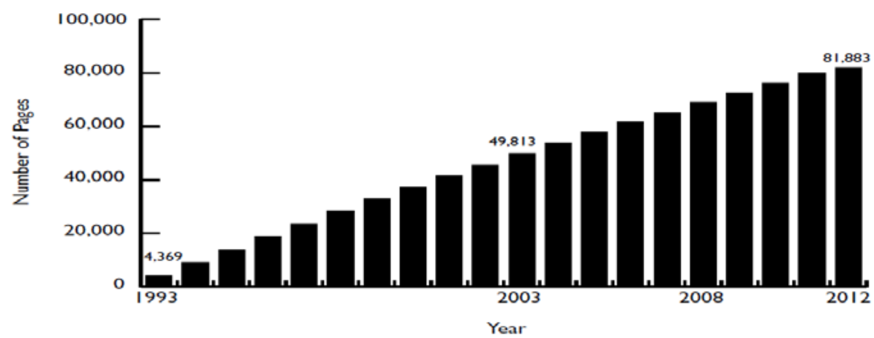
Regulation and the 'Fourth Branch of Government'

By Karen Kerrigan and Ray Keating[1]

In a 2009 *Newsweek* piece titled "We Are All Socialists Now," Jon Meacham wrote, "Bush brought the Age of Reagan to a close; now Obama has gone further, reversing Bill Clinton's end of big government."[2] However one ascribes responsibility for government's decades-long expansion, it's undeniable that federal regulations are increasing in number, size, scope, and cost. And while Congress distracts itself with cliff-hanging debates over the budget, federal bureaucrats are busy enacting rules that are profoundly changing how business operates in America.

Figure 11. Cumulative Final Rules Published in the Federal Register, 1993–2012



Source: National Archives and Records Administration, Office of the Federal Register.

Make no mistake: Regulators now rule the roost. As law professor Jonathan Turley recently noted, "Today, the vast majority of 'laws' governing the United States are not passed by Congress but are issued as regulations, crafted largely by thousands of unnamed, unreachable bureaucrats." "In the new regulatory age," Turley observed, "presidents and Congress can still change the government's priorities, but the agencies effectively run the show based on their interpretations and discretion."[3]

Turley has neatly described this regulatory phenomenon—the massive tangle of ever-growing bureaucrats, rules, regulations, and enforcement orders that comprise the federal administrative state—as the "fourth branch of government." "The rise of this fourth

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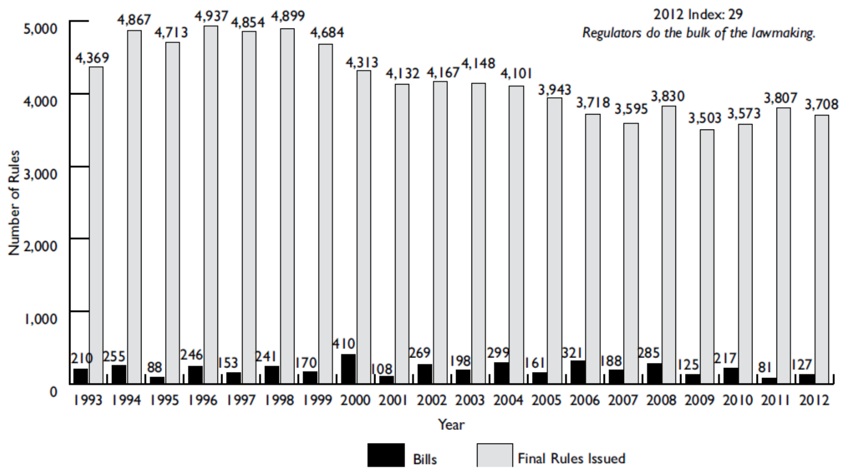
[2] Jon Meacham, "We Are All Socialists Now," *Newsweek*, February 6, 2009 (http://www.newsweek.com/we-are-all-socialists-now-82577)

[3] Jonathan Turley, "The Rise of the Fourth Branch of Government," The Washington *Post*, May 24, 2013 (http://www.washingtonpost.com/opinions/the-rise-of-the-fourth-branch-of-government/2013/05/24/c7faaad0-c2ed-11e2-9fe2-6ee52d0eb7c1_story.html)

branch," he wrote, "*represents perhaps the single greatest change in our system of government since the founding*."[4] [Emphasis added]

