THE IMPACT OF REGULATIONS ON EMPLOYMENT

HEARING

BEFORE THE

SUBCOMMITTEE ON NATIONAL ECONOMIC GROWTH, NATURAL RESOURCES, AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTH CONGRESS

SECOND SESSION

MAY 16, 1996

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THE IMPACT OF REGULATIONS ON EMPLOYMENT

THURSDAY, MAY 16, 1996

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON NATIONAL ECONOMIC GROWTH,
NATIONAL RESOURCES, AND REGULATORY AFFAIRS,
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:10 a.m., in room 2154, Rayburn House Office Building, Hon. David M. McIntosh (chairman of the subcommittee) presiding.

Present: Representatives McIntosh, Fox, Tate, Gutknecht, Shadegg, Ehrlich, Peterson and Slaughter.

Staff present: Mildred Webber, staff director; Karen Barnes, professional staff member; David White, clerk; Bruce Gwinn, minority senior policy analyst; and Liza Mientus, minority professional staff member.

Mr. MCINTOSH. Everyone wants a cleaner environment, a safer workplace, and a healthier life. All Americans want Federal regulations to help us attain those goals.

When we have regulatory programs in which 60 percent of the money spent on the failed Superfund program each year goes to lawyers and consultants instead of cleaning up hazardous waste, the top six most frequent OSHA citations on business are for paperwork violations, no true threats to workers' safety, and FDA delays in approving life-saving drugs and medical devices cost tens of thousands of lives, the Federal regulatory system fails to achieve a cleaner, safer, healthier America.

Instead, Americans are saddled with red tape that costs jobs, lowers wages and destroys opportunities to achieve the American dream for the most vulnerable members of society.

On Tuesday, this subcommittee held a hearing on the unintended consequences of raising the minimum wage. We heard from Don Baisch, who started working in a minimum wage job at Burger King in Eureka, CA, 3 years ago. He said he took the job despite the advice of social service workers who warned him that he could make more money if he stayed on welfare. Well, today, Don is the manager of that Burger King restaurant. He is a self-sufficient, single father, raising his 2-year-old daughter.

Don's boss, Melody Rane, who owns the Burger King, told us that if the federally mandated minimum wage is increased, she won't be able to offer the same job opportunity to others like Don Baisch. In fact, she will have to lay off four full-time and eight part-time workers in addition to raising her prices.

Also, at that hearing on Tuesday, Jim Militello, the owner of Source Team, a company that places disabled Americans in entry-level jobs, testified that raising the minimum wage will make it much harder for people with disabilities to find jobs and part-time work to help them become self-sufficient.

One of Jim's clients, a fellow named Bernie Hellgeth, who was partially paralyzed after a stroke, got a new start with the help of Source Team. Other disabled people may not have that opportunity. Clearly, raising the minimum wage has a real human cost.

One of the things that I want to do is look at the costs of regulations in creating job opportunities and increasing the pay for employees.

This subcommittee has traveled to 15 different cities and held field hearings on the issues of regulations. And witnesses at nearly every hearing have testified that if they didn't have to absorb the huge cost of complying with Federal Government red tape, they would hire more workers or increase their pay.

Bruce Gohman, the president of a small construction company, testified at our hearing in St. Cloud, MN, that he employs only 47 people.

He deliberately keeps the number below 50, although he would like to hire more, because he wants to avoid the additional regulations which come with more employees. Other witnesses from our field hearings are here today and will share their testimony.

We will also hear important testimony from expert economists and policy analysts who have studied how the cost of big Government depresses jobs, wages and overall national economic growth.

One of our witnesses today, Professor Lowell Gallaway from Ohio University, has conducted a recent study for the Joint Economic Committee which shows that limiting big Government spending is critical to raising the average American worker's wages.

In fact, it shows that if Federal spending levels were held constant in their 1965 level and Federal taxes were adjusted accordingly, the typical worker would have taken home enough additional pay between 1973 and 1994 to buy a new home.

Regulations make it more expensive for businesses to hire workers, particularly small businesses, which account for more than half of the total employment in the United States.

As Mark Wilson, a labor policy analyst at the Heritage Foundation, will show, the average cost of hiring an employee in private industry is $17.10 per hour, 43 percent of which is due to Government regulations, taxes and mandated benefits.

For a minimum wage worker, the cost is $4.76 per hour, 22 percent of which is due to Government regulations, taxes and mandated benefits.

We must reduce the cost of big Government so that workers can take home more pay. Getting rid of unnecessary regulations and counter-productive regulations will leave small businesses with more money to hire workers and pay workers higher wages.

We all want a cleaner environment, a safer workplace and a healthier life without the burden of unnecessary red tape, which costs us jobs and costs the American worker real increases in their standard of living.

But our regulatory system is broken. It fails to protect Americans, and it imposes huge costs. I believe that we can both protect public health and safety, create more jobs and increase wages for American workers, but it will take real reform of our regulatory system to accomplish that.

I want to thank the witnesses who are here today for sharing your testimony. We will schedule an additional hearing in which your testimony will be made available to Government officials responsible for these regulations, and we will seek to find out their rationale for imposing these costs on the American people.

[The prepared statement of Hon. David M. McIntosh follows:]

ONE HUNDRED FOURTH CONGRESS

Congress of the United States

House of Representatives

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

2157 RAYBURN HOUSE OFFICE BUILDING

WASHINGTON, DC 20515–6143

Opening Statement
Chairman David McIntosh
Subcommittee on National Economic Growth,
Natural Resources and Regulatory Affairs
May 16, 1995 Hearing on "The Impact of Regulations on Employment"

Everyone wants a cleaner environment, a safer workplace and a healthier life. All Americans want federal regulations to help us attain those goals. When we have regulatory programs in which:

- Sixty percent of the money spent on the failed Superfund program each year goes to lawyers and consultants instead of to clean up hazardous waste;
- The top six most frequent OSHA citations on business are for paperwork violations, not true threats to workers' safety;
- And FDA delays in approving life-saving drugs and medical devices cost tens of thousands of lives;

the federal regulatory system fails to achieve a cleaner, safer, healthier America.

Instead, Americans are saddled with red tape that costs jobs, lowers wages, and destroys opportunities to achieve the American dream for the most vulnerable members of society.

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Don's boss, Melody Rane, who owns the Burger King, told us that if the federally mandated minimum wage is increased, she won't be able to offer the same job opportunity to the next Don Baisch. In fact, she will have to lay off four full-time and eight part-time workers in addition to raising her prices.

Jim Militello, the owner of Source Team, a company that places disabled Americans in entry-level jobs, testified that raising the minimum wage will make it much harder for people with disabilities to find jobs and become self-sufficient. Bernie Hellgeth, who was partially paralyzed after a stroke, got a new start with the help of Source Team. Other disabled people may not have that opportunity.

Clearly, raising the minimum wage has a real human cost. There is a better way to raise wages which also creates more jobs -- that is easing the burden of regulations on employers. As our witnesses today will testify, regulations kill jobs.

This Subcommittee has traveled to 15 cities and held field hearings on the issue of overburdensome regulations. Witnesses at nearly every hearing have testified that if they didn't have to absorb the huge cost of complying with government red tape, they would hire more workers or pay higher wages. Bruce Gohman, the president of a small construction company, testified at our hearing in St. Cloud, Minnesota that he employs only 47 people. He deliberately keeps the number below 50, although he would like to hire more, because he wants to avoid the additional regulations which come with more employees. Other witnesses from our field hearings are here today to share their stories with us.

We will also hear important testimony from expert economists and policy analysts who have studied how the cost of big government depresses job, wage, and overall national economic growth. One of our witnesses today, Professor Lowell Gallaway from Ohio University, has conducted a recent study for the Joint Economic Committee which shows that limiting big government spending is critical to raising the average American worker's wages. In fact, it shows that if federal spending levels were held constant at their 1965 level and federal taxes were adjusted accordingly, the typical worker would have taken home enough additional pay between 1973 and 1994 to buy a home.

Regulations make it more expensive for businesses to hire workers -- particularly small businesses which account for more than half the total employment in the United States. As Mark Wilson, labor policy analyst at the Heritage Foundation, will show, the average cost of hiring an employee in private industry is $17.10 per hour, 43% of which is due to government regulations, taxes and mandated benefits. For a minimum wage worker the cost is $4.76 per hour, 22% of which is due to government regulations, taxes and mandated benefits. We must reduce the cost of big government so that workers can take home more pay. Getting rid of unnecessary and counterproductive regulations will leave small businesses with more money to hire more workers and pay their workers higher wages.

We all want a cleaner environment, a safer workplace, and a healthier life -- without the burden of red tape that costs jobs. But our regulatory system is broken. It fails to protect Americans and it imposes huge costs. I believe that we can both protect public health and safety and create more jobs and higher wages for American workers, but not without real reform that restores common sense to government regulations.

Mr. McINTOSH. Let me ask now if any of my colleagues have an opening statement. I notice none of our colleagues from the minority are here, but Mr. Shadegg, do you have an opening statement?

Mr. SHADEGG. Mr. Chairman, I don't at this time. Thank you.

Mr. McINTOSH. Thank you. Mr. Tate, do you have an opening statement?

Mr. TATE. Thank you, Mr. Chairman. I'd just like to add that I just want to thank the chairman for coming out to Washington State to have a field hearing where we had the opportunity to hear from individuals that we'll hear from in a few minutes.

I think it drove home the point that overregulation is strangling the opportunities for working people to get family wage jobs, for people to go out and start small businesses.

And I just commend your leadership even in the face of adversity many times here in Congress where people are trying to fight us every step of the way defending the status quo, defending the way things have always been done.

I just want to commend the chairman for his efforts to lead the charge to bring some common sense back to our regulatory process.

Mr. McINTOSH. Thank you, Mr. Tate. I appreciate it. I appreciate you helping to host that field hearing out in Washington State.

Mr. Ehrlich, do you have any opening statements or remarks that you'd like to make today?

Mr. EHRLICH. I have nothing to add to Congressman Tate's comments. He certainly put it very well.

Mr. McINTOSH. Thank you very much. Mr. Gutknecht, do you have any opening remarks?

Mr. GUTKNECHT. Mr. Chairman, I just want to say I'm sorry that I didn't make it to Washington. I do want to commend you for the people that you have brought before this subcommittee, not only in the field hearings but here in Washington.

We have forgotten for too many years, I think, in the Congress that regulations have consequences and that there are costs to everything that this Congress does. And I think it's good that we bring in some of these folks to hear what is really happening out there beyond the great beltway. So I look forward to the testimony today.

Mr. McINTOSH. Thank you very much, Mr. Gutknecht. And by the way, Randy informed me, when we had the field hearing there, that we had arrived in the real Washington.

Let me now call forward our first panel of witnesses.

They are Judi Moody, who is the owner of CEG Northwest; Gary Bartlett, president of GW Bartlett & Co.; Dick Walton, owner of Maroney's Cleaners & Laundry; Tommy Alexander, owner of J.T. Alexander & Son; and James Jackson, operator of four Amoco stations and president of Washington-Maryland Service Station Association. Thank you all for joining us.

[Witnesses sworn.]

Mr. McINTOSH. Thank you. Let the record show that each of the witnesses answered in the affirmative. Please go ahead and take a seat.

As our first witness in this panel today, I'm going to call Mr. Gary Bartlett, who is president of G.W. Bartlett & Co., a small manufacturing company that he started in his family's garage and has now grown to more than 100 employees which sells products around the world.

I had the good fortune of meeting Gary when I was first running for Congress. He came to me and said, "I can compete in a world marketplace and sell products in the automobile industry that competes with Germany and the Japanese, but my biggest enemy is Uncle Sam and all of the red tape and the regulations that they impose upon me."

Gary, I appreciate you coming forward. I also want to say a word of thanks on behalf of the people of the Second District for your hard work in the White House Small Business Conference where you very well represented the interests of employees and employers in the Second District. Thank you, and please share your testimony with us.

STATEMENTS OF GARY BARTLETT, G.W. BARTLETT CO.; JUDI MOODY, OWNER, CEG NORTHWEST; RICHARD WALTON, OWNER, MARONEY'S CLEANERS & LAUNDRY; JAMES JACKSON, WASHINGTON-MARYLAND SERVICE STATION ASSOCIATION; AND TOMMY ALEXANDER, OWNER, J.T. ALEXANDER & SON, INC.

Mr. BARTLETT. Well, thanks for those comments. With what I did last summer for small business, the way I look at it, with the problems that I see in business, it was the very least that I could do.

