

Prepared Comments of  
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Hearing on the  
Cost Justifying Regulations:  
Protecting Jobs and the Economy by Presidential and Judicial Review of Costs and Benefits

House Judiciary Committee  
Subcommittee on Courts, Commercial and Administrative Law  
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## **I. Introduction**

### *A. Qualifications*

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

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

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

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

### *B. Summary of opinions*

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

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

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

## **II. The public and our economy would benefit substantially from the careful consideration of the costs and benefits of regulations**

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

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

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

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

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

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

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

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

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

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

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

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

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

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

1. *Notices of proposed rulemaking*— One of the most important aspects of the Notice of Proposed Rulemaking process is to obtain guidance from the public about how best to craft a rule. A federal agency should solicit ideas from the public first rather than

develop a predetermined rule before seeking public comment. An agency that can articulate in detail the possible costs and benefits to various segments of our economy of each proposed rule and alternatives to it demonstrates some thoughtful analysis behind the proposed rule. And the agency can explain other forms of the rule, including no new rule, that can be considered. Part of the reason to make these cost-benefit analyses public at the NPRM stage is to enable the public to vet the analyses. Can the analyses withstand public scrutiny? Are they internally consistent? Do the numbers make sense? Here is what the federal agency identifies as the likely benefits and costs of the regulation. Here is what federal agency identifies as the likely distribution of those benefits and costs.

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

### **III. Federal agencies have substantial legal and regulatory requirements, including Executive Orders 12866 and 13563, to document their consideration of the costs and benefits of proposed and new regulations**

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

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<sup>1</sup> Executive Order 12866, Section 1.

<sup>2</sup> Ibid.

Moreover, the Executive Orders instruct federal agencies to evaluate not only new rules but existing rules as well. Executive Order 12866 requires agencies to consider whether existing rules may contribute to a problem that new rules are intended to correct: “Each agency shall examine whether existing regulations (or other law) have created, or contributed to, the problem that a new regulation is intended to correct and whether those regulations (or other law) should be modified to achieve the intended goal of regulation more effectively.”<sup>3</sup>

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

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

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

#### **IV. The executive orders are not sufficient to ensure reasoned rulemaking**

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

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

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

#### **V. The FCC does not effectively document or weigh the benefits and costs of its rulemakings**

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

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<sup>3</sup> Ibid., Section 1 (b) (2).

<sup>4</sup> Executive Order 13563, Section 6(b).

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

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

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

#### **VI. Outside parties that participate in FCC proceedings do not insist that the agency consider costs and benefits of regulations because of the lack of judicial review**

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

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

#### **VII. FCC regulatory decisions would likely improve with greater consideration of costs and benefits**

Careful and thoughtful consideration of costs and benefits of regulation could substantially improve the regulatory decision-making process at the Federal Communications Commission. Whether one agrees or disagrees with the new rules, it is impossible to determine

from the Commission's record whether the benefits of the new rule exceed the cost. The Commission provided no cost-benefit analysis for the new rule, nor did it explicitly consider and calculate the benefits and costs of alternative rules, including no regulation.

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

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

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

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

**VIII. Assigning to a federal agency the responsibility for reviewing the compliance of all agencies—including independent agencies--with requirements for cost-benefit analyses could help standardize practices and give the public a more predictable standard of analysis**

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