
Regulation Reform

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The cost of regulation has four elements: (1) compliance costs, (2) opportunity costs, (3) defense costs, and (4) governmental administrative costs. Defense costs are costs to defend against allegations that rules and regulations were violated. The Small Business Administration estimates that the cost of compliance, defense, and government administration in the United States is about \$1.75 trillion (Crain and Crain 2010, 12).

Opportunity costs are much harder to estimate and may have a bigger impact on the economy. There are two kinds of opportunity costs: the cost of delay and the benefits forgone in connection with projects not undertaken. Regulation has a chilling effect and discourages people from taking chances on innovative products and services. For example, Goldman Sachs decided it was unable to offer Facebook shares to U.S. investors because of uncertainty over the Security and Exchange Commission's (SEC) interpretation of law and regulations (Macey 2011). Although Facebook will eventually go public, regulatory uncertainty has created a delay of more than eighteen months at this writing. Eighteen months in the fast-moving world of global commerce is almost an eternity.

In theory, democracy is a self-correcting system, but this mechanism is thwarted by lobbyists who petition legislators in ways the public never sees and cannot match, by regulators who are captured by the industries they regulate, by special interests that concentrate political contributions, and by bureaucracies insulated from public pressure.

Attempts at reform historically have failed to reduce substantially the burden of regulation and have often resulted in increased regulation. Real reform requires a dramatic paradigm shift in the architecture of regulation. Such a shift is possible if Congress has the courage to act.

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Normative Regulatory Framework

Economic literature is divided into positive and normative economics. Positive economics seeks to describe how economic forces work in an objective fashion. Normative economics deals with values and what should be (Byrns 2011). A significant published literature describes the costs and burdens of regulation. Little is gained by summarizing this literature, so in this article I provide a normative framework for analysis and a principled model for regulatory reform.

Approvals

The Problem

An old proverb says, “He who wastes time, wastes life.” But one of the problems with regulation is that the government has no sense of urgency. In *Griffith v. NJDEP*,¹ a New Jersey Appellate Court held that a delay of seven years in approving permits was not unreasonable. In *Wyatt v. United States*,² the U.S. Supreme Court held that a delay of seven years in approving mining permits was not unreasonable.

Economics Nobel Prize winner Milton Friedman (1999) claimed that Food and Drug Administration (FDA) delays cost lives because its regulatory system is inherently biased against approval. If a safe and effective drug is not approved, there is little criticism of the FDA besides that of the drug maker. However, if a dangerous drug is approved, the FDA and its staffers will be subjected to intense scrutiny and criticism. The same bias against approval exists at every level of government from town zoning boards to federal agencies.³ For the government agency, there is little cost to denial and delay, but a potentially a large cost for approval. This regulatory bias can be reversed, and there are several legal precedents for doing so.

Proposed Standards

At one time, the British Crown reserved to itself the power to grant corporate charters. When the colonies split from the British Empire, state legislatures assumed the sovereign’s powers and granted corporate charters to those of wealth and influence. But the people grew to believe that granting charters to the privileged was bad policy. As a

1. *Griffith v. State of New Jersey*, Department of Environmental Protection, 340 N.J. Super. 596, 775 A.2d 54 (App. Div. 2001).

2. *Wyatt v. United States*, Nos. 99–5054, 99–5059 (Fed. Cir. 2001).

3. I was the seventh lawyer to represent a builder who had been trying to get building permits in Medford, New Jersey, for twenty-five years. I finally resolved the situation when I asked the town’s solicitor to cite any rule or regulation the builder had not complied with. The solicitor could cite none. A state judge directed the township to issue the permits.

result, laws were passed in most states to grant corporate charters to anyone who fulfills basic requirements. Approval is virtually automatic (Carey and Eisenberg 1980).

Approval for an initial public offering is virtually automatic as well. A company goes public by filing a registration statement with the SEC. After the registration statement is filed, if the SEC does not object within twenty days, the registration is effective, and the company becomes a public company.

A similar protocol might be established for other approvals. Each activity for which an individual or business must seek government approval must be regulated by statute. Absent a statute, there is generally no requirement that approval be sought. Statutes have specific requirements or require administrative agencies to set specific criteria for approval. Constitutional equal protection requires all similarly situated persons be treated the same way, and constitutional due process forbids the government from acting in an arbitrary, capricious, or unreasonable manner (Reed et al. 2008). In theory, regulations can be reduced to decision rules that can be quickly evaluated by using software.