Thank you for asking me to testify before the House Subcommittee on National Economic Growth, National Resources, and Regulatory Affairs about one of my experiences with Government regulation.

I'm Gary Bartlett, president of G.W. Bartlett Co. of Muncie, IN. I was asked by Congressman McIntosh to testify about the impact of regulations on my business and the resulting impact on employment.

This brief narrative describes only one instance of regulatory cost. The overall cost of unnecessary regulation is difficult for me to determine.

For example, two EEOC claims in 1 year cost nearly $100,000 to defend, and we won both of them. 1995 was a relatively quiet year with regards to regulation. 1996 and 1997, however, could prove to be extremely costly.

The cost of unnecessary regulation is not just the direct cost for attorneys, consulting firms, construction or fines. There is a human cost as well.

The money that we have wasted could have been spent on making our business expand. Expansion in my business equates to more employees.

The following more defined regulatory costs could prevent us from hiring an additional 100 employees within the next 18 months.

A brief history of the business. I started G.W. Bartlett Co. in October 1975, while working for my dad and uncle at their tire store on Broadway in Muncie, IN.

Before and after their normal working hours, my brother and I rented space and equipment from them to perform necessary duties for my newly formed company.

We did mechanical work on foreign cars in those days, and my dad and my Uncle Ed otherwise would have turned that business down.

We moved the business to 1912 Granville Avenue in October 1976. Although our business started primarily to work on foreign cars as mechanics, it has evolved over the years into a manufacturer of high-end interior trim components for use in the automotive aftermarket and the original equipment automotive market. We also manufacture leather golf accessories.

Our marketplace is about evenly split between Europe and America at the present time. We have grown from two people in 1975 to about 100 people in America and 10 people in our office in Kempston, England.

Of the Government-created regulatory problems that I've experienced over the last 9 years, including frivolous EEOC claims, nonexistent OSHA infractions, problems with the Clean Air Act, problems with the Clean Water Act, compliance with the Americans with Disabilities Act, problems with covert compliance and complying with the FMLA, an EPA problem that I have, has been seemingly unsolvable.

In March 1986, I received a letter from the State Board of Health asking me to report any underground storage tanks that were on my property.

And Mr. Chairman, in the book of information I gave you, there is a copy of that letter in that.

Being a good citizen and responsible business owner, I duly reported a partially submerged 275-gallon crank case waste oil tank.

When we would change the oil on a car, we would pour the used oil into a funnel inside of the building. The used oil would go from the funnel through the wall via a 3-inch pipe into this partially submerged 275-gallon galvanized tank.

In October 1989, a heavy rain caused the tank to float from its position. As the tank was no longer being used, I made the second mistake. I decided to have it removed by the book. And my letter also is included.

At that time, in October 1989, I had no idea of the test procedures and requirements necessary. Subsequent soil testing that was required showed hydrocarbon soil contamination around the tank.

Over the years, there were times that the tank did overfill, but we would recognize that and clean it up, as it was in a reasonably visible space, and we didn't want oil showing up around the tank.

I thought that a minor excavation would correct an otherwise insignificant problem. After the monitored excavation monitored by IDEM, or Indiana Department of Environmental Management, I was instructed to fill in the hole by IDEM field representative Phil Eley. I thought the problem was behind me.

By August 1991, I had not received a no further action required letter and discovered that IDEM would not approve or disapprove my actions to date—letter also included in that—and further, to my dismay, Phil Eley and most of the others that I had worked with no longer worked with IDEM.

In February 1992, I needed to expand part of our building over the contamination site. The cleanup process began to repeat itself.

I hired Ontario Environmental to do a Phase II environmental audit to determine the exact location of the remaining contamination.

After numerous calls and letters to local, State and Federal officials, including President Bush, Kathy Prosser, Commissioner of IDEM, did respond finally and sent cleanup project manager Michael Anderson to oversee our project.

We partially demolished the building in question and excavated yet more soil. In May 1994, after rebuilding the partially demolished old building and building over the contaminationsite, Ashlee Insco, a low-level clerk at IDEM, misread an engineering report and reclassified us from special waste to hazardous waste.

Even with test results to the contrary, Ashlee Insco refused to back off. Mike Penning, from IDEM's Hazardous Waste Compliance Section, drove up to Muncie to inform me that IDEM was in the process of filing criminal charges against me.

This time I had to hire another consulting firm, Hydrotech of Anderson, IN, utilize the services of Kerimeda Environmental again and Barnes and Thornburg for legal work to defend myself against these charges.

Ashlee Insco still refused to back off, and if it wasn't for Mike Anderson's intervention, I have no idea where it would have gone.

The results. The contaminated soil is still there. I received approval from Mike Anderson to spread it out, and now it has grass growing from it.

There is no groundwater contamination. It is not migrating, and there is no threat to humans, plants or animals. I would guess that the contamination did not come from our waste oil tank but from the 1950's or 1960's, when a print shop was in the facility.

It will cost me an additional $90,000 to $150,000 to complete a useless cleanup. I've wasted to date $55,919.11. I've wasted hundreds of unproductive hours. I've invested $400,000 of my own money in the real estate.

We now need to sell this property to finance a new facility. We're just simply running out of room. But unfortunately, banks won't finance property with environmental problems, therefore virtually eliminating any potential buyers.

If I can't sell my building on Granville Avenue, eventually I'll expand, because we'll be forced to do it, but the loss of $150,000 to $200,000 will certainly slow down growth. If we move to a larger facility, I would estimate that we'll hire and train 100 new people within 19 months. If I elect not to move, we won't hire anybody.

The biggest cost to me, though, is how I now view my own Government. After years of continual attacks, I've come to look at them as the enemy.

Small business people like me have many major obstacles to consistently overcome. They can include foreign competition, changing market trends or hundreds of others, but the biggest impediment to growth for me is my own Government. Thank you very much.

[The prepared statement of Mr. Bartlett follows:]

G. W. Bartlett Co., Inc.

HOUSE SUBCOMMITTEE ON NATIONAL ECONOMIC GROWTH,
NATURAL RESOURCES AND REGULATORY AFFAIRS
THURSDAY, MAY 16, 1996
TESTIMONY OF
GARY W. BARTLETT
PRESIDENT OF G. W. BARTLETT COMPANY, INC.

Thank you for asking me to testify to the House Subcommittee on National Economic Growth, Natural Resources and Regulatory Affairs about one of my experiences with government regulation.

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I started G. W. Bartlett Company in October 1975 while working for my dad and uncle at their tire store on Broadway Avenue in Muncie. Before and after their normal working hours my brother and I rented space and equipment from them to perform the necessary duties for my newly formed company. We did mechanical work on foreign cars that dad and Uncle Ed otherwise would have turned down.

The new business moved to 1912 Granville in October of 1976. Although the business started primarily to work on foreign cars, it has evolved over the years into a manufacturer of high end interior trim components for use in the automotive aftermarket and the original equipment market. We also manufacture leather golf accessories. Our market place is about evenly split between Europe and America.

We have grown from two people in 1975 to about 100 here in America and 10 in our office in Kempston, England.

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Muncie Indiana 47303-2701
United States of America

317-289-1586
800-338-8034: US & Canada
317-289-1251: Facsimile

G. W. Bartlett Co., Inc

Of the government created regulatory problems that I have experienced over the last 9 years (not the 19 1/2 that I have been in business) including frivolous EEOC claims, non-existent OSHA infractions, problems with the clean air act, problems with the clean water act, compliance with the ADA, problems with COBRA compliance, and complying with the FMLA an EPA (or IDEM) problem that I have has been unsolvable.

In March of 1986 I received a letter from the State Board of Health asking me to report any underground storage tanks that were on my property (see first letter in IDEM letter section). Being a good citizen and a responsible business owner, I duly reported a partially submerged 275 gal. crankcase waste oil tank. When we would change the oil in a car we would pour the used oil in a big funnel inside of the building. The used oil would go from the funnel through the wall via a 3 inch pipe into this partially submerged 275 gal. tank.

In October of 1989 a heavy rain caused the tank to "float" up from its position. As the tank was no longer being used, I made the 2nd mistake. I decided to have it removed by the book (see first letter, G. W. Bartlett Co. to IDEM). At that time (October 6, 1989), I had no idea of the test procedures and requirements necessary. Subsequent soil testing required showed hydrocarbon soil contamination around the tank. Over the years there were times that the tank overfilled and oil did escape. These times were rare and were caught and rectified quickly.

I thought that a minor excavation would correct an otherwise insignificant problem. After the monitored excavation I was instructed to fill the hole in by IDEM Field Representative, Phil Eley. I thought that the problem was behind me.

By August, 1991 (approximately) I had not received a "No Further Action Required" letter and discovered that IDEM would not approve or disapprove my actions to date (see Anne Black letter of September 11, 1991) and further to my dismay Phil Eley and the others that I had worked with were no longer with IDEM.

In February of 1992, I needed to expand part of our building over the contamination site. The clean up process began to repeat itself. I hired Ontario Environmental to do a "Phase II" Environmental audit to determine the exact location of the remaining contamination. After numerous calls and letters to local, state and federal officials including President Bush, Kathy Prosser, Commissioner of IDEM did respond and sent Clean Up Project Manager, Michael Anderson to oversee our project.

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G. W. Bartlett Co., Inc.

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The Results

The contaminated soil is still here. I received approval from Mike Anderson to spread it out and it now has grass growing from it. There is no ground water contamination. It is not migrating, and there is no threat to humans, plants or animals. I would guess that the contamination did not come from our waste oil tank, but from the 1950's and 60's when a print shop was in the building. It will cost me an additional $90,000.00 to $150,000.00 to complete a useless clean up. I have wasted $55,919.11. I have wasted hundreds of unproductive hours. I own this building. I have $400,000.00 invested in the real estate. I need to sell this property to help finance a much needed new facility, but unfortunately banks won't finance property with environmental problems, therefore, virtually eliminating any potential buyers. If I cannot sell my building on Granville Avenue, I will eventually expand anyway. The loss of $150,000.00 - 200,000.00 will certainly slow down growth. If we move to a larger facility, I would estimate that we would hire and train 100 new people within 18 months. If I elect not to move, we won't hire.

The biggest cost to me, though, is how I now view my own government. After years of continual attacks I have come to look at them as the enemy. Small business people like me have many major obstacles to constantly overcome. Those can include foreign competition, changing market trends or hundreds of others. But, for me the largest impediment to growth is the current adversarial posture of the Federal Government.

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Mr. MCINTOSH. Thank you very much, Mr. Bartlett. Let me say your entire book of materials here will be put into the record.

Let me at this point say that I have been called to a meeting with some of the leadership on this minimum wage issue.

So I'm going to deputize one of our members, Gil Gutknecht of Minnesota, to Chair the meeting, after consulting with our Vice Chairman, Mr. Jon Fox, and Gil will continue to do that.

I was wanting to ask one quick question out of order, if I could have unanimous consent. What would you estimate as the percentage of your payroll which you listed in 1994 as being about $1.7 million, as a percent of that, what would you estimate your annual cost to comply with regulations were during that year?

Mr. BARTLETT. I have done some homework on that and had our accounting department put numbers together on 1994, and 1994 was a relatively easy year for regulation for us.

But of $1.7 million in payroll, we spent $30,456 on various fees relating to Government compliance and regulation. So as a percent, in 1994, about 1.7 percent of payroll or $406 per employee, and that was an easy year.

Mr. MCINTOSH. That was for outside consultants and fees?

Mr. BARTLETT. Yes.

Mr. MCINTOSH. Of that payroll, how many people on your staff spend time doing paperwork to comply with Federal regulations?

Mr. BARTLETT. I would think that nobody on the production floor does, but everybody in our office outside of the sales department. We probably have 10 people that work on it, certainly not every day all day long, but every week there is a problem that comes up that some 1 or more of the 10 people that run the office have to deal with it.

Mr. MCINTOSH. Out of a total employee force of 100?

Mr. BARTLETT. Right now we are about 85 employees.

Mr. MCINTOSH. On the line?

Mr. BARTLETT. Total employees in our Muncie facility.

Mr. MCINTOSH. As of today?

Mr. BARTLETT. As of today.

Mr. MCINTOSH. So part of the time well over 10 percent of your employees are spending their time complying with Federal regulation?

Mr. BARTLETT. That is correct.

Mr. MCINTOSH. If you have a chance, when you get back, if it's possible to give a rough estimate of that $1.7 million, how much of that goes to pay people who spend time complying with regulations. That would be helpful to the committee, and we'll add that to the record.

