

Moreover, if the requirement for regulatory analyses is to be meaningful, it seems to me that there has to be some provision for judicial review of the adequacy of these analyses—judicial review not of the analysis at the time it is first issued, but of the analysis as a part of the record of final agency action.

MONITORING AND COORDINATION

The proposals for a broader monitoring role for ACUS seem to me sound if that role is focussed on legal/procedural questions, including "hybrid" rule-making procedure and expedited procedures in cases currently subject to trial-type requirements, on compliance with the Freedom of Information Act, the Advisory Committee Act, the Sunshine Act, and the Federal Reports Act, and on recruiting and evaluation of Administrative Law Judges.

However, there is also a need for monitoring on the economic policy side—monitoring which should be assigned to a different body. That body should play a role analogous to that of the Council on Environmental Quality with respect to:

- guidelines for preparation and review of regulatory analyses, and
- inter-agency coordination to promote balancing of conflicting agency objectives and policies.³

When the Carter Administration continued in modified form the Ford Administration requirement for inflation impact statements,⁴ it accompanied this action with the establishment of a Regulatory Analysis Review Group to perform functions along these lines. The ABA Commission in its recommendation 4 proposed a mechanism for inter-agency coordination and this recommendation was approved at the August session of the ABA House of Delegates. Most of us would not have much doubt as to the authority of the President under existing law, to establish such coordination among Executive Branch agencies. But it seems desirable to include in the coordinating process the work of the so-called independent agencies and to remove any legal questions about such inclusion by providing a clear statutory basis for the Regulatory Analysis Review Group.

³Environmental Quality Act of 1970, *as amended*, 42 U.S.C.A. § 4372; Executive Orders 11,514 and 11,991; Council on Environmental Quality, National Environmental Policy Act—Regulations, Implementation of Procedural Provisions, 40 C.F.R. 1500–1508; *Andrus v. Sierra Club*, 47 U.S.L.W. 4676 (June 11, 1979).

⁴Exec. Order No. 11,821 (Nov. 27, 1974, Ford); Exec. Order No. 12,044 (Mar. 24, 1978, Carter).

I should add a caution. The Supreme Court has held that the public interest standard employed so frequently in regulatory legislation should not be read to embrace every national objective or policy, but instead should be read in the light of the specific purposes of the particular regulatory scheme.⁵ The coordinating process should not become a basis for avoiding this limitation and expanding the powers of agencies like the Federal Trade Commission or the Securities and Exchange Commission.

POLITICAL ACCOUNTABILITY

One of the common themes—perhaps the principal theme—in the vast literature on regulatory reform is the need for better controls on delegated authority, for greater political accountability. The two competing proposals are:

- the legislative veto, which commands substantial congressional support and emphatic presidential opposition, and
- the ABA Commission proposal, just approved by the ABA House of Delegates, for greater presidential participation in significant rule-making, a proposal thus far received coolly in the Congress and not endorsed by the White House.

Yet the strong support for the legislative veto seems to me to mandate consideration of the alternate approach proposed by the ABA Commission. It is not necessary to come to definitive conclusions about the constitutionality of the veto but only to recognize that the questions are substantial⁶ and that the balance of practical considerations is by no means self-evident.

We have had such presidential involvement in agency rule-making in this Administration to a limited degree. There are at least three good reasons for providing a clear statutory authorization for the President's role. The first is to remove any doubts as to the authority with respect to the independent agencies. The second is that the particular cases in which the President is likely to intervene should not be

⁵NAACP v. FPC, 425 U.S. 662 (1976); *cf.* Natural Resources Defense Council v. Securities and Exchange Commission, [Current] CCH FED. SEC. L. REP. ¶ 96,832 (D.C. Cir. April 20, 1979).

⁶GELLHORN, BYSE & STRAUSS, ADMINISTRATIVE LAW, CASES AND COMMENTS, 119-122 (7th ed. 1979); Bruff and Gellhorn, *Congressional Control of Administrative Regulation*, 90 HARV. L. REV. 1369 (1977); Schwartz, *The Legislative Veto and the Constitution—a Reexamination*, 46 GEO. WASH. L. REV. 351 (1978); McGowan, *Congress, Court, and Control of Delegated Power*, 77 COL. L. REV. 1119 (1977).

tied up in litigation as to whether he had the authority to intervene and as to the limitations on that authority. The third is that the procedural safeguards for such participation should be defined in advance and not left to case-by-case judicial determination.