Table 1 Model Approval Statute

To promote economic development and improve national competitiveness, the following approval procedure will be used when any individual or business applies for approval required under any law, rule, or regulation within the United States.

- A. All applications for approvals or permits will be made electronically.
 - B. To the extent possible, all governmental agencies will use software to evaluate whether approval should be granted within established laws and regulations.
 - C. Approval for any legal, permitted, and regulated activity involving \$10 million or less will be granted automatically unless the relevant government agency objects within thirty days of the filing of an application for said activity.
 - D. Approval for any legal, permitted, and regulated activity involving more than \$10 million and less than or equal to \$1 billion will be granted automatically unless the relevant government agency objects within sixty days of filing an application for said activity.
 - E. Approval for any legal, permitted, and regulated activity involving more than \$1 billion will be automatically granted unless the relevant government agency objects within ninety days of filing an application for said activity.
 - F. Any government agency that rejects any application for any permit or approval will, within thirty days of said rejection, set forth in detail each and every provision of any law, rule, or regulation that is the basis of said rejection. The governmental agency will also specify the corrective action necessary to bring the application into compliance with the relevant law, rule, or regulation.
 - G. Should any governmental agency fail to detail the reasons for rejection of an application in a timely way, the application will be deemed approved.
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After completion of an application, the approval process should be automatic, subject to a rejection by the relevant government agency. Elimination of uncertainty and regulatory delay would significantly boost the economy. Improvements based on reduction of delay are documented in several World Bank studies (e.g., World Bank 2008, 2010). The model approval statute shown in table 1 suggests a more efficient way to grant governmental approvals.

Standard for Regulation

Current Standards

Constitutional equal protection requires that the interests of individuals and businesses be balanced against governmental interests. The general rule is that government must have a rational basis for laws, rules, and regulations.⁴ The courts will find that a law, rule, or regulation has a rational basis if there is a relationship between a government interest and the law, rule, or regulation in question. For example, there is a rational basis between a reduced speed limit on a tightly curved section of road and the government interest of reducing injuries. The limitation of personal freedom is rationally related to an articulable government interest. Courts strike down as violations of equal protection those laws, rules, and regulations that do not meet the rational-basis tests, but they almost always uphold laws that do meet this test.

Courts require strict scrutiny of laws, rules, and regulations when they have a disparate impact based on a person's race, ethnicity, or national origin. They will uphold laws, rules, or regulations under the strict-scrutiny test only where the government has a compelling interest. Where the strict-scrutiny standard is applied, laws, rules, and regulations are almost always overturned.

A third standard, which has evolved in the past half-century, is the quasi-strict-scrutiny standard, which says that where there is a suspect class such as women or homosexuals, government must have an interest that is greater than a rational basis but less than a compelling interest. These cases are frequently, but not always, decided against laws, rules, or regulations that limit the conduct of those in a suspect class.

The Problem

Part of the problem is that regulators, bureaucrats, and elected officials think they have the moral authority to substitute their judgment about the minutia of life for ordinary people's judgment. Further, when the rational-basis test is used, the difference between having a rational basis and not having one is whether the regulator is a good storyteller. There are many good storytellers in government.

4. *United States v. Carolene Products Co.*, 304 U.S. 144 (1938).

Proposed Standards

The rational-basis test should be replaced with a substantial-harm test. The latter test would require government to demonstrate by clear and convincing evidence that but for the law, rule, or regulation, people or property would suffer substantial harm. The requirement of clear and convincing evidence would preclude government agencies from simply asserting that a law, rule, or regulation will prevent substantial harm while simply substituting their judgment for that of people and businesses. A substantial-harm test would balance governmental interests in public safety with maximum personal and business freedom.

Were the “substantial-harm” and “clear and convincing evidence” standards implemented, they might be used to prune existing laws, rules, and regulations. People and businesses should be able to challenge any law, rule, or regulation on the basis that either (1) the law, rule, or regulation does not prevent substantial harm to people or property, or (2) there is no clear and convincing evidence that the law, rule, or regulation prevents substantial harm to people or property.

Table 2
Model Standard for Regulation

To promote economic development and improve national competitiveness, the following minimum standard is set for all laws, rules, or regulations that restrict individual or business behavior.