Let me say thank you to all of our witnesses for coming today, on my behalf. We've got a great subcommittee of chiefly freshman and will take your testimony and use it to continue to fight to roll back these unnecessary regulations. So at this point I'm going to turn over the Chair to Mr. Gutknecht who will continue with the hearings.

Mr. GUTKNECHT [presiding]. OK. I'm going to yield to my colleague from the great State of Washington, Representative Randy Tate, for the purposes of an introduction.

Mr. TATE. Thank you, Mr. Chairman. I'm very pleased to introduce Judi Moody to the subcommittee, and I want to thank Judi for traveling all the way back here to the other Washington, 3,000 miles away from her home, to deliver important testimony that this committee needs to hear.

Judi is a small business owner from Sumner, WA, which is a small city in western Washington. Her and her husband have owned a small manufacturing representative business for years.

We had a hearing out in Washington State, and during the open mic period Judi had the opportunity to speak for a minute or two.

And I can tell you both the chairman and myself are very impressed with what she had to say and thought it was important that Judi come all the way back here to Washington, DC, to deliver this message directly.

Judi has also been active in citizens' efforts locally, whether it be limiting the size and scope of State government to protecting profit rights of individuals in Washington State.

Let me tell you why. She has seen close and firsthand how Government regulations have squashed her opportunities to create a second small business, and she is going to tell us a little bit about that today.

Judi represents countless Americans out there that are trying to open small businesses but many times shy away or are just flat out discouraged by the regulatory process and burden that's thrust upon them.

I think the committee is going to have their eyes opened today by some real insightful testimony. I just appreciate Judi and her husband taking the time to come all the way back here and time away from their business and family.

Mrs. MOODY. Thank you very much, Congressman Tate and people of the subcommittee. I'd like to introduce my husband, Tom, who came all this way with me. Thank you very much.

My testimony is, I suppose, very typical of a lot of people that are going through the same things we are in trying to form a small business, although certainly not quite as compelling as the gentleman on my right, who just boggles the mind on what he has gone through in his business.

But I want to say that, like Randy Tate said, we have a small manufacturer's representative firm, we have for about 16 years. We have no employees at this time. We have subcontracting salespeople who get paid on commissions on the sales that they do.

Unfortunately, given the recent changes in the retail and wholesale marketplace in this country, we feel that our time is limited in the business that we're currently in.

As manufacturers and retailers across the country, profits are squeezed. They're downsizing. I guess you could say we're the classic middlemen who are most at risk of being phased out of the economic spectrum.

Like the fabled Willy Loman in "Death of a Salesman," my husband, who is in his early 50's, feels that he has nowhere in the corporate structure to start over, and I doubt that I would, either, at this stage of our career. So in that regard, being the entrepreneurs that we have always been, we have recently begun seeking out new business opportunities, and we hit on an idea which we thought would be relatively simple, which would be opening up a small paperback recycling bookstore and maybe serving espresso, coffee and snacks.

I don't know if you people are aware, but the other Washington is famous for coffee, and espresso stands dot every corner like slot machines and gas stations in Las Vegas.

So therefore, we thought, well, that's a natural profitmaker. So we went to a food convention in our local area, checking out the opportunities with espresso stands and different food items and things like that that we could sell in this little business.

We were, kind of, having a good time and going around from booth to booth sampling all the food, looking at the espresso machines, comparing costs and all this, and we finally came to a booth by the State of Washington Regulatory Agency called the Labor and Industries Department, whereby we learned that before we even secured a location and opened the door we would be besieged by book after book and form after form of regulations—everything from needing to provide industrial insurance for employees, chemical hazards awareness forms, general educational, medical first aid requirements, personal protective equipment requirements—all of this for the possibility of hiring one, maybe two employees to sell books and serve coffee.

It seemed that we would need a lawyer before we would even open the door, and having come out of a business that was not really regulated—the only regulations we faced are with the IRS, proper reporting of our tax forms—this is sort of mind-boggling, and we're only just touching the surface on local regulations. And I realize I am talking about State and local regulations here, but the very thought of dealing with so many layers of overlapping bureaucracy between local, Federal, State, county and city, who knows what each city requires, let alone the county?

And we hadn't even got to the health department yet, let alone tax reporting for having one employee, maybe two employees.

At the current time, for instance, we have a Keogh plan that covers my husband and myself for our retirement, and we've put into this plan for the last 15 years.

But I understand if we hire one employee we have to contribute equally to that employee. Whether or not we make a profit as a business or not, we must contribute to that employee's self-employment retirement plan.

It's just like between this, that and the other thing, and not to mention environmental regulations that we have gone through in our lives with the property rights struggles, as Congressman Tate mentioned, we are being squeezed every which way but loose in our personal lives, with our property. It's enough to make one cry uncle. Needless to say, after we left that convention with our spirits deflated thinking how are we ever going to be able to comply with these requirements and still make a profit, let alone stay in business, it's just mind-boggling.

I'd like to take a minute to talk about minimum wage, since this seems to be the current issue on the table as well.

Assuming we're able to tackle the regulatory hurdles and do manage to open a small bookstore, now we're being told that we must pay our employees at least 90 cents an hour more than we first planned should this new law pass.

When planning our store concept, we anticipated letting our employees keep all the tips from the espresso stand to supplement their minimum wage.

They would also more than likely be part-time workers going to college or possibly young mothers needing extra income.

The minimum wage bill Congress is contemplating would place undue hardships on people like us who have no way of knowing whether we'll be able to weather the economic storm sure to beset any new business.

And I'd like to make an aside comment on minimum wage. I haven't heard anybody while addressing this issue talk about employees that are on tips and commissions, and I think that's a very valid point.

If you're on minimum wage and you have a tendency to make good money on tips and commissions, you're probably going to make a lot more money than a lot of people that are at higher salary.

I know some shoe salesmen at Nordstroms that have been reported to make about $100,000 a year strictly on commissions. So I think this whole minimum wage thing really, really needs looking into in a more realistic light than I've seen so far.

Furthermore, I maintain that people like us will become the employers of the future. As more and more corporate people become castaways of the downsizing trends, we'll be here to pick up the slack.

If I'm able to hire one or two employees, maybe more, if successful and I eventually franchise my idea, my one or two employees could become hundreds.

For the sake of these employees of the future and small business people everywhere, I beg Congress to implement common sense regulatory reform.

We need all the help we can get just to get started. Don't make it more difficult than it already is by heaping scads of overlapping regulations on top of each other day in and day out.

I could cite numerous horror stories other business owners have relayed, but time does not permit hearing them all.

In closing, I want to thank you for listening. I don't know at this point what new business, if any, we will be entering into in the future.

I would like to think that the Government is here to assist me in providing the best business I can be to the community.

However, when I hear that phrase, "I'm from the government, and I'm here to help you," I'm tempted to run for the hills. Hopefully, you can make it better. Thank you so much.

[The prepared statement of Mrs. Moody follows:]

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

TESTIMONY OF JUDI MOODY
MAY 16, 1996

Greetings: Thank you very much for the opportunity to speak before you today about my concerns on governmental regulation and its effect on small business. My husband and I own a small manufacturers representative business in Washington state. We have no employees, but work with contractual sales people who assist us in selling our products. Given recent changes in the retail and wholesale market place, we feel that our time is limited in the business we are currently in. As manufacturers and retailers' profits are squeezed, we are the classic "middlemen" who are most at risk of being phased out of the economic spectrum. Like the fabled "Willy Loman" in Death of a Salesman, my husband who is in his early 50's feels that he has nowhere in the corporate structure to go to start over.

In that regard, being the entrepreneurs we have always been, we have recently begun seeking out new business opportunities. We hit upon an idea which we thought would be relatively simple--opening a paperback recycling book store and serving espresso coffee and snacks. Well, we went to a food show at our local convention center and had a wonderful time sampling all the goodies and researching opportunities. At last we came to the State of Washington's Labor and Industries table, whereby we learned that before we even secured a location and opened the door, we would be besieged by book after book and form after form of regulations--everything from needing to provide industrial insurance for employees, chemical hazards awareness forms, general educational, medical and first aid requirements, personal protective equipment requirements, and so on--all of this for the possibility of hiring one, maybe two employees to sell books and pour coffee! It seemed that we would need a lawyer before we even opened the door.

I realize that I am am speaking about State regulations here. But the very thought of dealing with so many layers of overlapping bureaucracy--State, County (as in health department), city--who knows what each city requires?--and finally federal - tax reporting, both quarterly and yearly, pension plans (we have a Keogh plan now and must cover any new employee we may hire), etc. is enough to make us cry UNCLE!!

Needless to say, we left that convention, spirits deflated, thinking how are we ever going to be able to comply with all these requirements and still make a profit, let alone stay in business? Now I'd like to take a moment to discuss the minimum wage issue that has been gathering so much steam lately. Assuming we are able to tackle the regulatory hurdles and do manage to open a small bookstore, now we are being told we must pay our employee/s at least 90 cents an hour more than we first planned, should this new law pass. When planning our store concept, we anticipated letting our employee/s keep all the tips from the espresso stand to supplement their minimum wage. They would also more than likely be part-time workers, going to college or possibly young mothers needing extra income. The minimum wage bill Congress is contemplating would place undue hardships on people like us who have no way of knowing whether we will be able to weather the economic storms sure to beset any new business.

Furthermore, I maintain that people like us will become the employers of the future. As more and more corporate people become castaways of the downsizing trends, we will be here to pick up the slack. If I'm able to hire one or two employees, maybe more if successful, and I eventually franchise my idea, my one or two employees could become hundreds. For the sake of these employees of the future and small business people everywhere, I beg Congress to implement common sense regulatory reform. We need all the help we can get just to get started. Don't make it more difficult than it already is by heaping scads of overlapping regulations on top of each other day in and day out. I could cite numerous horror stories other business owners have relayed, but time does not permit hearing them all.

In closing, I want to thank you for listening. I don't know at this point what new business if any we will be entering into in the future. I would like to think that the government is here to assist me in providing the best business I can be to the community. However, when I hear that phrase: "I'm from the government and I'm here to help you, I'm tempted to run for the hills"! Hopefully you can make it better!

Many thanks,

JUDI MOODY

Mr. GUTKNECHT. Mrs. Moody, I'm not sure we can make it better, but we'd at least like to not make it any worse, and that's part of what this committee is doing.

Our crack staff has prepared just for your benefit, you probably already know this, but for the benefit of everyone else, these are all the Federal regulations and forms that a new business has to comply with.

So when you say those magic words, "We're from the Federal Government. We're here to help you," this is some of the help that you get when you decide that you want to go out and start a new business in the United States of America.

Mr. TATE. Mr. Chairman, has the committee staff weighed that?

Mr. GUTKNECHT. No, but we should. That's a good point, Representative Tate. Mrs. Moody, the bells and whistles that you heard going on were to announce that we have a series of votes.

So most of us, we're going to have to go over to the House floor and vote. Representative Tate, did you have any other questions or comments you wanted to make at this time?

And then I think what I will do is we will recess the committee until about 10 minutes after 11. It would be my hope that we will have a 15-minute vote and a 5-minute vote and could be back here to reconvene about 10 minutes after 11.

And all of us do want to hear all of the testimony you have, but I think that's what we'll do. We'll go into recess now. We'll get back here as soon as we can.

It would be my hope to reconvene at 10 minutes after 11. Thank you.

[Recess.]

Mr. GUTKNECHT. I call the meeting back to order. We apologize for the inconvenience to the people here to testify and our guests.

I'm going to now yield to my colleague from Arizona, Mr. Shadegg, for the purposes of an introduction.

Mr. SHADEGG. Thank you, Mr. Chairman. I reserved any opening remarks, but let me make some now. The gentleman I want to introduce is, kind of, the average American story, born and raised in northern California, served in the military with the U.S. Coast Guard, graduated from St. Mary's College, spent a period of time in his life working for several large corporations, including General Electric, Honeywell and IT&T.

Now he and his wife, Charlotte, manage Maroney's Cleaners in Phoenix, AZ. But the story he is going to tell is a story which I think often gets lost here.

There is, of course, the rhetoric which surrounds this city, this rhetoric which we hear on the floor, the President talking about people endangering the environment or people endangering the safety of workers by what we have tried to do.

Yet I think those remarks seriously demean the real discussion which needs to go on. No one, absolutely no one wants to promote or advance dirty air or dirty water.

My State, Arizona, is a pristine State. It's a State in the West settled late in the history of this country with an environment which we all care about preserving.

The natural resources laws which we have passed, the environmental laws which we have passed are indeed well-intentioned.

But as we have already heard from the two witnesses who have spoken to date in this hearing, those well-intended laws often have unintended consequences which do grave damage.