NOTICE AND COMMENT RULE-MAKING

At this point, I will depart from the views of the ABA Commission. The ABA Commission recommendation and the pending bills provide for a modified or expedited legislative-type hearing procedure in some cases now governed by the trial-type hearing requirements of 5 U.S.C.A. §§ 554 *et seq.* The ABA Commission concluded that there was no need for analogous revisions of notice and comment rule-making governed by 5 U.S.C.A. § 553.

With all deference to the distinguished lawyers who made this judgment, it seems to me to reflect a debatable assessment of the implications of *Vermont Yankee*.⁷ Professor Davis has predicted that subsequent cases will not treat *Vermont Yankee* as a "reliable guide."⁸ But the Supreme Court is where it is, *Vermont Yankee* is on the books, and the language of that decision throws into question a whole line of decisions, principally in the D.C. Court of Appeals, establishing procedural protections beyond the literal scope of section 553.⁹

In several recent statutes,¹⁰ Congress has provided for a rule-making procedure better adapted to some current issues than the modest provisions developed in a much different context in 1946. I suggest we take another look at revisions of section 553 to cover important rule-making cases, revisions modelled on the Clean Air Act and comparable statutes.¹¹ The elements of a general reform for important rules are clear:

⁷*Vermont Yankee Nuclear Power Corp. v. NRDC*, 435 U.S. 519 (1978).

⁸DAVIS, *ADMINISTRATIVE LAW TREATISE*, 605-616 (2d ed. Vol. 1, 1978); Testimony of Judge Henry J. Friendly before the Committee on Governmental Affairs, United States Senate, 4-5 (May 16, 1979).

⁹*American Airlines v. Civil Aeronautics Board*, 359 F.2d 624 (D.C. Cir. *en blanc* 1966); *cert. denied*, 385 U.S. 843 (1966); *International Harvester Co. v. Ruckelshaus*, 478 F.2d 615 (D.C. Cir. 1973); *Mobil Oil Corporation v. Federal Power Commission*, 483 F.2d 1238 (D.C. Cir. 1973); *Portland Cement Association v. Ruckelshaus*, 486 F.2d 375 (D.C. Cir. 1973), *cert. denied*, 417 U.S. 921 (1974); DAVIS, *ADMINISTRATIVE LAW TREATISE*, Chapter 6 on Rulemaking Procedure (2d ed. Vol. 1, 1978).

¹⁰Clean Air Act § 307, 42 U.S.C.A. § 7607; Toxic Substances Control Act §§ 6(c), 19, 15 U.S.C.A. §§ 2605(c), 2613; Magnuson-Moss Act, 15 U.S.C.A. § 57A; Department of Energy Organization Act, 42 U.S.C. § 7191; DAVIS, *ADMINISTRATIVE LAW TREATISE*, §§ 6.9, 6.10 (2d ed. Vol. 1, 1978).

¹¹Hamilton, *Book Review of Davis, Administrative Law Treatise*, 127 U. PA. L. REV. 855 (1979).

- a provision for oral presentation of data and argument,
- a carefully defined opportunity for cross-examination,
- clear ground rules on ex parte communications,
- the opportunity for affected persons to respond to data considered by the agency,
- a clear definition of the rule-making record,¹²
- a clearer definition of the obligation to make findings, including obligatory discussion of alternatives and of significant comments, and
- a clear definition of standards of judicial review, perhaps "substantial evidence" for factual determinations, and "arbitrary and capricious" for policy determinations.

RULE-MAKING V. ADJUDICATION

It has been suggested¹³ that one unhappy consequence of more stringent rule-making requirements would be to provide an incentive to agencies to resort to case-by-case adjudication as their principal mode of policymaking—a resort perhaps sanctioned by *Chenery II*.¹⁴ The concern seems to me a legitimate one and suggests that we should re-examine the doctrine of *Chenery II* and consider whether the Administrative Procedure Act might not incorporate limits on the imposition through adjudication¹⁵ of substantial new general requirements.

REVISION OF THE FOIA

The recent Supreme Court decision in *Chrysler v. Brown*¹⁶ leaves the protection of confidential data supplied to the government by the private sector to substantial judicial interpretation of the scope of a criminal statute¹⁷—a statute which is itself undergoing reexamination

¹²Pedersen, *Formal Records and Informal Rulemaking*, 85 YALE L.J. 38 (1975); DAVIS, ADMINISTRATIVE LAW TREATISE, §§ 6.4, 6.10 (2d ed. 1978).