The root causes of this change are too complex to examine here. But based on simple observation of the last four years, or even the last twenty, Turley is undoubtedly right. So never mind Congress, for, as George Will wrote, "Congress makes a mockery of itself when the Federal Register, a compilation of the regulatory state's activities, is a more important guide to governance than the Congressional Record."[5]

Figure 20. The Anti-Democracy Index: Rules as Multiples of Public Laws Enacted, 1993–2012



Sources: Federal Register data from National Archives and Records Administration and from Wayne Crews' tabulation at tenthousandcommandments.com. Public Laws data compiled by Wayne Crews from Government Printing Office, Public and Private Laws at http://frwebgate.access.gpo.gov/cgi-bin/browse?DB=112_cong_public_laws&template=plaws.tpl&sortoption=alphabetical; and from National Archives, Previous Sessions: Public Law Numbers, http://www.archives.gov/federal-register/laws/past/index.html.

The verdict is in: We now live in the Age of Regulation. If you own or run a business, you probably know this, and know it first-hand. Whether it's mind-numbing compliance with the tax code, financial disclosure rules, health and safety regulations, Obamacare or various enforcement orders and information requests; business in the Age of Regulation can easily get lost in the bureaucratic maelstrom. How business executives and entrepreneurs navigate the mess can mean, at times, the difference between profitability and financial failure.

The costs of regulation to businesses are real and substantial. Economists John Dawson at Appalachian State University and John Seater at North Carolina State University recently looked at the impact of federal regulation on economic growth, and offered some breathtaking findings. They reported:

> "Regulation's overall effect on output's growth rate is negative and substantial. Federal regulations added over the past fifty years have reduced real output

[4] Ibid.

[5] George Will, "A Congress That Reasserts its Power," The Washington *Post*, January 16, 2011 (http://www.washingtonpost.com/wp-dyn/content/article/2011/01/14/AR2011011404663.html)

> growth by about two percentage points on average over the period 1949-2005. That reduction in the growth rate has led to an accumulated reduction in GDP of about $38.8 trillion as of the end of 2011. That is, GDP at the end of 2011 would have been $53.9 trillion instead of $15.1 trillion if regulation had remained at its 1949 level."[6]

Pick an industry sector and you will find regulatory regimes invariably growing and extending their reach, requiring enormous amounts of compliance time—efforts that sap productivity, reduce employment, and erode profits. Take the health care sector. In a February 10, 2014, analysis, Sam Batkins, director of regulatory policy at the American Action Forum, reported: "Currently, the Office of Information and Regulatory Affairs (OIRA) within the White House is reviewing an avalanche of new Affordable Care Act rules (ACA), including the infamous Individual Mandate Tax. In total, these 28 paperwork burdens total more than 45.7 million burden hours. For perspective, it would take more than 22,800 employees working full-time to complete the new paperwork (assuming 2,000 employee hours annually)."[7]

Or consider manufacturers. According to a study by NERA Economic Consulting, "[R]egulations create real costs for business and slow the growth of the manufacturing sector." NERA found that the "cumulative burden of these regulations," which has been piling up for years, "contributes significantly to long-term slowing of growth of the manufacturing sector."[8]