It struck me listening to the people who have already spoken today, that we've lost our sense of history, that we formed this Nation to escape an all-powerful king, a central monarch that exercised all authority and that presumed to know what was good for everyone.

We went forward as a Nation with the idea that the genius was not that America could create the best bureaucracy in the world but rather that individual initiative and freedom and allowing people to make choices in their own lives and decentralizing power would make America great.

It, kind of, shocks me we have now come back to where each of the witnesses here before us has talked about the fact that we have so created today such centralized power and authority. It's much like the monarchy we tried to escape and that the Founding Fathers were concerned about not recreating.

Dick Walton and his wife Charlotte, as I indicated, operate one of the dry-cleaning establishments in Phoenix. It's one of the, I think, medium-size to large dry-cleaning establishments in Phoenix, and his story is a story of not a businessman who wants to rape and plunder his employees or the environment or the health and safety of the people of our community but rather someone who simply wants to run a business and who is concerned that the regulatory mechanism we have created is literally out of control and doing real damage.

I think you will appreciate his testimony. I seriously wish that more Americans could hear it, because when we polarize the debate, I think we do damage.

This is a story about well-intended laws gone awry and about the inability of us as a Nation to cope with that and simply return to balance without it being politicized and somebody saying, no, the other side wants to destroy all of the protections which the regulatory structure is intended to create.

I appreciate very much Dick Walton traveling here from Phoenix, AZ, to tell this story. Dick, thank you very much for coming. I know this takes time out of your business out of what you got to be doing to earn a living.

But we very much appreciate your coming forward, because inside the beltway, we don't hear messages like this often enough.

Mr. WALTON. Well, I certainly appreciate your giving me the opportunity to come here. I'm honored to be here. Actually, I'm delighted to be here. I think it's a wonderful city.

I wish that my wife Charlotte could be here, too. Regrettably, she has to stay behind and run the business. In the 24 hours since I've been gone, the compressor has burnt up, the manager from the plant that she is managing has found out his father has died, and he will be gone tonight through the weekend and through Monday.

One of the key employees I hired to substitute for route relief drivers has decided to quit. The essence of small businesses is that they're small. There just aren't that many people there.

Before I get into my testimony, I want to say thank you to Chairman McIntosh and to Congressman Shadegg for this opportunity.

Like Congressman Shadegg said, my name is Richard Walton, although I'm comfortable with Dick. I, along with Charlotte, operate Maroney's Cleaners and Laundry in Phoenix, AZ. Maroney's is an 85-year-old family laundry business. Founded in 1911, Maroney's became a business before Arizona became a State.

Today, Maroney's operates out of two plants, both in Phoenix, with its 10 fleet trucks, seven route drivers and drive-through locations. It provides service to Phoenix, Scottsdale, Mesa and Tempe.

Naturally, as a business, Maroney's has to comply with a great number of Federal, State and local regulations. Payroll generation alone requires compliance with IRS, Arizona Department of Revenue requirements.

We pay an outside service $120 a week for payroll, $9 a week for tax service. An outside service is also employed to help with unemployment claims and U.S. labor laws like sexual harassment. The cost for this service is $2,652 a year.

Laws affecting hiring practices like EEOC rulings, Immigration and Naturalization Department policies necessitate periodic reviews and possible reprinting of employee applications, manuals and other internal company documents.

The act of hiring new employees, verifying IDs, making copies and filling out I–9 forms requires a half hour per new hire. Maroney's must now become expert at recognizing illegal aliens and detecting counterfeit documents.

We now are the Border Patrol. We have to stop the hiring of illegal immigrants. You know, my feeling on that is if the Government doesn't want us to hire them, don't let them in the country.

OSHA reporting, filing First Report of Injury, Form 200, requires approximately 2 hours per injury. OSHA requirements for a safe workplace sometimes cost more than necessary because Maroney's doesn't own any buildings.

Landlords reluctant to make costly repairs wait too long causing a chain reaction of repairs. OSHA also requires us to buy gloves, masks, eye wash stations.

State and local requirements have added costs for backflow prevention devices, annual inspections fees, alarm subscriber permit fees, alarm penalty fees.

The Clean Air Act as administered by the State has added reporting requirements and annual permit fees. And of course, thousands of dollars are spent each year to send off hazardous waste.

I brought some exhibits here today, one of which is how I comply with the Clean Air Act. I nailed the regulations to my wall for each of the stores along with the permits and other forms that I have to fill out. It's the only way I can follow the paper trail.

By far, however, the regulations that have hurt us the most are the environmental ones. These well-intentioned laws have unintentionally harmed innocent people, drained off personal savings, denied companies like Maroney's the future benefit of retained earnings.

Maroney's, like other innocent parties, is on the path to financial ruin trying to defend itself against unjust liability provisions inherent in Superfund.

Like many of the Nation's 30,000 dry-cleaners, Maroney's is at risk for the use of perchlorethlyne, the primary cleaning solvent used by most dry-cleaners.

Whenever perch is discovered, dry-cleaners are blamed. I'd like to explain now how some of these events unfold and stunt our economic growth. Perhaps, too, we can explore how some of this Nation's glory is lost when we create and condone those unjust laws.

The Maroney's story begins in 1989. As I told you, we have two stores, one in central Phoenix and one in east Phoenix.

The east Phoenix store in 1989 came under inspection because of discovery of perchlorethlyne in water wells in a 6 square mile area.

The site was tested October 4, 1989, by Earth Technology Corp. for the Arizona Department of Environmental Quality as part of an investigation of the east central area. The laws in Arizona that resemble Superfund are called WQARF, Water Quality Assurance Revolving Fund. They have all of the heinous liability provisions that Superfund has.

Our potential liability at that time was unknown. Because 100 jobs were at stake, I spent the better part of the day watching those tests.

I knew that the employees inside that building were at risk. I knew that building had been there 30-some years. I waited months to find out what the conclusions were of those tests. I watched the oscilloscope. It doesn't mean too much to me. Then, they made the 18-foot test.

I asked them if they had inspected other dry-cleaners that day, and they said yes. I said, "Did you find anything?" "Yes, 3,000 parts per million." And I said, "Well, do you use the same tube? If you're going to sniff the air underground—" "Well, change the tube," they said.

They sent the probe down, and I watched the oscilloscope again. They changed the tube, and they made the test again. I can still hear the sound of the inspector's voice ringing in my years. "You've got mighty clean dirt down there, Mr. Walton." And I said, "Why is that?" He said, "Well, it's reading 2.8 parts per million, and the background air is three parts per million."

That was half the test. The other test was a core sample, which they would do under microscope. For some reason, I wasn't allowed in the mobile lab to see what those tests were, but I waited months to find out what the conclusions were of those tests.

Essentially, the State came back and said in a roundabout way that the parts per million averaged, like, about 15. I couldn't quite figure how they got that, since I'd seen the oscilloscope read 2.8. But 15 appeared to be the threshold for further investigation, and I didn't hear anything more. Many of my competitors in that 6-quarter-mile area have been under the gun for how many years now, 7 years.

To some degree, I was relieved to think that the man that had operated that site for 30-some years had maybe not fouled his nest.

But in 1992, my wife was notified—I always thought we owned two businesses. She was notified about a site in west Phoenix that, apparently, the Maroney's Corp. had owned 23 years ago. And apparently, our name on a deed was enough to involve us in a larger contaminated site. This was a site of 25 square miles with 200 possible responsible parties.

The lawyer, Jim Barick was his name, was quite adamant that Maroney's certainly must have done something there. I don't know what, because the same manager that operated the site that I just described the testing on also founded that business.

Maroney's sold that business 17 years ago. They only operated it for 6 years. To my understanding, it was a state-of-the-art business.

My wife Charlotte and her father were in the equipment sales business. They sold laundry and dry-cleaning machinery, and their partner, who was an active partner—they were silent—was able to buy the best equipment possible.

So I doubt very much that that site could have contributed to the 25-square-mile aquifer contamination. It's very difficult for dry-cleaners to contaminate because all of their solvent is contained within steel tanks within machines. Even though the machine is very similar to a home washer, unlike a home washer, you do not pull a plug and drain solvent to the sewer. You recycle it through a distillation process, and you reclaim it and you reuse it. Our industry, however, thinks that over time perhaps the disposal of wastewater, which is a byproduct of the humidity that is in clothes that comes out of the distillation process, that is separated in the separator—perch, by the way, is quite heavier than water.

It's 13½ pounds per gallon, as opposed to 8 for water. So it sinks to the bottom of water containers, and we have a device on the machine that's very similar to a turkey grease and juice separator in home cooking. One chemical is at one level, and the other is at another level. So we separate the two very often.

Over the years, dry-cleaners have put that water down the sewer. We've now learned that sewer systems leak, that sewer systems are not seamless tubes. They're segmented sections of jointed pieces, and they do, in fact, leak. And it's believed that maybe over time the trace amounts of solvent have accumulated in these joints and leaked into underground aquifers.

The other possibility is that filters that were taken out of dry-cleaning machines and thrown in dumpsters, and dumpsters may have leaked. So some sites have gotten contamination that way.

The upshot of this is that you lose your constitutional rights in this sort of engagement. EPA doesn't have to take you to court and doesn't have to find you guilty.

The liability provisions of SERCLA and WQARF allow them to assess you fines. We did the prudent thing. We hired an attorney. Our only defense was that I don't think we did anything wrong.

When I came back here in 1993 to lobby Congress, we had spent $60,000 trying to say I don't think we did anything wrong. Today, we have spent over $200,000.

As you can well imagine, in a small company, $200,000 would go a long way toward replacing equipment, paying additional wages. It would buy us a building. It would replace our 10 fleet trucks, which cost about $25,000 apiece today.

The man, Jim Barick, who was the opposing attorney in this case, turns out to be the author of the Arizona WQARF legislation. Jim Barick has since renounced his position on that and has joined with me and other victims to create legislation in Arizona that repeals some of these liability provisions.

I'd like to give you a sense of the feeling that we have going through this. I know that all of these stories are important, and if I just relay the facts to you, I don't think you'd go away with an understanding today of how grave these issues are.

My kids don't want to go in business. My kids are afraid to inherit the business. My kids are afraid that we'll die, and they'll be responsible for it.

I want to say if future generations don't want to become entrepreneurs, where will the entrepreneurs of tomorrow come from, and where will young people go to work? Government?

How many jobs can Government create? Do people have to go to law school to go into business today? I don't know what the end to this problem is. It has some ugly facets to it.

I don't know how you clean up a 25-square-mile contaminated area. To me, it's like Lake Michigan with a straw. First of all, you can't touch it. The solvents that we have would go to the bottom.

Second, there is over 200 possible responsible parties in that area. There are some big players like Reynolds Metals, Van Waters and Rogers brought in solvent by the train car load. There is casting firms, even the county.

There is also some other sad aspects. The $200,000 that we spent on our attorney, of course, has just gone for attorneys fees. Nothing has been cleaned up, and in most cases, nothing ever will be.

I don't know how much it costs to clean up an area that big. $100 million? Who knows? But today our attorney is being approached by the county, and they're asking him to come to work for them.

To me, this seems like an unethical situation, and I feel for my wife, who has suffered the brunt of this. Like I say, I don't know what the end is.

When I look out the front door of my central location, this is what I see. It's an 11-story building. Underneath the 11-story building is five layers of underground parking. These people, apparently, are suffering contamination from underground petroleum storage tanks and have spent over $1 million trying to pump water.

Before I came here, 2 weeks ago they sent us a letter threatening us with suit. Co-mingled with that petroleum are trace amounts of perchlorethlyne.

So we are about to go under the knife again, and I don't know how much a small business can pay for a defense. Somehow, some way we need some kind of regulatory relief that recognizes the people's right to survive.

I don't think pollution is anything new. I think it has probably been with us since prehistoric times. Surely, somebody brought home an egg with poop on it, and it was thrown out of the cave. Surely, somebody urinated too close to the water supply was warned.

The point is I think that many rational people know what to do. They clean up, and they go on. But with today's Government, there seems to be some desire to kill you.

It's not enough to somehow work out a solution that allows you to survive. They somehow have to squash you. I guess why I'm here is to try and defend the 100 jobs that have been in existence for almost 85 years.

[The prepared statement of Mr. Walton follows:]

I am honored to be here today and grateful for the attention given to my testimony. I want to thank Chairman McIntosh and Congressman Shadegg for this opportunity.

My name is Richard Walton (I am comfortable with the name "Dick").

I along with my wife Charlotte operate Maroney's Cleaners & Laundry in Phoenix, Arizona.
- Regrettably she cannot be here today.