¹³Karnel, "Regulatory Reform: Government Renewal or Rout" (July 17, 1979); Woodward & Levin, *Judicial Review of Agency Action*, 31 AD. L. REV. 329, 344 (1979). Bruff & Gellhorn, *supra* note 6, at 1424-26.

¹⁴SEC v. *Chenery Corp.*, 332 U.S. 194 (1947); NLRB v. Wyman-Gordon, 394 U.S. 759 (1969); NLRB v. Bell Aerospace Co., 416 U.S. 267 (1974); cf. *United States v. Storer Broadcasting Co.*, 351 U.S. 192 (1956); DAVIS, ADMINISTRATIVE LAW TREATISE, §§ 7.24 *et seq.* (2d ed. Vol. 2, 1979).

¹⁵SCHWARTZ, ADMINISTRATIVE LAW §66, at 185 *et seq.* (1976); *Morton v. Ruiz*, 415 U.S. 199 (1974).

¹⁶47 U.S.L.W. 4434 (April 18, 1979).

¹⁷18 U.S.C. § 1905; Memorandum of Assistant Attorney General Babcock to All Agency General Counsels (June 21, 1979).

as part of the criminal code codification process¹⁸ The question is whether we should not seek a clearcut legislative treatment of the important issues left in such an unsatisfactory state by *Chrysler v. Brown*.

Any such revision should plausibly provide:

- a clear cut definition of protected private sector information,
- a clear cut treatment of the relationship to other statutes,¹⁹
- a procedure for identifying and segregating such information,
- a procedure for notification to the supplying party of requests for such information,
- a reasonable opportunity to the supplying party to challenge the request before the agency to which the request is addressed, and
- an opportunity for the supplying party to seek judicial review of unfavorable agency action.

CRIMINAL SANCTIONS FOR REGULATORY VIOLATIONS

The criminal code codification bill passed by the Senate in early 1978 made extensive changes in criminal provisions of regulatory legislation, particularly in the culpability language.²⁰ These changes were questioned by the American Bar Association²¹ and vigorously challenged by the business community. Present indications are that criminal code legislation to be considered in the 96th Congress will not deal with regulatory offenses.

The inappropriateness of criminal sanctions for many regulatory violations was recognized about a decade ago by the Brown Commission in the study which became the basis of all subsequent criminal law codification legislation.²² The Brown Commission analysis has been endorsed in more recent studies.²³

¹⁸Section 1525 of S. 1437 (95th Cong. 2d Sess.); REPORT 95-605, PART 1, CRIMINAL CODE REFORM ACT OF 1977, COMMITTEE ON THE JUDICIARY, UNITED STATES SENATE, 508-512.

¹⁹Memorandum of Assistant Attorney General Babcock, *supra* note 17, at 6.

²⁰S. 1437, Title VI.

²¹Resolution of House of Delegates, American Bar Association, February 1979. reproduced in 34 BUS. LAW. 1148 *et seq.* (1979); *Report on Proposed Federal Criminal Code of an Ad Hoc Committee of the ABA Section of Corporation, Banking and Business Law*, 34 BUS. LAW. 725, 743-51, 797-807 (1979).

²²NATIONAL COMMISSION ON REFORM OF FEDERAL CRIMINAL LAWS, STUDY DRAFT OF A NEW FEDERAL CRIMINAL CODE, 1970, xlvii.

²³*Developments in the Law-Corporate Crime: Regulating Corporate Behavior through Criminal Sanctions*, 92 HARV. L. REV. 1227 (1979); Report of the Ad Hoc Committee, *supra* note 21.

The time is ripe for an intensive review of this area with a view to confining criminal penalties basically to cases of fraudulent conduct and to conduct which consciously creates a serious threat to health or safety. Civil penalties and other civil enforcement mechanisms would be employed for less serious violations.²⁴

How should this kind of review be effectuated? One mechanism would be an across-the-board sunset provision on criminal sanctions in regulatory legislation—a sunset provision which might be embodied in the criminal code bills now under consideration. The threat of criminal indictment for violations of technical and obscure requirements not involving morally reprehensible behavior should not be part of the regulator's or prosecutor's arsenal.

Mr. Smith: Thank you, Bill. That brings our panel to an end, but first I would like to conclude with this comment. There is a distinction between the analytic framework that Steve recounted at the outset and the ways in which it is encapsulated and made a part of the decisional process. The regulatory analysis was a way that appealed to us. I think the vast majority of the Commission thinks it would be a mistake to have that be an element of judicial review. There are ways in which one can discipline the government other than resort to the court system, and we have suggested a vast number of those in other portions of our report.