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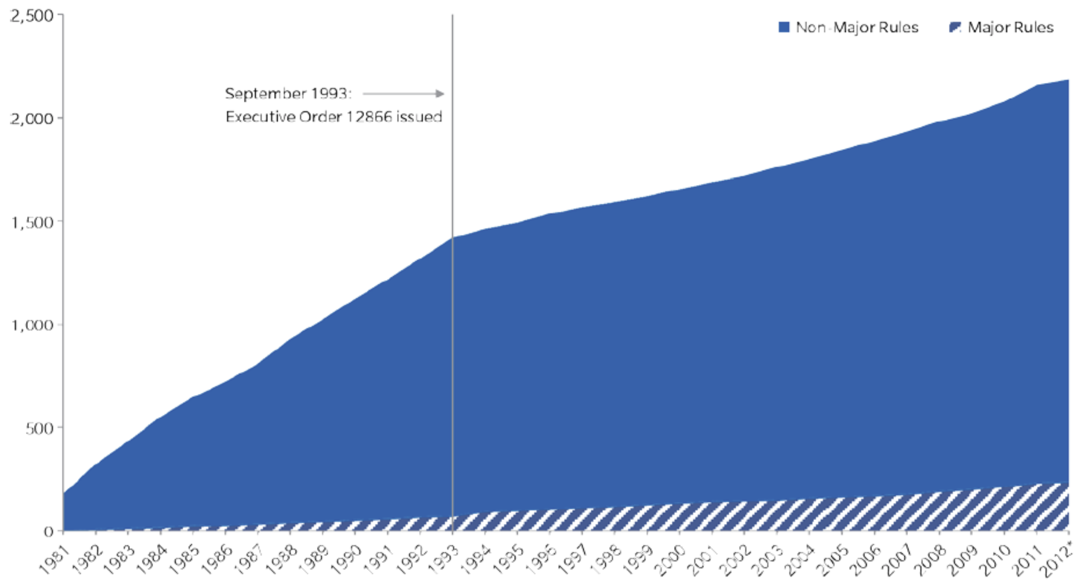
[6] John Dawson and John Seater, "Federal Regulation and Aggregate Economic Growth," January 2013 (http://www4.ncsu.edu/~jjseater/regulationandgrowth.pdf)
[7] Sam Batkins, "White House Holding 45 Million Hours of ACA Paperwork Including the Individual Mandate," February 10, 2014 (http://americanactionforum.org/insights/white-house-holding-45-million-hours-of-aca-paperwork-including-the-individ)
[8] NERA Economic Consulting, "Macroeconomic Impacts of Federal Regulation on the Manufacturing Sector," August 21, 2012 (https://www.mapi.net/system/files/NERA_MAPI_FinalReport_0.pdf)

Figure 5: Cumulative Major and Non-Major Manufacturing Regulations by Year, 1981-2012



Note: President Bill Clinton issued Executive Order 12866 in September 1993, greatly reducing the scope of OIRA regulatory review.
*The count of regulations in 2012 is shown only through April.

Source: OIRA dataset; NERA analysis.

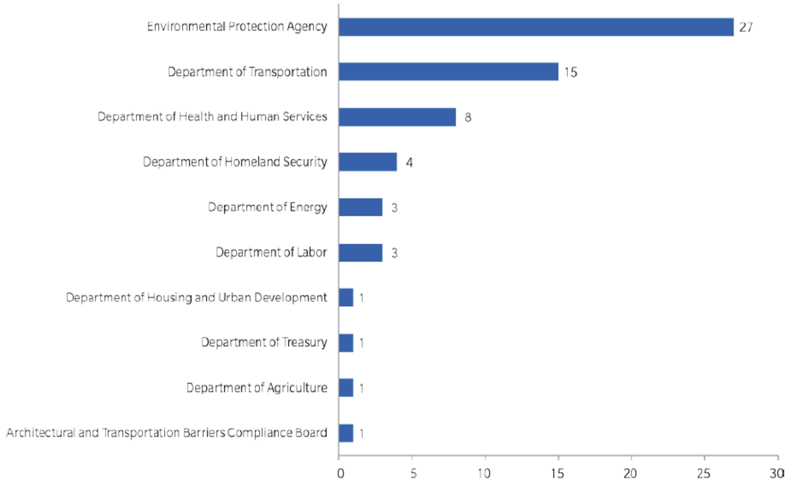
NERA found that all subsectors of the manufacturing sector "are impacted negatively" by regulations. Interestingly, the analysis shows that energy-intensive sectors "are most affected." Specifically, because of the growing regulatory burden, "chemicals and petroleum products sectoral output could fall by about 9.0% to 10% per year on average over the next decade." More broadly, NERA estimates that:

> Output from the subsectors classified under the North American Industry Classification System (NAICS) 31, including food, beverage, and textile manufacturing, could be 2% to 5% lower over the next decade than it would be without the growing regulatory burden. Similarly, output from wood, paper, printing, petroleum, chemical, and plastic subsectors under NAICS 32 could be reduced by 2.5% to 6.5% from where the level of output would be without the growing regulatory burden.[9]

The sheer number of regulations imposed on manufacturers tells a sobering story. NERA found that "2,183 unique regulations have been imposed" on the sector between 1981 and April 2012. Some of these are "major regulations," or those that have a cost of $100 million (or more) annually on the economy. "From 1993 to 2000," NERA noted, "the average number of major regulations was 36. This figure increased to an average of 45 per year from 2001 to 2008. Under the current presidential administration, the average was *72 major regulations per year between 2009 and 2011*."[10] [Emphasis added]

[9] Ibid.
[10] Ibid.