Maroney's is an 85 year old family laundry business. Founded in 1911, Maroney's became a business before Arizona became a state.

Today, Maroney's operates out of two plants, both in Phoenix. With its 10 fleet trucks, 7 route drivers and convenient drive-thru locations it provides service to the Phoenix area, Scottsdale, Mesa and Tempe.

Naturally as a business, Maroney's has to comply with a great number of Federal, State and local regulations.

Payroll generation alone requires compliance with I.R.S. and Arizona Department of Revenue requirements. We pay an outside service $120. per week for this service ($9.00/wk for Tax Service)

Other Employee Costs are:
F.I.C.A. @ 7.65% of Gross Wages
S.U.I. @ .51% of first $7,000 of each employee's wages.
F.U.T.A. @ .80%
Workers Compensation Insurance - $2.82/$100 for each employee.

An outside service is also employed to help with unemployment claims and U.S. Labor Laws like Sexual Harassment. The cost for this service is $2,652/year.

Laws affecting hiring practices, like E.E.O.C. rulings, Immigration & Naturalization Department policies necessitate periodic review and possible re-printing of Employment Applications, Manuals and other internal company documents.

The act of hiring new employees, verifying i.d.'s making copies and filling out

I-9 forms require 1/2 hour per new hire. Maroney's must now become expert at recognizing illegal aliens and detecting counterfeit documents.

O.S.H.A. Reporting - Filing First Report of Injury/Form #200 requires approximately 2 hrs. per injury.

O.S.H.A. requirements for a safe workplace sometimes cost more than necessary because Maroney's doesn't own any buildings. Landlords, reluctant to make costly repairs wait too long, causing a chain reaction of repairs. O.S.H.A. also requires gloves, masks and eye wash stations.

State and Local requirements have added costs for Backflow Prevention Devices, Annual Inspections fees, Alarm Subscriber Permit Fees and Alarm Penalty Fees.

The Clean Air Act as administered by the State has added reporting requirements and annual permit fees. And of course thousands of dollars are spent each year to send off Hazardous Waste.

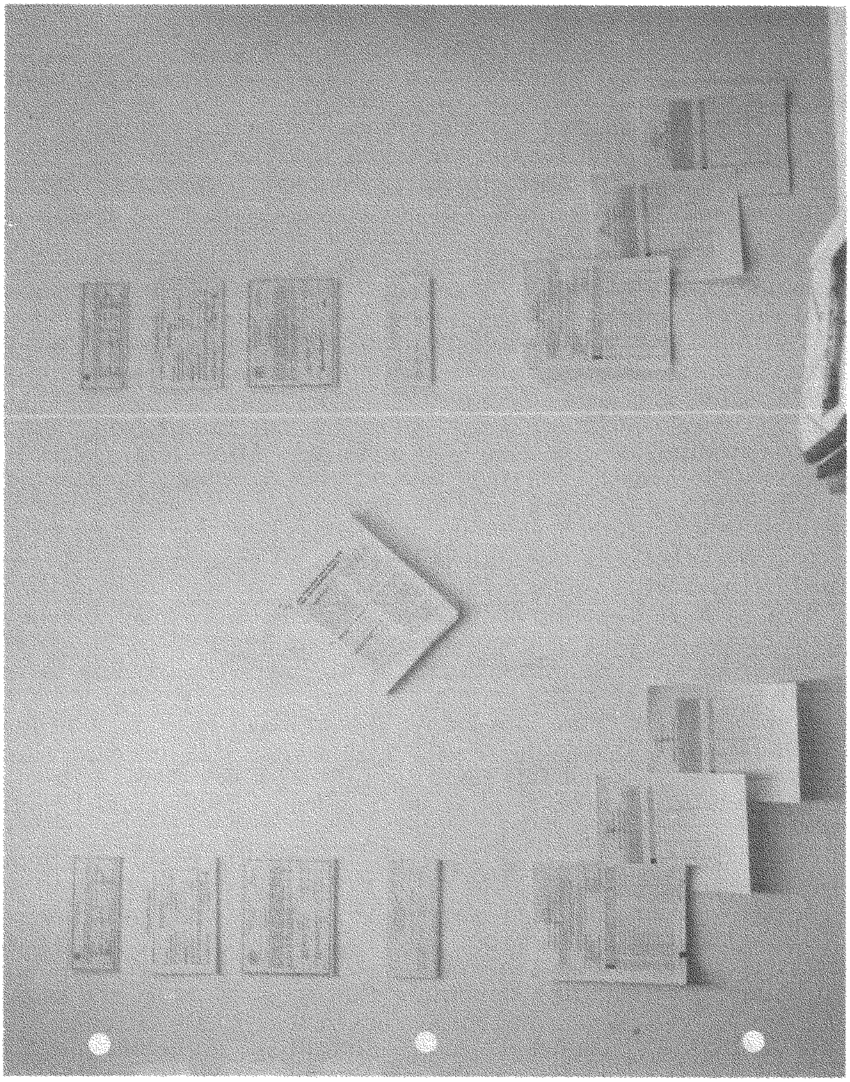
By far however the regulations that have hurt the most are the environmental ones. These well intentioned laws have unintentionally harmed innocent people, drained off personal savings, denied companies like Maroney's the future benefit of retained earnings.

Maroney's like other innocent parties is on the path to financial ruin trying to defend itself against unjust liability provisions inherent in Superfund, C.E.R.C.L.A. and W.Q.A.R.F.

Like many of the nations 30,000 dry cleaners Maroney's is at risk for the use of perchlorethlyne, the primary cleaning solvent used by most dry cleaners. Whenever perc is discovered dry cleaners are blamed.

I'd like to explain how some of these events unfold and stunt our economic growth. Perhaps too, we can explore how some of this nations glory is lost when we create and condone these unjust laws.

In conclusion I would pray for this committee's consideration for regulatory reform.



Mr. GUTKNECHT. We want to thank you for your testimony. If you want to summarize, we do want to try and keep as close to the 5-minute rule as we can.

Mr. WALTON. I recognize that all these stories are important, and in the 3 years I've been involved with this, there are just thousands of cases like this.

I just wanted to give you a sense for the feeling of what it is to go through this and for the uncertainty of the future and how it affects our country. And I certainly appreciate the opportunity to express those feelings.

Mr. GUTKNECHT. Well, Mr. Walton, I don't suspect this makes you feel all that much better, but we have been having field hearings and hearings here in Washington for now a year and a half, and you are not alone.

You represent the views of an awful lot of small business people who, as Ross Perot said, feel like the Government is coming at them rather than coming from them.

I do want to acknowledge at this time the ranking member of this subcommittee, a colleague of mine from Minnesota, Collin Peterson. Congressman Peterson, do you have an opening statement?

Mr. PETERSON. Thank you, Mr. Chairman. I appreciate you all having this hearing. I have got a dry-cleaners in my district that has given me the same kind of stories and testimony. So I sympathize with what you're up against.

I really have been one of those on this side of the aisle that have been trying to help to undo some of these regulations and bring some sense to them. Unfortunately, we haven't been able to get much moving over in the Senate.

I apologize for being late today. The problem is that I had four committee meetings going on at the same time this morning, three of which are all out of this same committee, which seems to me we could do a little better job of scheduling some of this stuff, I would hope.

I'm going to have to go back to the hearing on the National Cheese Exchange, which is going on in the Agriculture Committee.

I just want to note that it's somewhat ironic that we're having these coinciding hearings, one of which is trying to alleviate Government regulation, and this other one that I'm going to the majority is trying to regulate something that most of us on the Democratic side think is working pretty well in the private sector.

So I think it's somewhat ironic that we have another committee going on where the Democrats are defending the free enterprise system, and the Republicans are trying to regulate it and screw it up.

I don't know exactly what all that means, but we have a very simple situation where the National Cheese Exchange, it operates so efficiently and so simply that they're in trouble.

It costs $600 a year to belong to this exchange. They sell carloads of cheese. The buyer pays $50. The seller pays $50. They meet a half an hour every Friday, and they're trying to do away with it and set up a Government system whereby we'll spend millions of dollars trying to get the Government to figure out what the price of cheese is rather than this simple exchange in Green Bay, WI.

So I have to go back over there and participate in that. Mr. Gutknecht and Mr. McIntosh, I would implore you to go over to talk to your colleagues in the Agriculture Committee and get them to rein in some of what they're doing over there.

So I thank you for holding this hearing. I will continue to work with you to try to eliminate some of these regulations and apologize for not being able to be with you the rest of the hearing.

Mr. GUTKNECHT. Thank you, Congressman Peterson, and I think it demonstrates that the temptation to regulate is not a singularly partisan issue. Some of our folks want to do that as well.

I also want to welcome Congresswoman Slaughter to the hearing. Do you have an opening statement that you'd like to share?

Ms. SLAUGHTER. I don't. Thank you, Mr. Chairman. You know this committee is having two subcommittee hearings at the same time. So I'm just going to try to bounce from one to the other the best I can. Thank you.

Mr. GUTKNECHT. Thank you. I would now like to welcome Mr. James Jackson, who operates four Amoco stations in the Washington, DC, and Maryland area. Welcome, Mr. Jackson.

Mr. JACKSON. Good afternoon, Mr. Chairman, and good afternoon to the members of the committee also. My name is James Jackson, and I'm president of the WMDA Service Station and Automotive Repair Association and the owner of four Amoco stations in Washington, DC.

Our association represents 1,500 service station dealers and automotive repair owners in Maryland, Delaware, and Washington, DC. I am also my association's delegate to the Service Station Dealers of America.

To get right to the point, regulations directly affect decisions I make in the area of employment. When I cannot pass the costs of these regulations to the consumer, I look at my staff and see where I can cut back on employee hours. And when the times are really tough, I decide if I can afford an employee at all.

Another consideration, when dealing with regulations, is the time I have to spend filling out forms and dealing with regulators on the phone. Let's look at the various industry fees that my service station pays.

In addition to their costs, please keep in mind that the compliance of these regulations take a lot of time, time I could spend training employees or pitching in at the cash register or working the pumps during the busy times, and yes, time I could use spending with my family.

Now, I know that we need regulations. We need them because we have to have standards that businesses must meet so we can have clear air and water.

I was delighted when my daughter took a job with Prince George's County, our neighboring county in Maryland, the County Department of Environmental Regulatory Affairs, because I know she would have to serve the public, and she enjoys doing that.

But we need to have smart regulations that work. Let me give you an example of what I am talking about. In the District, there are some people that inspect pumps, meters and underground storage tanks.

Instead of three groups of people, three agencies showing up at different times, one group does it all. I know them, and I trust them.

The DC government made sure that we could do that with one person and eliminate having several different people come in doing several different jobs, and that's time I can also spend by doing that, more time with my employees and training.

If this is a government of the people, it should do more things like that. Now, let's look at what I spend on regulations with employees in a year.

I have 18 full-time employees and about eight part-time, which mostly work part-time weekends, work various different jobs, just working weekends filling out for some extra income. Of course, these numbers change from time to time, but it's a pretty good indication of what an employee costs at my station.

I have it broken down that Workmen's Comp costs about $1,000. Unemployment insurance is about—this is per month. Unemployment insurance is about $450.

The UST nozzle and pump inspection is about $525, and tire fee is about $800 a year. Water and sewage is up about $1,000. Tank registration is about $4,000 per year.

That $4,000 is $1,000 per tank that we have to pay just to register the tanks, that still has to be inspected by the Government just only to sell gasoline. And on top of that, we have sales tax. That comes to over $30,000 for a year in fees and inspections, about $2,000 per employee per year. Taking into account the hours worked by part-time employees, I spend about $2,000 per full-time employee. Let's look at what the dealer pays, the money that goes out on our profit on a gallon of gasoline, regular unleaded gasoline.

We have a DC fuel tax which is 20 cents per gallon. We have the Federal tax which is 18.3 per gallon. We got a credit card fee. The credit card fee that I pay per month on any Government transaction that comes into my station is 3 cents per dollar to fuel a Government vehicle or any noncompany credit card that's used. I have to pay a fee for using that credit card.

I have to pay increased rents, and the rent is increased due to the Stage 2 updates. If I have to have new pumps put in or new hoses and underground storage and that kind of stuff and it's done on my location, then my rent goes up accordingly and spread out over 20 years to pay for that update, let alone the update that the company wants on their investment. So each year I look for a rent increase regardless whether I make any money or not.

OK. Out of that I still have to pay payroll. I have to pay my rent—this is what I just spoke about—insurance and utilities.

As you can see, the dealers are not benefiting from the current price increases. Our profit margins are lower than they have been in some time.