Regulatory analyses are not the only device, or procedural step, in which the concepts of Chapters 3 and 4 can be used. Our approach to regulatory reform is through many roads. Sunset is also a structure within which to apply these principles, and that is the subject of our next panel.

Mr. Grenier: Thank you very much, Dick. I think we will all agree that the first panel got us off to a very fine, flying start for the rest of the program.

²⁴*Developments—Corporate Crime*, *supra* note 23, at 1365 *et seq.*

APPENDIX A

USING COST-BENEFIT ANALYSIS IN REGULATION

Michael S. Baram

Following is the table of contents and concluding section from Mr. Baram's "Final Report to the Administrative Conference of the United States: Regulation of Health, Safety and Environmental Quality and the Use of Cost-Benefit Analysis" (March 1, 1979). This Report was reviewed and approved by the Administrative Conference's Committee on Agency Decisional Processes for purposes of presentation at the Conference's Nineteenth Plenary Session, held June 7-8, 1979. Favorable action was taken on the substance of Mr. Baram's third recommendation. (*See* Section 305.79-4 of the Recommendations of the Administrative Conference of the United States, 44 Fed. Reg. 38,817, 38,826 (July 3, 1979).

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 - 1. The National Environmental Policy Act and C/B/A
 - 2. Various Enabling Statutes and C/B/A
 - a. Environmental Protection Agency
 - b. Nuclear Regulatory Commission
 - c. Other Agencies
 - (1) Army Corps of Engineers (COE)
 - (2) Bureau of Reclamation
 - (3) Food and Drug Administration (FDA)
 - (4) Consumer Product Safety Commission (CPSC)
 - (5) Federal Aviation Administration (FAA)
 - (6) Occupational Safety and Health Administration (OSHA)
 - (7) A Note on Additional Agency Users of C/B/A

IV. Cost-Benefit Analysis Under Executive Orders

- A. Ford Administration "Inflationary Impact" Executive Orders
- B. Carter Administration "Regulatory Analysis" Executive Order
 - 1. Executive Order 12044
 - 2. Guidance for Conduct of Regulatory Analyses by the Agencies

3. Guidance for Conduct of Regulatory Analyses by the Regulatory Analysis Review Group
4. Functions of the Council on Wage and Price Stability and the Regulatory Analysis Review Group
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V. Agency Structuring of Discretion on C/B/A Use

- A. Statutory Authority and Guidance for Use of C/B/A
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VI. STRATEGIES FOR REFORM

A. Findings

As a result of this assessment of federal regulation and the new uses of c/b/a, several general conclusions can be offered.

First of all, use of c/b/a can be viewed favorably from a number of perspectives. For example, to the extent c/b/a is actually used to drive a decision process (and is not merely a cosmetic), and to the extent that the users act objectively, in good faith, and with requisite analytical rigor, *rational decision-making is promoted*. In such cases the derivation and use of inferences and determinations from existing data and information become a more logical process, which, in turn promotes agency credibility and the acceptance of agency decisions by the Executive Office, the courts and Congress.

Further, c/b/a promotes use of a consistent and predictable analytical structure for organizing data and opinions on the numerous issues involved in a proposed regulatory action. Therefore, *procedural due process or fairness can be enhanced* by the resulting clarity in the articulation of the decision-process; and *agency accountability or reviewability by the courts, the Executive Office, Congress and the public can be increased*.

C/b/a also offers decision-makers a *pragmatic method for reaching decisions in the multi-objective, pluralistic value context in which most agencies function*. It offers a utilitarian approach to decision-making, on matters involving varying types and levels of risk, which promotes the general welfare. It is therefore particularly suitable to a democratic society because it strives to accommodate all preferences simultaneously.

Nevertheless, review of actual c/b/a practices has led to identification of several problems and limitations. These can be clustered into three general categories: *Methodological*, *Substantive*, and *Institutional*.

Methodological

Several methodological problems have always beset c/b/a practices. These include, for example, the problems of: (a) quantification, valuation and monetization in considering health, environmental amenities and other factors not normally subjected to market or economic measurement; (b) consideration of attributes in the aggregate without sufficient concern for distributional implications on specific populations and regions; and (c) the choice of discount rates for estimating future costs and benefits.