Figure 2: Distribution of 63 Screened Rules by Agency



Note: Light-Duty Greenhouse Gas Emission Standards and Corporate Average Fuel Economy Standards [75 FR 25323] was issued jointly in 2010 by the Environmental Protection Agency and the Department of Transportation. For this reason, the count of rules shown above sums to 64.

Source: NERA

When broken down by manufacturing subsector, NERA shows:

- "41 major regulations and 375 non-major regulations were directly related to the NAICS 31 sector, which includes food, beverage, and textile manufacturing."
- "65 major regulations and 755 non-major regulations were directly related to the NAICS 32 sector, which encompasses businesses involved in wood, paper, printing, petroleum products, chemicals, and plastics."
- "185 major regulations and 1,423 non-major regulations were directly related to the NAICS 33 sector, which includes machinery and transportation equipment."[11]

This frenzy of regulatory activity is taking its toll on the economy, and the public is taking notice. According to a recent survey conducted for The Center for Regulatory Solutions, significant majorities believe there are too many regulations, and that regulations are often counterproductive. This view stems from the public's aversion to the process by which regulations are made, which an overwhelming majority believes is rigged against them. Here are some highlights from the poll:

- 60 percent said government regulations are more likely to "harm the economy" than help it;
- Nearly 66% of respondents said regulations "mostly hurt" America's economic competitiveness, consumers, jobs, entrepreneurs and small businesses, American workers, and "Americans like you";

[11] Ibid.

- Of those who have personally worked with regulations, nearly 75 % of respondents said the experience has given them less confidence in the ability of the government to regulate businesses;

- An overwhelming 84 % of respondents believe that there are too many special interests involved in shaping government regulations.[12]

The public's views on overregulation would seem to indicate a ripe political opportunity for legislative intervention. As CRS's polling results show, there is a bipartisan consensus against overregulation, and Democrats, Republicans, and Independents want policymakers to address it. But gridlock in Congress leaves it seemingly powerless to resolve the problem.

That leaves the courts as the only legal check on the Executive Branch's authority. But the courts for the most part have been disinclined, either by doctrine or temperament, to second guess or overturn the prerogative of regulators. And with several new Obama appointees now on the U.S. Court of Appeals for the DC Circuit—the nation's second most important court that deals principally with federal regulations—the prospect of dislodging the regulatory excesses of the last four years appears highly improbable.

So for businesses concerned about the impact of overregulation on their profitability and license to operate, the Age of Regulation is not going to pass any time soon. If anything, it now appears to be an ingrained fact of American life, at least for another generation. Achieving a significant course correction therefore requires an initial acknowledgement that regulatory reform will take years to accomplish.

Institutional Reforms Needed

So, what can be done to correct this bias towards over-regulation and misguided regulation? Under the current incentive structure, any positive gains from deregulation, for example, almost seem destined to be short-lived. For example, Congress and President Ronald Reagan worked together during the 1980s to rein in regulatory costs. But that was a unique achievement in recent history, and post-Reagan, the pro-regulation incentives took hold once more, and regulatory activity and costs resumed their growth.

Public choice economists understand that institutional and constitutional limitations, or checks and balances, are needed to achieve greater balance when it comes to imposing regulations. Economists James Gwartney and Richard Wagner explained:

> "The challenge before us is to develop political institutions capable of bringing, to the fullest extent possible, the self-interest of politicians, bureaucrats, and voters into harmony with the general welfare of a society. In other words, public choice economists seek to design political

[12] The Center for Regulatory Solutions: "Poll: Big Majority Thinks Regulatory Process Too Secretive, Politicized," (http://centerforregulatorysolutions.org/poll-big-majority-thinks-regulatory-process-too-secretive-politicized/)

> structures and procedures capable of directing the political players to serve the general welfare just as Adam Smith's invisible hand directs market participants to serve the general welfare. With regard to the achievement of this objective, one thing is certain: success rests upon our ability to develop and institute sound rules and procedures rather than on our ability to elect 'better' people to political office. Unless we get the rules right, the political process will continue to be characterized by special interest legislation, bureaucratic inefficiency, and the waste of rent seeking.[13]

Among the possible reforms relating to regulation are the following:

• **Supermajority Votes:** Given the costs of regulatory burdens on businesses, entrepreneurs, workers, and investors, and in turn the potential impact on economic growth and jobs, requiring a supermajority vote (such as 60 percent in each chamber of Congress) to pass bills imposing major regulations on businesses, entrepreneurs and investors would be a check on the bias to regulate. This is aligned with proposals to require supermajority votes to impose tax increases given that regulatory costs are just as real and costly as tax increases to businesses, consumers and the economy.