And it is important to remember that while the oil companies have to absorb these taxes and regulations, too, dealers are the ones who face the consumer on a daily basis.

Therefore, the market will only allow us to make so much profit on a gallon of gasoline. So please remember that with the fuel tax and other environmental regulations, with small businesses like ours, it's not long before the cost of doing business is so great that we have to lay off people and, in some cases, we have to close our doors permanently. Thank you for the opportunity to speak.

[The prepared statement of Mr. Jackson follows:]

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May 16, 1996

Testimony of James Jackson, President of the WMDA Service Station and Automotive Repair Association

Committee on Government Reform and Oversight

Subcommittee on National Economic Growth, Natural Resources and Regulatory Affairs

EFFECT OF REGULATIONS ON EMPLOYMENT

Good afternoon Chairman McIntosh and members of the Committee. My name is James Jackson and I am President of the WMDA Service Station and Automotive Repair Association and the owner of three AMOCO stations in Washington, D.C. Our Association represents 1500 service station dealers and repair shop owners in Maryland, Delaware and Washington, D.C. I am also my Association's delegate to the Service Station Dealers of America.

To get right to the point, regulations directly affect decisions I make in the area of employment. When I cannot pass the cost of these regulations on to the consumer, I look at my staff and see if I can cut back on employee hours, or when times are really tough, I must decide if I can afford them at all.

Another consideration when dealing with regulations is the time I have to spend filling out forms and dealing with regulators on the phone. I have provided a list of the various industry fees a typical Maryland service station pays. In addition to their costs, please keep in mind that compliance for these regulations takes a lot of time. Time I could spend training employees, or pitching in at the register or pumps during busy time. And yes, time I could be spending with my family.

Now, I know we need regulations. We need them because we have to have standards that businesses must meet so that we have clean air and water. I was delighted when my daughter took a job with the Prince George's County Department of Environmental Resources because I knew she would serve the public. But we need smart regulations that work. Let me give you an example of what I am talking about. In the District, the same folks inspect fuels, pump meters, and underground storage tanks. Instead of three groups of people from three agencies showing up at different times, one group does it all. I know them and trust them. The D.C. government made sure they could do not do one, but several jobs, just as I do with my employees. The District and all other governments should do this a lot more.

Now let's look at what I spend on regulations for an employee in a year. I have _______ full time employees and _______employees.* Of course these numbers change from time to time, but this is a pretty good indication of what employees cost at my stations.

WORKERS COMPENSATION
UNEMPLOYMENT INSURANCE
UST/PUMP METER/FUEL INSP.
TIRE FEE
ARENA FEE (FORMERLY PUBLIC SAFETY FEE)
USED OIL
1998 EPA UST UPGRADE
WATER/SEWAGE
OTHER LICENSES
SALES TAX

Taking into account the hours worked by part time employees, I spend ________________________ per full time employee.

Now let's look at where the dealers' money goes for a gallon of regular unleaded gas.

RACK PRICE (less tax)
TAX/REGULATIONS:
D.C. FUEL TAX 20.00
Federal Fuel Tax 18.3
Environmental Costs_______
TOTAL _______________

As you can see, dealers are not benefitting from the current price increases. Our profit margins are lower than they have been in some time. And it is important to remember that while the oil companies have to absorb these taxes and regulations too, dealers are the ones who face the consumer on a daily basis. Therefore, the market will only allow us to make so much from a gallon of gas.

So please remember that whether its fuel taxes or other environmental regulations, with small businesses like ours it's not long before the cost is so great that we have to lay people off.

Mr. GUTKNECHT. Thank you, Mr. Jackson. Now we're going to turn to Mr. Alexander. Tom Alexander is the owner of T.J. Alexander & Sons. Can you tell us a little bit about your story?

Mr. ALEXANDER. Yes, sir. Thank you, Mr. Chairman, and members of the subcommittee. My name is Tom Alexander. It's J.T. Alexander & Sons, Inc. It's a small, independently owned petroleum marketing company in Mooresville, NC.

We come from a very small rural community in Piedmont, NC. We started the business, my dad did, in 1935. I joined him in 1961. We have about 36 employees, from truck drivers to transport drivers to members who work in convenience stores, to clerks who work in the office.

In addition, our company serves about 150 fuel oil customers in our area. However, we have two companies that we sell to that serve some 900 customers in rural North Carolina.

A lot of these are farmers. A lot of them are senior citizens who still live in rural America, who burn kerosene and fuel oil in their heaters.

By the way, this past winter was extremely cold, even in North Carolina, and we had to have a lot of supply available for these people.

We're at about a 75-mile radius around our area that we serve. The largest city is my home town of about 30,000 people. I'm here today testifying not only on the behalf of my company but on behalf of Petroleum Marketers Association of America, known as PMAA, and the National Association of Texaco Wholesalers.

To put it simply, Government regulations are the bane of my existence as a small business person. In a recent survey done by PMAA of over 800 marketers who responded, Government regulations have been the biggest obstacle in our growth and success over the past 10 years.

Excessive Government regulations cost jobs and raise consumer prices. I know that as a small business person, in my business, more and more I have to make decisions on whether or not I will open or close an outlet based upon Government regulations. These decisions mean fewer jobs and less compensation in the marketplace.

For instance, as my colleague to the right said, we pay over 41 cent per gallon in Federal and State taxes on each gallon of gasoline that's sold.

This costs us about 5 cents a gallon just for regulations that we have to pay on all the gasoline that we sell.

Many locations that we're very concerned about have closed in the rural area of our State, basically, because they could not meet the regulations of the underground storage tanks, when it costs about $25,000 to up grade a tank and you're not selling the quantity of gasoline to even break even over a 6-year period.

So we have a number of locations that have closed. This, in turn, loses business in our area, and it causes unemployment.

Nowhere has the impact of governmental regulations been felt greater than in recent developments of petroleum product market.

As a retailer of motor fuel, everyone wants to know why has gasoline and diesel fuel prices gone up so much. So to say the least, we're the guys wearing the black hat.

The wholesaler is looked at as the guy that causes this. We sell to retailers. The retailers come to us and want to know, "Why are you raising the price of gasoline?"

The price of gasoline is based upon a raise in price from the refiner and from the marketplace. There are many factors that have contributed to the price increases, and they've been well detailed.

One very significant contributor of price increase that has received very little attention, and that is the Government's role.

In just the last 3 years, Congress has mandated the use of three new fuels—one, diesel fuel that is dyed that goes into on-road, oxygenated fuels and reformulated gasoline.

These are just a few of the major new fuels. In addition, there are areas that require an RVP gasoline that has a low RVP rating.

Of course, then, there is California that has diesel and fuel and gasoline that's unique just to that State. Under normal circumstances, all these regulatory changes would have severely taxed the petroleum storage and distribution infrastructure, but these are not normal circumstances.

In addition, Federal regulations regarding above and below ground storage tanks are being implemented in tandem with these requirements for new fuels.

The effect of these regulations has discouraged the construction of new storage facilities and simultaneously encouraged the closing of others.

So at a time when additional storage capacity was needed to accommodate additional fuels mandated by Government regulations, other regulations were reducing the fuel storage available.

The historic brilliance of our country's petroleum supply and distribution system has been its flexibility. If there was a problem in one area, supply could be shifted.

But with these new fuels that have to be mandated by the Government, this flexibility no longer exists. The truth is that Government regulations have contributed significantly to the erosion of the petroleum marketing, storage and distribution infrastructure.

The margin for error is less than it has ever been before. It is inevitable that the price of gasoline will attract a lot of political attention.

When prices are low, everything is quiet as people accept the fact that the market works. However, when prices rise, it somehow signals that the market no longer works.

Of all the suggestions for the Government action to reduce prices, the only one to have any real affect would be the repeal of the 4.3 cents a gallon Federal excise tax, but that, too, has got a few problems.

As reported from the Ways and Means Committee, the tax repeal would not provide a refund for retailers like myself for gasoline that's in the storage tanks on the effective date of the repeal.

But what's even more inequitable is not providing a refund for floor stocks tax is that when the tax is reimposed on January 1997, these same retailers must pay a floor tax on the fuel in inventory at the end of the year.

How is it that the IRS can process my floor tax stock refund but can't figure a way out to tax me? I strongly urge that this problem be rectified before enactment.

Either we should get a refund and then pay the floor stock tax and then the excise tax is reinstated, or we should get no refund and pay no floor stock tax.

The only way to guarantee that tax repeal will be totally passed through is to impose some form of Government price controls. The Government imposed those controls in the 1970's, and the prices were much higher then than they are today.

Those who seek guarantees today would be the first to object if, when these taxes are increased, there was a mandate to pass them through.

One could look at what happened when the excise tax question was originally imposed and wonder whether it was ever passed through to customers. In 1993, the price fell 6 cents a gallon.

There is no way to tell whether the tax would go to the consumer because gasoline prices may increase. The marketplace will control exactly what happens.

So we don't know, whether the tax is repealed, whether it goes directly to the consumer or whether the price of gasoline in the marketplace will go up and down.

In conclusion, Mr. Chairman, Government involvement is largely to blame for the volatility of the petroleum markets today, but in terms of addressing this volatility, the less Government does the better we are.

As was stated, I also have three sons who are in my business. It's a very big concern of theirs about whether or not they should stay in the petroleum marketing business.

We have over 112 storage tanks underground. We have to spend a great deal of money every year. Somewhere in the neighborhood of $100,000 per year over the last 10 years was spent to meet regulations, to line tanks to bring it into regulations of the EPA mandates.

This comes up to around 4 to 5 cents per gallon of everything that we sell. So we ask you to certainly think about and to help us, as business people, that we might be able to survive in the marketplace and that we might be able to do a better job to create more jobs for people so that we have them working for us and that we might, in turn, be able to make a profit in our business. I thank you very much.

[The prepared statement of Mr. Alexander follows:]

Testimony of Mr. J.T. Alexander, Jr.
J.T. Alexander & Son, Inc.
Mooresville, N.C.
on behalf of the
Petroleum Marketers Association of America (PMAA) and
the National Association of Texaco Wholesalers (NATW)
Before the Subcommittee on National Economic Growth, Natural Resources and Regulatory Affairs
May 16, 1996

Thank you Mr. Chairman and members of the subcommittee. My name is Tommy (J.T.) Alexander, Jr. I am the President of J.T. Alexander and Son, Inc., a small, independent family owned petroleum distribution business in Mooresville, NC. My company has been in business since 1935 and has 36 employees. In addition, my company serves over 150 customers and 28 locations and the business spans a radius of 75 miles in primarily rural areas. I am testifying today on behalf of the Petroleum Marketers Association of America (PMAA) and the National Association of Texaco Wholesalers (NATW).

PMAA is a federation of 41 state and regional trade groups representing some 10,000 small, independent petroleum marketers. Collectively these 10,000 marketers sell half the gasoline, three quarters of the home heating oil and 60% of the home heating oil consumed in the U.S. annually.

NATW is a national organization representing 500 branded Texaco wholesalers and convenience store operators from 44 states. In addition, nearly 200 supplier associates, former Texaco wholesalers, and marketers of other branded and unbranded petroleum products are NATW members.

Mr. Chairman, to put it simply, government regulations are the bane of my existence as a small business person. And, if a recent survey done by PMAA is any indication, I am not alone. According to the 800 marketers who responded to that survey, government regulations have been the biggest obstacle to their growth and success over the last 10 years. Sadly, these same marketers predict that government regulations will remain their biggest obstacle over the next 10 years.

I hope the efforts of this subcommittee will prevent that prophecy from coming true.

Excessive government regulations cost jobs and raise consumer prices. Intuitively, I know that as a small business person and I bet it can be easily proven by an economist. Nowhere has the impact of government regulations been felt greater than in the recent developments in the petroleum products markets.

As a retailer of motor fuels, everyone wants to know why the price of gasoline and diesel fuel has gone up so much. My customers want to know; the media wants to know; and the government wants to know.

There are many factors that have contributed to the price increases and they have been well detailed. The one, very significant, contributor to the price increase that has received very little attention has been the government's role.

Over the past 10 years, Congress has enacted and EPA has enforced with great zeal, several environmental laws which are contradictory in terms of the way they apply to the petroleum industry. In just the last three years, Congress has mandated the use of three new fuels. On October 1, 1993, EPA required that all diesel fuel burned in on-highway vehicles be low-sulfur. In 1994, oxygenated fuels were mandated for many parts of the country. On January 1, 1995, several areas were required to have reformulated gasoline. To make these new fuels, refiners had to make great investments in their plants in order to comply with the new laws.