These problems have become apparent in reviewing NRC decision-making in particular, which provides the richest c/b/a regulatory experience to date. Choice of health values or values for "life and limb," such as \$1000 per man rem in the NRC, will always be a controversial and subjective matter, and should only be dealt with in a sophisticated and open regulatory or Congressional process, sensitive to the essentially arbitrary nature of the task. The low-probability, high-harm risk of reactor meltdown or of geological disturbance leading to catastrophic results cannot readily be accommodated in the c/b/a framework. Yet, as the recent dam failures of other agencies indicate, they must be considered in agency review processes, before construction, to establish appropriate design controls. Disaggregation of attributes to promote consideration of unequal impacts on different populations

and regions is necessary to achieve a true understanding of the distributional implications of decision-making, but seems antithetical to the highly aggregated societal perspective embodied in c/b/a.

Substantive

The substantive issues flow, in part, from the methodological limitations. Valuation, quantification and monetization of environmental and health amenities are considered by the general public and by those professionals, such as doctors and lawyers, whose professional ethics call for maximization of the individual patient's or client's interests, to be an inappropriately economic treatment of factors which transcend economics. Moreover, the c/b/a approach, if highly aggregated, may be insensitive to specific distributional implications as noted above, and may lead to conflicts with Constitutional concepts of equal protection.

The data and assumptions used in c/b/a are often derived from elitist experts and/or regulated organizations motivated by self-interest to a considerable extent. These inputs may be influenced largely by the values of their sources. The courts have started to demand that such inputs be "tested," before use, against the preferences of lay sectors of the public which do not have expertise or data-generating capabilities. In other words, the selection of data on measurements of risks and benefits, the development and application of discount rates, the choice of analytical methods to read the data and the choice of safety factor, for example, are subjectively based determinations to a considerable extent. Judicial requirements of good faith objectively by agencies leads to the conclusion that the data and methods be publicly tested and openly verified before use in c/b/a. Furthermore, the subsequent determination of acceptable risk levels, in the absence of standards for acceptable risk, is a subjective matter, and again, the courts and the public have demanded an open, articulated decision-process.

Institutional

As this review indicates, institutional issues abound. A few bear repeating here. The "crisis management" atmosphere for agency regulation, promoted by Congressional requirements with short deadlines for agency action, and by the media and political and other forces, militates against thoughtful conduct and timely use of c/b/a. The failure of agencies such as NRC and EPA to develop openly coordinated

analytic approaches to shared problems such as radiation and to adopt common values for health effects and environmental attributes; the silence of the CEO on how to conduct NEPA balancing analyses; the lack of EIS and regulatory analysis coordination; the obscure but significant roles played by COWPS and OMB in regulatory decision-making; and the practical difficulties of providing for meaningful public participation and timely access to information and deliberative meetings are but some of the institutional problems identified in this study. Furthermore, the timing of a c/b/a is often conclusive as to its actual influence on decision making: if done too late, it may not do more than provide a *post hoc* rationale for a decision already reached on other grounds.

It has been noted that "we should avoid the erroneous belief that the performance or potential power of analysis will be uniform in all contexts," that "we need to discriminate, rather than to reject analysis *in toto*," that "there is little doubt that analysis has been oversold . . . [but] that performance [to date] should not be taken as defining the limits of this flexible tool . . . [which can] prove to be a most serviceable instrument."*

Appropriate use of c/b/a in decision-making is an issue which lies at the heart of the new regulatory programs for protecting health, safety and environmental quality. This is because each agency is now faced, in the usual case, with multiple statutory objectives which must be reconciled in each decision, no matter how disparate the objectives may be; and because of specific statutory and presidential requirements to conduct various predecisional economic analyses. Therefore, a balancing or "tradeoff" process is increasingly necessitated as the analytical foundation for agency decisions, and the growing use of cost-benefit analysis reflects how agencies are responding to this need.

B. Strategies for Reform

Various regulatory reforms are now being proposed and implemented, and many of them have included provisions for increasing use of cost-benefit and other balancing techniques in regulatory decision-making. These reforms include the "Regulatory Analyses" called for by Presidential order, the creation of RARG, the reconsideration of NEPA

*Schlesinger, "Uses and Abuses of Analysis," Memorandum prepared for the Subcommittee on National Security and International Operations, Committee on Government Operations, U.S. Senate (April 1968).

implementation, amendments to the water and air pollution control laws and other statutes authorizing specific statutory agency programs on health and the environment, and new legislation which would affect all federal agencies and participants in administrative processes. In addition, various measures to improve Congressional legislative and oversight processes, and judicial review of agency decision-making have been proposed. Many of these measures, expressly or implicitly, directly or indirectly, raise the cost-benefit issue.

With this dynamic background in mind, and with the perspective provided by research in the analytic techniques and decision-processes of several federal agencies, several strategies for reform have been developed.