• **Congressional Approval of Rules and Regulations:** Given that Congress has incentives to pass regulatory measures, but leave the actual details of creating and imposing rules, mandates and regulations to agency bureaucrats, the system amounts to regulation without representation. Members of Congress are able to take credit for imposing regulations, and later, if necessary, to blame agencies and bureaucrats if matters go awry. It is critical to establish full responsibility for regulating to Congress. Therefore, before being finalized and imposed, all major rules and regulations should be subject to votes in Congress.

• **Sunsetting Rules and Regulations:** All new and existing rules and regulations should be sunsetted, so that Congress is required to re-evaluate regulations after a certain period of time. For example, a regulatory measure may have become obsolete due to changes in technology, or transformations of industries. In addition, the basic efficacy of any regulation needs to be periodically reviewed to eliminate or reform regulations that have become outdated, proven ineffective, and/or imposed excessive burdens. Setting a sunset date on regulatory measures makes sense as a check against outdated, inefficient regulation serving as a drag on the economy.

• **Regulatory Budget:** More information and greater transparency regarding federal regulations is desirable, and a regulatory budget, if properly done, could be a tool to achieve such goals. A regulatory budget would provide an accounting of the annual costs and benefits of all federal regulation, along with additional information of regarding the effectiveness of regulations. The challenge of a regulatory budget, however, is to break away from the incentives for government bureaucrats and agencies to minimize the

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[13] James Gwartney and Richard E. Wagner, "The Public Choice Revolution," *Readings in Public Choice* Economics (Ann Arbor, MI: The University of Michigan Press, 2004, edited by Jac C. Heckelman), pp. 15-16.

reported costs and maximize the presumed benefits of regulation. But if a legitimate, independent regulatory budget were established, it could serve as a valuable check on the pro-regulation bias by, for example, having Congress set a cap on the regulatory budget, with costs having to be distributed among agencies and efforts.

In a 1996 study, Clyde Wayne Crews summed up the potential benefits of a regulatory budget: “Regulatory costs imposed on the private sector by federal agencies can never be precisely measured, and a budget cannot achieve absolute precision. Nonetheless, a regulatory budget is a valuable tool. The real innovation of regulatory budgeting is its potential to impose the consequences of regulatory decision-making on agencies rather than on the regulated parties alone… Budgeting could fundamentally change incentives. Under a budget, adopting a costly, but marginally beneficial, regulation will suddenly be irrational. Congress would weigh an agency's claimed benefits against alternative means of protecting public health and safety, giving agencies incentives to compete and expose one another's ‘bogus’ benefits. Budgeting could encourage greater recognition of the fact that some risks are far more remote than those we undertake daily.”[14]

• **Independent Congressional Regulatory Analysis:** Rather than relying on analyses from the Office of Management and Budget or agencies themselves, Congress needs an independent means to analyze rules and regulations, such as subjecting them to rigorous cost-benefit analysis, especially for regulatory legislation under consideration, and for purposes of evaluating existing rules and regulations. This could be done through the Congressional Budget Office or the GAO, and should be paid for by reductions elsewhere in government spending so as to not create additional tax burdens.[15]

The U.S. Constitution is rooted in Madisonian principles of limitations, and checks and balances on governmental powers. Public choice economics is rooted in the same principles, and makes clear the need for institutional and constitutional limitations on the power to regulate. The goal of regulatory reform is not to blindly slash regulations – especially given that many regulations have provided clear benefits for the nation. Rather, reform is needed to bring balance to the regulatory equation, and to limit or check the clear biases that exist, again as both public choice economics and history have shown, to regulate no matter the numerous and often sizeable costs.

[14] Clyde Wayne Crews, “Promise and Peril: Implementing a Regulatory Budget,” The Competitive Enterprise Institute, March 31, 1996, accessed at http://cei.org/studies-issue-analysis/promise-and-peril-implementing-regulatory-budget.

[15] James L. Gattuso and Diane Katz, “Red Tape Rising: Regulation in Obama’s First Term,” The Heritage Foundation, May 2, 2013, p. 9.