These are just the major new requirements. In addition, there were other areas that also required different types of fuel. Many areas required gasoline with a lower reid vapor pressure to meet Clean Air Act requirements. Some states increased the amount of oxygenate added to the fuel over and above that required by EPA; some states mandated which oxygenate had to be used to meet this requirement.

Some states decided to "opt-in" to the reformulated gasoline program, which EPA regulations allowed them to do. At the last minute, some of these same states decided to opt-out of the program, which EPA also allowed them to do leaving the industry to hold the bag. And then of course, there is California which has a diesel fuel and a gasoline that it is unique to that state.

Under normal circumstances, all of these regulatory changes would have severely taxed the petroleum storage and distribution infra-structure. But, these were not normal circumstances. In addition, federal regulations regarding both above and below ground storage tanks were being implemented in tandem with these requirements for new fuels. The effect of these regulations was to **discourage** the construction of new storage facilities, while simultaneously **encouraging** the closure of existing facilities.

So, at a time when additional storage capacity was needed to accommodate all the additional fuels mandated by government regulations, other regulations were reducing the level of fuel storage available.

These are not the only contributions the government has made to our current situation. The historic brilliance of our country's petroleum supply and distribution system has been its flexibility. In other words, if there was a problem in one area, supply could be shifted to another because gasoline was essentially fungible. If there was a problem with domestic supply, suppliers could acquire product on the world market and bring it to the U.S. This access to many sources of supply offered a buffer to dramatic price increases. If the price started to rise in a market, fuel from elsewhere would enter that market thus depressing the price.

With all the "boutique fuels" now mandated by the government, such flexibility no longer exists. This reduced flexibility brought on by government regulations has the effect of increasing price volatility in the market. The truth is that government regulations have contributed significantly to the erosion of the petroleum marketing storage and distribution infra-structure and the margin for error is less than it has ever been before.

Mr. Chairman, gasoline prices are, without a doubt, the most visible of all retail prices. We put our prices on huge signs in front of our stations and a mere glance allows the consumer to compare one price with another.

Because of this visibility, it is no wonder that gasoline prices also attract a lot of political attention. When prices are low, everything is quiet as people accept the fact that the market works. However, when prices rise, it somehow signals that the market no longer works. There are calls for investigations and the government feels compelled to act.

With regard to the current price hikes, we have the Justice Department spending taxpayer dollars investigating whether there is collusion or price fixing going on in the petroleum industry. This is at a time when no reputable economist or even the Secretary of Energy believes such illegal activity is occurring.

We have the President of the United States ordering the sale of 12 million barrels of crude oil out of the Strategic Petroleum Reserve (SPR) at a price approximately $7 per barrel less than what we paid when we put the oil in the reserve. It is important to understand that 12 million barrels is less than a day's supply to the U.S.

We have the Congressional leadership recommending that the 4.3 cents per gallon excise tax imposed on motor fuel on October 1, 1993 be temporarily repealed. Of all the suggestions, this would have the greatest impact on reducing the retail price of fuel, but it too is fraught with problems.

As reported from the House Ways and Means Committee, the tax repeal would not provide a refund to retailers like myself for gasoline that is in retail storage on the effective date of the repeal. This is in spite of the fact that we paid a floor stocks tax when the tax was imposed in 1993. IRS argues that it is too difficult for them to process refunds for all those retailers. The implications of this is that retailers will attempt to recover the taxes already paid on their inventory, thus delaying the point at which the consumer benefits from the repeal.

In many cases, particularly for smaller retailers, market forces may reduce the price well before they are able to reduce their inventory. In such an instance, the retailer faces the Hobson's choice of whether to reduce his price and remain competitive, thus not recovering the tax already paid; or not reducing the price, recovering the tax, but losing customers to a competitor.

But, what is more inequitable than not providing a refund for floor stocks tax is that when the tax is re-imposed on January 1, 1997, these same retailers must *pay* a floor stocks tax on fuel in inventory at the end of the year.

How is it that IRS can not process my floor stocks tax refund, but they can sure figure out a way to tax me? I strongly urge that this problem be rectified before enactment. Either we should get a refund and then pay a floor stocks tax when the excise tax is reinstated; or we should get no refund and pay no floor stocks tax on January 1.

The floor stocks tax is not the only problem with the excise tax repeal. Some legislators want an assurance that the repeal will be passed through to the consumer. With all due respect, it should be a requirement that before anyone is allowed to serve in Congress that they must take, and pass, a basic economics course. If so, we might not be faced with such suggestions.

The only way to guarantee that the tax repeal will be totally passed through is to impose some form of government price controls. The government imposed such price controls in the 1970's and if my memory serves me correctly, both the real price and the price adjusted for inflation was far greater then, than it is today.

Those who seek guarantees today would be the first to object if, when taxes are increased, there was a mandate to pass them through. One could look at what happened when the excise tax in question was originally imposed and wonder whether it was ever passed through to consumers. For example, in July 1993, three months before the tax was imposed, the national average retail price of fuel was $1.12 per gallon. By the end of September, that price dropped to $1.09. In early October, after the tax had been imposed, the price rose back to $1.12, less than the 4.3 cents per gallon assessment. By December, the price was back to $1.06 per gallon.

Taken as a six month time line, one could argue that the price of gasoline dropped 6 cents per gallon over a six month period during which a 4.3 cent per gallon tax was added. Does this mean the industry did not pass through the tax? Probably not. More than likely, it means that the price in December, 1993 and today is 4.3 cents per gallon higher than it would have been had there been no excise tax increase.

Similarly, if the tax is repealed the only thing one can safely predict is that whatever the price, it will be 4.3 cents per gallon less than what it would be had the tax remained in place. Consider my situation for a moment. When I get my invoice for a gasoline purchase, it is broken out by the price of the product and the excise tax. Once the tax is repealed, the excise tax portion of my invoice will show a reduction of 4.3 cents, but if the wholesale price of the fuel goes up six cents, it is unfair to expect me to lower my retail price.

The truth is that after the excise tax is repealed, no one can predict what the retail price will be because the tax is only one component of the price. The price could go down 8 cents per gallon; or it could go up by that amount. No participant in the market is able to make any guarantees because no one knows what the market will do. The one thing that is safe to say, however, is that whatever, the retail price, it will be 4.3 cents per gallon less than it would have been and the tax not been repealed.

In conclusion, Mr. Chairman, government involvement is largely to blame for the volatility in the petroleum markets today. But, in terms of addressing that volatility, the less the government does, the better.

Thank you and I will be happy to answer any questions you may have.

Mr. GUTKNECHT. Thank you, Mr. Alexander. Your comments concerning this whole rush to do something about gasoline prices reminded me of something that we said the other day at one of the hearings.

I really believe that markets are more powerful than mandates anyway. We've had proof. You reminded me of the 1970's what happened when we had wage and price controls.

Frankly, what has happened in the Eastern Bloc, the Soviet Union and the former Eastern Bloc where they tried to impose Government mandates on their economy, it was a 70-year experiment that failed.

We are going to try and stick to the 5-minute rule. I have a couple of questions, and then I'm going to yield to my colleague, Mr. Shadegg.

First of all, Mrs. Moody, I think your comments or your testimony was pretty powerful. Have we had this weighed yet? But I can report that we now have a number.

There are 39 different rules, regulations and mandates that you have to comply with, and that does not include the State and local mandates.

So starting a business in the United States of America is much more complicated today than it has ever been. I'm not sure how much we can reduce that, but that's one of the charges of this committee.

I would suspect that you think that there are an awful lot of people in the same situation you are.

Mrs. MOODY. I know there are. I talk to them all the time.

Mr. GUTKNECHT. You were talking about employing approximately how many people?

Mrs. MOODY. Well, if we open this new business, we were thinking of one or two employees to help us out in a small retail business.

Right now we only have one salesman. It's not a retail type of a thing. It's a wholesale thing. So we don't have the regulatory accountability.

But if we do open a retail business, it will be two at the most. I'm just not sure it's worth it. We've discussed it over and over again since we went to that convention, and the more we think about it, the more we're leaning toward not doing it at all and staying with simply just home marketing based with something the two of us can do and getting into something different, keeping on what we're doing now, but maybe branching off into something else we can market from our house with just the two of us.

It's not worth it. It's not worth the headaches. It's not worth the financial risk. Why should we risk our capital, our time, our health worrying about all of this and trying to create jobs and trying to be good citizens? There is no payoff, and especially after listening to these gentleman on a larger scale. Uncle. I'll cry uncle.

Mr. GUTKNECHT. It doesn't get any better when you get bigger. I think most of the members of this subcommittee, in the testimony we've heard, understand that we are in grave danger of killing the goose that lays the golden eggs. The free enterprise system was built on the basic notion of people being willing to go out and take a chance at it. Mr. Bartlett, at first I couldn't remember where I'd seen you before, but I was in Muncie, IN, for the field hearing, and you testified, I believe, then and talked a little bit.

Mr. BARTLETT. Yes. I remember you, though.

Mr. GUTKNECHT. And frankly, I don't know if we've made things a whole lot better since you testified. We've been wading away at this thing.

Mr. BARTLETT. Well, Mr. Chairman, I have to say that I'm sincerely worried about the future of small business in America, and I have to say that I'm absolutely astonished to be here today and see few people on the Republican side and nobody on the Democratic side, the very people that gave us these ridiculous regulations that we have to work with.

And if people like me and the other people that are at this table continue to do things like this and we see no results, we see nothing moving forward, nobody from the Democratic side, at what point do we quit?

When do we not do things like this? When do you say nothing is going to change. We're going to have problems. We're going to go bankrupt. Nobody listens. When do we just quit? Nobody on the Democratic side is here. I'm astonished, and actually, I'm angry about it.

Mr. GUTKNECHT. And I won't even make any apologies. We do have an awful lot of things going on but especially when people come from far distances to come and share their stories.

But we thank you for coming, and we are waging this war, and I must tell you it's frustrating from our perspective as well.

For either of the gentleman, and especially from Mr. Jackson, you have at least one or two stores here in the District of Columbia?

Mr. JACKSON. Four.

Mr. GUTKNECHT. You have four stores in the District?

Mr. JACKSON. Yes.

Mr. GUTKNECHT. Do you have any minimum wage people?

Mr. JACKSON. Yes.

Mr. GUTKNECHT. Now, I'm also on the Washington, DC Oversight Subcommittee. We learned the other day, when we were talking about minimum wage, that the District actually has a minimum wage that's already $1 an hour higher than anywhere else in the country.

Mr. JACKSON. Exactly. And Workmen's Comp is also higher, and unemployment insurance is also higher.

Mr. GUTKNECHT. Do you think that that has any impact on the number of jobs that are available? Because we have a couple of economists that testified the other day that there is a direct relationship between teenage unemployment and a higher minimum wage.

It struck me that here in the District especially where we have a particularly chronic problem with teenage unemployment that that may be one of the contributing factors. Do you have an opinion about that?

Mr. JACKSON. Yes, very much so. It's very hard to pay a teenager when you got to pay him the same as your regular help or some adult person there, but the law mandates we got to pay these people $5.25 per hour, if they're in school, doing summer work or whatever. That's the law.

So quite frankly, you try to stay away from it and try to do some other programs to help with the teenagers during the summer, work with some of the recreation departments and contribute some things there.

It's just unaffordable to hire a teenager at that price when you got them working beside an adult that's making the same thing.

Mr. GUTKNECHT. So in your opinion, it probably does contribute to even worse——

Mr. JACKSON. Yes, it does. Yes.

Mr. GUTKNECHT. So you have more idle teenagers out on the streets.

Mr. JACKSON. I think that's why we have so many out on the streets, because if you hire them, you got to pay them the $5.25. There is no doubt about it.

And it's startled me to find out that the Federal Government is just paying $4.25. I mean, it's really kind of rough.

Mr. GUTKNECHT. Well, Mr. Alexander, I appreciate your testimony. Perhaps you want to comment on minimum wage?

Mr. ALEXANDER. Well, in operating convenience stores, if we pay the minimum wage to—and I was just telling our colleagues a moment ago—I think if we really paid a minimum wage to convenience store operators, I'm afraid we would have as much theft as we would wages.

Most of your minimum wages or the minimum wage that we pay is somewhere in the neighborhood of $8 an hour, and if you don't pay that going rate, McDonald's or Burger King or your competitor down the street will come along and hire your person.

Mr. GUTKNECHT. And you're talking about rural North Carolina, now?

Mr. ALEXANDER. Yes, sir.

Mr. GUTKNECHT. Because we've heard that back in any district in Minnesota the minimum wage virtually does not exist anymore because you can't get people.