The findings on agency use of c/b/a in regulatory decision-making on health, safety and environmental matters, described in this report, necessitate three sets of reform strategies, which are presented below. The first set deals with the need for Congressional clarification of statutory directives to the agencies to perform c/b/a and supervision on certain key aspects of c/b/a applications. The second set addresses the Office of President, now embarking on a course of "regulatory analysis" of agency decisions. The third set addresses the federal agencies directly and the need for structuring of discretion to correct some of the important defects in their uses of c/b/a.

Finally, it should be noted that the overall intent of these reforms is neither to foster nor exclude the use of c/b/a and other balancing analyses, nor to provide guidance as to when c/b/a should be used, but (1) to ensure good regulatory practices in circumstances whenever such methods are employed; and (2) to ensure generic applicability of the measures proposed, so that the reforms will be implemented in all regulatory sectors where agency balancing analyses are mandated.

1. Strategies for Congressional Reforms

a. Congress should conduct a comprehensive review of agency implementation of its major legislative enactments in the fields of health, safety and environmental protection, for purposes of determining the extent to which agency uses of c/b/a or other balancing techniques in their regulatory decision-processes are consistent with legislative intent, statutory objectives and sound administrative practice.

This review should also include within its scope, consideration of how agency and Executive Office implementation of Executive Order 12044 influences agency implementation of the statutory requirements,

and the identification of conflicts between Executive Order and statutory requirements which have prevented the agencies from acting consistently with legislative intent, statutory objectives and sound administrative practice.

Thereafter, Congress should clarify its legislative intent and ensure agency compliance with its intent, statutory objectives and sound administrative practice by amending these statutes, or taking other necessary legislative actions.

b. Congress should conduct a special review of agency implementation of the *National Environmental Policy Act's* requirements for "balancing analysis" and other methodological requirements of Section 102(2), and therefore should clarify its intent and provide further guidance to the agencies by amending NEPA on the following matters:

- NEPA applicability to agency rule-making;
- Coordination of NEPA implementation procedures with the procedural requirements of Executive Order 12044;
- Whether EPA's impact assessment mandate requires quantification of all or several elements of any subsequent balancing analysis; and to the extent quantification is required, how such quantification is to be achieved; and what, if any, discount rate is to be used for estimating the future impacts of agency action subject to NEPA.
- Whether agencies are required by NEPA to choose the best alternative resulting from the balancing analysis, as the action to be undertaken; or whether and under what circumstances, a less favorable alternative may be adopted.

c. Congress, in enacting new legislation or in amending existing legislation, in the fields of health, safety and environmental quality, should articulate more precisely the factors that federal agencies should consider in reaching decisions, and furnish the "intelligible principles" necessary for agency use in decision-making designed to meet any multiple objectives required by such legislation.

If a cost-benefit approach should be followed by the agency, it should be expressly stated, together with guidance as to how it is to be meaningfully integrated with Executive Order 12044 requirements. If such an approach is not to be followed by the agency, this should also be expressly stated and the required approach described, together with guidance to the agency as to how to pursue the required approach despite possible conflicts with Executive Order 12044 requirements.

If Congress decides to promote a cost-benefit or other balancing analysis approach to regulatory decision-making under any statute, it should maintain oversight over the various critical methodological issues which affect the application of such analytical methods to agency decisions and which thereby lead to significant societal impacts, such as the following issues for example:

- Valuation of intangible costs and benefits,
- Use of discount rates to determine values for future costs and benefits,
- Consideration of distributional effects.

Decisions or guidelines on each of these issues should be developed directly in the Congressional setting or be delegated with guidance to an appropriate interagency body for resolution. In either case, the essentially non-expert, subjective nature of these methodological issues must be recognized and appropriate measures should therefore be promoted to elicit and use values and opinions from all societal sectors.

2. Strategies for Reforms in the Office of the President

The Office of the President, consistent with general policy and Constitutional constraints on Executive intervention in the administration of statutory requirements by the regulatory agencies, should issue an Executive Order amending Executive Order 12044. This new Order should provide further guidance to the Regulatory Analysis Review Group, the Council on Wage and Price Stability, the Office of Management and Budget and the Council of Economic Advisors in order to assure their implementation of Executive Order 12044 in a careful manner which avoids obstructing agency implementation of legislative requirements on health, safety and environmental quality.

The new Order should enlarge the membership of the Regulatory Analysis Review Group (RARG) to include agency and non-governmental personnel representing the legally-protected health, safety and environmental interests at stake in the Regulatory Analysis process.