- A. No law, rule, or regulation within the United States shall be enacted that restricts individual or business action unless
 - (i) It will prevent substantial harm to people or property.
 - (ii) Such harm to people or property is documented by clear and convincing evidence.
 - B. Once this statute is enacted, all new and existing laws, rules, and regulations that restrict individual or business action may be reviewed by courts of competent jurisdiction, and any law, rule, or regulation that fails to meet the minimum criterion set forth in paragraph A must be declared void.
 - C. Existing laws, rules, and regulations may be challenged by any individual or business restricted by them. Upon filing a challenge action, the relevant governmental agency shall have sixty days to provide the court with clear and convincing evidence that the questioned law, rule, or regulation will prevent substantial harm to people or property.
 - D. Laws, rules, and regulations challenged under this statute may not be challenged again for five years.
 - E. Nothing in this statute shall apply to nationally regulated industries that are inherently dangerous and listed in this statute. The following are inherently dangerous activities for purposes of this statute: nuclear power, airlines, aircraft, and pharmaceuticals.
 - F. Nothing contained herein shall affect any law, rule, or regulation approved under a strict-scrutiny or quasi-strict-scrutiny test.
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Where laws, rules, or regulations are challenged, the government should have a limited amount of time to provide clear and convincing evidence. If no evidence is forthcoming or if it is insufficient or speculative, the courts should be required to nullify any such law, rule, or regulation. Table 2, outlining model standards for regulation, suggests language that can be used to prune needless regulations while protecting public safety.

Concise Standards

The Problem

Government micromanagement is a major impediment to a thriving economy (Cavalli 2011). Regulatory ambiguity makes the situation even worse (Fisch 2010; Society for Human Resource Management 2010). James Madison in *The Federalist No. 62* said that ambiguity in the law poisons the blessings of liberty itself “if the laws be so voluminous that they cannot be read, or so incoherent that they cannot be understood” (1788). But long and complex bills seem to be the norm and have become a drag on both personal liberty and economic activity. For example, the Affordable Health Care for America Act, also known as “Obamacare,” is 1,990 pages long (Computational Legal Studies 2009), and the Dodd-Frank Wall Street Reform and Consumer Protection Act is 2,300 pages long (Wallison 2010). Agencies such as the Environmental Protection Agency, the Department of Health and Human Services, and other governmental agencies publish untold pages of regulations.

The sheer volume of regulations chills innovation and invites governmental agencies to crush any innovation not to their liking. It is also extremely expensive for both government and industry to hire lawyers to interpret and apply such regulations. All of this puts a drag on the economy and makes the country less competitive.

The Solution

The solution is a reform statute that would require all government agencies to reduce their regulatory requirements to a limited number of pages, written in clear, simple English and field tested for understandability by ordinary citizens. For example, regulations might be limited to some definite length—say, no more than the length of the U.S. Constitution, which is about twenty-four pages. Special interests and other opponents of regulatory reform might argue that such a page limit is arbitrary. However, the law recognizes the need to make judgments about cutoffs in the interest of the orderly administration of government. For example, a person must be at least seventeen years of age with parental consent or eighteen without consent to enlist in the military (U.S. Department of Defense 2012), must be at least twenty-one, but not more than thirty-nine to become a West Virginia state trooper (West Virginia State Police 2012), and must be at least twenty-one to purchase alcohol in New Jersey (ABC 2011). Table 3 provides a model statute for drafting laws, rules, and regulations.

Table 3 Drafting Standards

To promote economic development and improve national competitiveness, the following standard shall control all laws, rules, or regulations that restrict individual or business behavior.

- A. No law, rule, or regulation within the United States shall be enacted that restricts individual or business action unless it is
 - (i) Less than or equal to twenty-four pages;
 - (ii) Written in plain English;
 - (iii) Understandable to average citizens.
 - B. Once this statute is enacted, all new and existing laws, rules, and regulations that restrict individual or business action may be reviewed by courts of competent jurisdiction, and any law, rule, or regulation that fails to meet the criteria set forth in paragraph A must be declared void.
 - C. Congress shall have two years to revise existing laws to conform to the requirements of paragraph A, or courts of competent jurisdiction may declare them null and void upon the filing of a challenge by any individual or business affected by such laws.
 - D. Regulatory agencies shall have two years to revise existing rules and regulations to conform to the requirements of paragraph A, but this period of time may be extended for up to two years if substantial revision is needed to enable statutes to conform to the requirements of paragraph A.
 - E. The requirements of paragraph A(iii) will be deemed met if three-quarters of a panel of ordinary citizens numbering at least thirty is able to read, understand, and interpret said laws, rules, or regulations. An ordinary citizen is one who has no legal training or training in the industry or subject matter regulated.
 - F. Nothing in this statute shall apply to nationally regulated industries that are inherently dangerous and listed in this statute. The following are inherently dangerous activities for purposes of this statute: nuclear power, airlines, aircraft, and pharmaceuticals.
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Citizen review panels might be composed of thirty volunteers selected from a pool of candidates paid, say, \$300 per day for their work. It would cost much less to pay such a panel for two or three days of work in reviewing a law, rule, or regulation for clarity (\$18,000 to \$27,000) than it would cost to try one case in federal court to interpret its meaning. If such a panel were unable to understand a law, rule, or regulation after three days of dedicated work, that inability would be a strong indicator that the bill is poorly written and did not meet the requirements of B(iii) in table 3.