The new Order should establish that RARG will function in open, deliberative proceedings, of which public notice is given, provide full public access to information that is used and its sources; and, in conjunction with the agencies under review, follow all requirements of the *Administrative Procedure Act*, as amended. Further, the Order should provide that RARG may depart from this policy only if the agency under review justifies such exception on the bases afforded by

the relevant provisions of its enabling statutes and the *Administrative Procedure Act*, as amended. (All references to the *Administrative Procedure Act* include its "Freedom of Information" and "Sunshine Amendments.") Further, the Order should provide that all RARG proceedings and materials germane to any agency's final regulatory action be incorporated in the agency record of decision and becomes otherwise available for purposes of public, Congressional, and judicial review.

Finally, the Order should direct RARG to the following key considerations that it should address and make public findings on, in its review of any proposed agency action under Executive Order 12044:

- Statutory or other authority and guidance for conduct of c/b/a or other balancing analysis by agency.
- Particular methods of analysis selected by RARG and the agency (c/b/a, cost-effectiveness analysis, qualitative or non-numerative "balancing"), and any attributes of such methods which are in potential conflict with governing legislation.
- RARG and agency methods for considering elements of the analyses which are not generally considered quantifiable or capable of expression in monetary units; discounting future costs and benefits; evaluating distributional considerations and other problems.
- Timing of c/b/a or other analysis vis-à-vis actual agency decision-making.
- Weight to be accorded to c/b/a or other analysis in actual agency decision-making.
- Due process and *Administrative Procedure Act* safeguards developed by agency and applied to c/b/a or other balancing analysis-based proceedings (articulation of procedures through regulations; public notice; opportunity for affected interests to testify before agency action and contest agency and RARG analyses; and restrictions on *ex parte* communications).
- Public participation in designing, contributing to and reviewing agency c/b/a's or other analyses.

3. *Strategies for Reforms in All Regulatory Agencies*

a. Each regulatory agency using c/b/a or other balancing analyses in regulatory decision-making, in order to promote consistent and explicit regulatory policy furthering the legislative and Executive requirements under which it operates, should promulgate a generic regulation describing its use of these analyses.

In this regulation, the following key considerations, for each sector of agency regulatory jurisdiction where such techniques are used or expected to be used, must be addressed fully:

- Statutory or other authority and guidance for conduct of c/b/a or other balancing analysis by the agency.
- Particular analytical method or approach selected by the agency (c/b/a, cost-effectiveness analysis, qualitative or non-numerative “balancing”); and any apparent conflicts between this method and the applicable governing legislation.
- Agency methods for handling generally unquantifiable elements of the analyses; discounting future costs and benefits; evaluating distributional considerations and other problems arising under the selected methodology.
- Timing of c/b/a or other analysis vis-à-vis actual agency decision-making.
- Weight to be accorded to c/b/a or other analysis in actual agency decision-making.
- Due process and *Administrative Procedure Act* safeguards developed by the agency and applied to c/b/a or other balancing analysis-based proceedings (articulation of procedures through regulations; public notice; opportunity for affected interests to testify before agency action and contest agency analyses; and restrictions on *ex parte* communications).
- Public participation in designing, contributing to and reviewing agency c/b/a’s or other analyses; and public access to information and assumptions used in the c/b/a’s or other analyses.

b. Thereafter, in any decision-making conducted pursuant to the promulgated regulation, each agency should:

- at the time of public notice of proposed rulemaking or the initiation of licensing or other regulatory proceedings, make publicly available its preliminary findings on such key considerations as they relate to the intended regulatory action and describe fully any actual balancing conducted.
- at the time of final regulatory action, and thereafter, include in the decision record, and otherwise make publicly available, any revised findings on such key considerations as they relate to the final action and describe fully any actual balancing conducted.

Particular care should be given to informing the public fully as to the information and assumptions used in such specific decision proc-

esses, the sources of such inputs, and any reasons for departing from the provisions of the generic regulation.

C. Conclusion

The cost-benefit techniques used today are the analytical descendants of Jeremy Bentham's proposals for reforming legal decision-making through the use of "felicific calculus."[†] Much of the philosophical and humanistic criticism of the Benthamite approach remains valid today, and is reinforced by Constitutional principals which reflect a more holistic approach to governance in a pluralistic society and limit the uses of economic analysis in decision-processes. Simply put, the Constitution does not require that government decision making be premised on simplistic economic analyses.

Nevertheless, a strong argument can be made that providing the greatest good for the greatest number remains one of the essential guidances to the administrative apparatus of government, and that c/b/a represents a potentially workable method for implementing this guidance. The Executive and its agencies have the inevitable responsibility for rational management of the federal enterprise to achieve optimal use of our limited resources, and optimal protection of our diverse interests. Use of c/b/a highlights this Executive responsibility. If such use continues, it must be accompanied by real public participation, by diligent Congressional, Executive and judicial supervision, and by agency "best efforts" to structure their discretion in order to solve the types of issues described in this study.

[†]BENTHAM'S POLITICAL THOUGHT (B. Parekh, ed.) (Barnes and Noble 1973). *See*, in particular, Ch. 5, "Of the Principle of Utility."

APPENDIX B

REGULATORY REFORM EFFORTS OF THE SEC

Roberta Karmel

I am very pleased to be a participant in this Conference because one of my primary concerns since I was appointed a Commissioner of the Securities and Exchange Commission has been regulatory reform. My interest is based, in part, on my sense that essential public trust and confidence in regulatory agencies is being eroded by a growing consensus that regulators are insensitive and insufficiently accountable.

Of course, virtually everyone today is for regulatory reform, which has become a political idea with something for everyone. The regulatory reform movement recognizes that the federal regulatory agencies are a permanent feature of our mixed economy, but demands that these agencies be made more responsive to changing economic and political conditions and operate more effectively and more efficiently. A variety of mechanisms have been suggested to achieve these goals. Most of these mechanisms fall into three major categories: (1) review of regulatory statutes and regulations; (2) selection or substitution of less intrusive and less expensive regulatory techniques for classical regulatory devices; and (3) improvement of the regulatory process.

I should note that although it is easy to obtain a consensus in favor of any of these general objectives or devices, as soon as one proposes a particular mechanism in any detail, such consensus dissolves and the proposal becomes controversial. With that in mind, I will briefly describe some of the regulatory reform efforts of the SEC.

As an advocate of regularized review of regulatory programs by both Congress and administrative agencies, I am pleased to state that the Commission is committed to self-review in several important areas. We are studying the effects of our rules on the ability of smaller issuers to raise capital and we have revised existing regulations and promulgated new regulations in order to ease the regulatory burdens we impose on such issuers. We are also re-examining our program for regulating investment companies, with a view toward relying more heavily on the managers of such companies and less on Commission rule-making for formulating standards of behavior.

There is more which we can and will do. Our Division of Corporation Finance is engaging in an ongoing review of the disclosure provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, with a view toward integrating the requirements of those

statutes and revising some basic reporting forms such as the Form 10-K. I have been encouraging the staff to embark upon a sunset review of the Guides for Preparation and Filing of Registration Statements, and I am confident such a review will soon be underway.

The SEC traditionally has utilized less intrusive regulatory techniques instead of classical regulatory devices. Generally, the Commission has preferred disclosure, self-regulation and competition over standard setting, licensing and rate-making. It can be claimed that the SEC was the first independent regulatory commission to engage in deregulation when the agency ordered the unfixing of stock exchange commission rates on May 1, 1975. Similarly, in 1975, Congress extensively amended the securities laws and directed the SEC to facilitate the development of a national market system which to some degree would substitute competition for further government regulation of the exchange markets. A very recent example of the choice of a less intrusive regulatory technique by the SEC is our recently adopted rule on ongoing private transactions. Instead of establishing a substantive standard of fairness for such transactions, the Commission decided that certain disclosures should be made to shareholders.

Current proposals for improving the regulatory process are numerous and varied. One regulatory reform measure which has had a significant impact on the SEC and other agencies is the Sunshine Act. As a Commissioner, I have been very concerned about regulatory process. I have devoted considerable time and energy to the problem of utilizing our processes to make the agency more responsive to changing economic and legal trends and more informative about our policies and programs.

I should note that regulatory reform is not a panacea for the ills of a pluralistic, post-industrial society. And adverse consequences can flow from reform measures. The review and simplification of rules involves more rule-making, more requests for comments, more pages in the Federal Register. The unfixing of commission rates increased the trend toward economic concentration in the securities industry and dislocated many businesses and employees. And the Commission's work to facilitate the development of a national market system involves the promulgation of extensive new SEC regulations. Open Commission meetings have chilled communication between Commissioners which is important to a collegial body. Nevertheless, I believe that those of us in government have no choice but to embrace regulatory reform. We must convince the American people that the regulation of business by government is workable, efficient, and in the public interest.