Agency Coordination

The Problem

The government is composed of many agencies and departments, each of which has rule-making, investigative, and sanctioning powers. This situation often results

in multiple agencies having jurisdiction over a single project, permit, or enterprise. In addition, laws rules, and regulations often overlap and require contradictory actions.

The Solution

The burden of managing and disentangling such overlap should not be borne by individuals and businesses, but by the government. Table 4 presents a model statute for coordination of agency rules, regulations, enforcement, and adjudication.

Conclusion

Regulations are a drag on the economy and chill innovation. Direct regulatory costs in the United States are \$1.75 trillion per year. The opportunity cost of projects forgone may be higher.

No one disputes the need for some regulation. No one wants to have to test their own pharmaceuticals or inspect the airplanes on which they fly. No one wants the return of child labor. But excessive regulation represents a significant drag on the economy, and it is making the United States uncompetitive on world markets. The issue is how to balance public-safety regulation with maximum individual and business freedom.

Table 4
Agency Coordination

The United States is becoming uncompetitive because of overlapping government agency jurisdiction and conflicting laws, rules, and regulations. The burden of overlapping jurisdiction and contradictory laws, rules, and regulations should not be borne by individuals and businesses, but by the government.

- A. For any legal, permitted, and regulated activity, individuals shall have to deal with only one agency and a single point of contact within such agency, which shall have oversight for coordinating all laws, rules, and regulations for that activity.
 - B. That single point of contact will be responsible for assuring, to the maximum degree reasonable, that the interests of other governmental departments and agencies are considered.
 - C. The single point of contact shall have authority to make findings, reach decisions, enter orders, adjust claims, dismiss causes or cases against individuals or businesses, grant permits, and negotiate with individuals and businesses on behalf of the U.S. government.
 - D. No department or agency within the government shall have standing to challenge the findings or disposition of any matter disposed of through the government's single point of contact.
 - E. Individuals and businesses shall have standing to challenge department or agency actions if they can show lack of due process.
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Four actions can be taken to reform regulations. First, a system should be established whereby approvals are automatically granted unless the government objects within a limited period of time.

Second, a substantial-harm test should replace the rational-basis test in deciding which laws, rules, and regulations will stand. Courts should be required to strike down as void any laws, rules, or regulations that do not actually prevent substantial harm. The burden should be on the government to demonstrate by clear and convincing evidence that substantial harm will be prevented by the law, rule, or regulation. Existing laws, rules, and regulations should also be required to pass the substantial-harm test, and if they do not, courts should be required to strike them down.

Third, all laws, rules, and regulations should be limited to some finite length—for example, the length of the U.S. Constitution—unless the laws, rules, or regulations relate to an inherently dangerous industry, such as nuclear power, aircraft, airlines, and pharmaceuticals. All laws, rules, and regulations should be written in plain English and be understandable by ordinary citizens not skilled in the law or the particular activity being regulated. Model legislation should provide for testing the understandability of laws, rules, and regulations with a panel of ordinary citizens.

Finally, governmental agencies have overlapping jurisdiction, rules, and regulations—some of which conflict with each other. The burden of sorting out overlapping laws, rules, and regulations should be borne by government and not by individuals or businesses. The government should be required to provide a single lead agency and single point of contact in that agency to review, approve, and administer all laws, rules, and regulations for a single individual or business.

Regulations are a drag on the economy and make the United States uncompetitive. However, they can be reformed in a way that protects public safety if Congress has the courage to pass the statutes suggested here.

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