Mr. ALEXANDER. You couldn't get the people to come to work for you for $4 an hour.

Mr. GUTKNECHT. But there again, markets are more powerful. The market is setting the price.

Mr. ALEXANDER. Yes, sir. And I think also, if we raise this minimum wage, it's going to have a ripple effect in that the person who is making the $8 an hour is going to demand more wages, so that we're going to be paying more wages. We're going to be able to hire less people.

So it can have a backlash to us who are in business who are hiring people to work. If you hired someone off the street for $5 an hour, don't you think the man who has been working for you for 6 months who is making $8, he's going to be looking for an increase also.

Mr. GUTKNECHT. Absolutely. My time has expired. This Congress and the Federal Government over the last 30 or 40 years has, sort of, had this ongoing experiment in terms of regulations and mandates, and the results have not been all that good.

I do agree, and, in fact, one of the guiding principles or little booklets that we hand out on this committee is "The Death of Common Sense," and what we've really been trying to do is just get back to common sense.

That's, I guess, all in the eye of the beholder, but there is a real concern, at least on the part of this Member and I think most of the members of this subcommittee that we are in serious danger of losing something that we have taken for granted for all of these years here in this country, and that is that entrepreneurial spirit to go out and take a chance and try to make something of it.

If we lose that, I don't know how we get it back. I really don't. So I appreciate all of you coming. My time has expired. I'm going to yield to my colleague from the State of Arizona, Mr. Shadegg.

Mr. SHADEGG. Thank you, Mr. Chairman, and I would echo all of your remarks. Let me just start by saying thank you to each one of you.

It is important that you come forward and tell your stories. It does help us create a record. Ms. Moody, your testimony about how you just ultimately, in frustration, give up lays the case for what is wrong here.

I think it very interesting that Mr. Walton mentioned that his children aren't really anxious to inherit his business. Indeed, they're worried that they may be forced to inherit it and become liable even though they don't even want that.

Mr. Alexander mentioned his children are worried about whether or not they want to get into this business because of the risks.

I thought there was great irony in Mr. Walton saying, "Well, I guess the prospect is that everybody will go to work for the government," and it turns out Mr. Jackson's daughter has done just exactly that.

I can't resist making one more comment about this. Mr. Bartlett, don't quit now. The fact that no one is there on that side, that our Democratic colleagues didn't show today establishes only that this war is really not being waged most importantly in Washington.

It's being waged across America. The election which is going to occur in a few short months is going to be a battle over whether we go back to this massive regulatory scheme or whether we go forward, whether we say, "Wait a minute. It was well intended, and we shouldn't repeal it all," but some of it has unintended consequences which are absurd. I want to talk about those in just a second.

Don't quit now. They don't listen to you here, but they will listen to you at the ballot box, and if you can go home to Indiana, if Mr. Walton can go home to Arizona, if Ms. Moody can go home to Washington, Mr. Alexander to North Carolina, Mr. Jackson here in the District and just tell this story over and over again about how you're good citizens trying to make a living, trying to make the American free enterprise system work for a good purpose, and the system has been made unworkable.

I want to point out one last irony before I ask a question. Mr. Walton and Mr. Bartlett, if I understand your testimony, it really is that you operated businesses for many years.

In Mr. Walton's case, I know he acquired a business that had been operated many years before. We're all here debating, "Well, we want to live up to these regulations. The regulations are burdensome, but we'll do our best. We'll live up to them. We'd really like you to ease them up a little bit, but we're good citizens. We'll live up to them."

Nobody here has said, "I'm not going to obey the law," and yet the essence of Mr. Walton's testimony and Mr. Bartlett's testimony is they lived up to every single regulation in existence at the time.

You operated the state-of-the-art dry-cleaners. Your predecessors operated it, Mr. Walton, state-of-the-art, had no idea they were doing anything wrong.

Mr. Bartlett started a small business. He operated those tanks exactly the way they should, and now, in Mr. Bartlett's case, I understand he faces criminal charges.

In Mr. Walton's case, you face financial ruin not for disobeying these massive regulations but for living up to them.

I guess I'd like your comments on that. Mr. Bartlett, I'd like to hear you state again for the record that once you extracted all this earth the grass is growing out of it fine, there is no damage.

Mr. Walton, I guess I'd like you to relate to us what the prospects are in the future for how you deal with being held accountable for cleaning up stuff that nobody can say you really did.

And then I know, Mr. Walton, you've expressed to me your feelings about the minimum wage and what it will do to your employees, and I guess I'd like to hear that.

Mr. BARTLETT. Well, I think that the laws were well-intentioned. I think that many of the people that work for EPA and IDEM are well-intentioned people, but the laws seem, from my perspective, to have a one size fits all mentality.

And one can't have a one size fits all mentality because every little business is different than the one before it. The laws seem to be so fragmented and so complicated that a small businessman like myself and many of the other people I know in this small business community can never ever understand the absolute correct way that you're supposed to do things.

You hire two consulting firms, you get two different answers. For a quick example, we were notified by IDEM that we had to comply with the Clean Air Act.

And I thought we don't have any particulate matter going out of the building. There is nothing outside. Why would we have to comply? So we hired an environmental consulting firm.

They said, "Yes, you do have to comply," $1,500 to tell me that. Didn't believe it. We hired another consulting firm, and they said, "Heavens, no. You don't have to comply." We submitted the letter from the second consulting firm, so we didn't have to comply.

And it was the same thing with the Clean Water Act, where we were told we had to comply, and every time that it rained in Muncie, IN, which would have been a lot this spring, we had to sample the water on our parking lot both in front of the building and in the back of the building.

And I thought why would you have to do that? Why do you have to sample the water every time it rains? At a cost of probably $150 we hired an environmental consulting firm. We didn't have to comply, but yet we were told that we would.

And I think that pretty much sums up what happens in these regulatory matters not just with the EPA but in many of them, fragmented rules, one size fits all mentality. And how can you comply?

Mr. SHADEGG. Mr. Walton, they are now trying to draw you into a lawsuit having to do with underground storage tanks across the street?

Mr. WALTON. The particular intersection we're at, has been surrounded by seven gas stations and gas stations for 35 years. So their primary problem is petroleum.

There is a trace amount of perchlorethlyne, and of course they assume because it's perc that it must be us. This is a brief list of household products that contain perchlorethlyne—Spray and Wash, Liquid Plumber, White Out, Shout, Resolve carpet cleaner, S&S spot solvent spray, Napa brake cleaner, electric motor contact brake cleaner, Radiator Specialty Company brake cleaner, Gunk Home and Audio, K2R spot lifter, glass cleaner and wax remover, B–33 engine degreaser spray, McKay all-purpose parts dips, jewelry cleaner, canned snow, paint thinner and rubber cement.

I can remember as a running man using B–33 engine cleaner and Gunk to degrease my engine at a 25 cent car wash. Of course, the significance of that is I was sending polluted chemicals down the storm sewers of Phoenix.

Recently, in Recycling Review, an article came out that said the average American household contributes 20 pounds of hazardous household contaminants a year.

There are now approximately 3 million people in Maricopa County. Does that mean we're getting 60 million pounds of household hazardous chemicals down the drain every year?

If it does, I don't see how you can hold businesses responsible when you can't distinguish whose chemical is it. If it was an engine degreaser, it was used by some of these gas stations and garages in the degreasing of engine parts and so on.

So first of all, it's very hard to point the blame at any one person, but that doesn't stop the government, of course.

The hideous provisions of retroactive liability, joint liability and strict liability are something I think that we all need to deeply understand.

If anyone here believes in retroactive liability, I think they should try it on their kids at home. If your son won't clean up his room, you tell your daughter to clean it up.

If she says, "Well, why should I clean up that polluted mess?" you tell her, "Well, I think there is a sock in there that belongs to you."

And if she's smart, she says, "Well, I don't think that belongs to me. I think that belongs to my girlfriend." You say, "Well, wait a minute. I'm going to impose retroactive liability. Your mother and I think you dropped a diaper in there when you were 18 months old. Clean up the whole thing."

Joint liability says that if one party doesn't clean up something, the other one is 100 percent responsible. To understand it, you need to almost exaggerate the concept.

Can you imagine being on the beach in Alaska when the Exxon Valdez dropped a million gallons of crude oil? If somebody had come up to you and said, "Do you realize that your jeep is leaking oil?" If you drop 5 quarts of refined oil and the Exxon Valdez drops a million gallons of crude oil, if Exxon goes bankrupt, you're 100 percent responsible for the cleanup of the beach?

When you start to see how heinous these liability provisions are, you realize that they just can't work. To my mind, what we've got going here is a prescription for a dysfunctional society.

Mr. SHADEGG. If you could, Mr. Walton, just briefly, your comments on the minimum wage.

Mr. WALTON. First of all, the concept of minimum wage brought to mind a small packet I received in the mail a little while back.

I think my mother is getting ready to die. She's had two strokes, and she's in her 80's. In the packet was some ribbons I had won in fourth grade for track, a 47-year-old photograph of a 10-year-old boy putting money in the bank.

I think the title of the article was something like, "What is he saving for?" And it says, "10-year-old Richard Walton is passing money to teller so-and-so. Many of Centerville's independent Journal carriers are saving money for their future."

The picture is significant to me not because it's my first job, but because it reminds me of my first job. I thought I was 7 years old when I was selling papers.

My mother tells me I was actually 6. I do remember that I couldn't count change. I just held my hand out. It was during the war years, and it must have been 1945. Maybe there weren't a lot of people around. We certainly wouldn't let a 6-year-old sell papers today.

But 50 years later, I understand the significance of that first job. What I learned from that job was not just that you could get money for work. What I learned was confidence. Handling those papers day after day, you cannot help but gain some confidence about that. Talk to any young mother that has raised a child and held it in her arms for a year, if you ask her, "Would you be any more confident raising the second child?"

"Oh, yes. It would be no problem. I've handled this kid for a year."

Talk to anybody that has worked with a hand tool for a year if they would have confidence.

The benefit here of work is beyond money. Confidence as a 6-year-old handling papers, first of all, made me realize that I was responsible for something. If I lost the papers, I was responsible for the money. Handling the papers made me aware of words and the power of words.

My second job was a carrier. The third job was working for the paper stuffing papers. Some of these jobs were wonderful, because they had an incentive side to them.

If I didn't get complaints on a route, I got a free pass to the movie theater on Saturday. The 50 cents or so that I made stuffing papers was enough to get me popcorn. I spent many wonderful weekends in those movie theaters.

I'm reminded of a recent article, too, regarding work in the——

Mr. SHADEGG. We're going to run out of time. I need you just to talk about what it's doing today to your workforce.

Mr. WALTON. All right. I think the point I want to make about my business with respect to minimum wage is we have many hourly people, and hourly people tend to gauge their worth based upon their pay relative to minimum wage.

In other words, if we bring somebody in at $6.50 an hour, they know they're above the $4.25 minimum wage by a certain amount. If you raise minimum wage, it lowers their self-esteem. What it does is it triggers a chain reaction of requests for raises. They want to be back where they were before.

What I was hoping to say here is that in this country we're not doing as much training as Europe is. I'd just like to read it, if I could. It's an article titled, "Holding onto your good people."

> American employers have not invested enough in the training and development of their people. Employers in Europe and Asia invest 5 to 7 percent of payroll into training, education and professional development.
>
> In the United States, the average is 1 to 3 percent. This includes more than fundamental driver-salesman training. Wise employers today recognize a desire of the majority of American employees to learn and grow.
>
> These people don't necessarily want higher positions or more money. They want to be better tomorrow than they were yesterday.

So there are benefits to work beyond just the wage. I've sat here wondering why do we even have a minimum wage. What would happen if we abolish minimum wage? Wouldn't the marketplace set the value of goods and services?

And with respect to larger issues like Superfund, I view minimum wage and the discussion of it like discussing etiquette. It doesn't matter where you set it, if you're about to be hit by an asteroid.

For me, the heinous provisions of Superfund will wipe the company out. It won't matter where you've set minimum wage. I hope my comments have been beneficial.

Mr. SHADEGG. Thank you very much. Mr. Chairman, I see my time has expired. Let me just conclude by saying your testimony is a part of the discussion that's going to go forward between now and election day, as I said earlier, over all of these issues, over the notion that Government knows better than people.

It's that fundamental. It is whether Government knows better than people how to run this Nation. I think you'll have a clear choice. I hope you will not, Mr. Bartlett, or any of you give up between now and then, at least. Thank you.

Mr. GUTKNECHT. Thank you, Congressman Shadegg. I would echo that this isn't so much a debate about right and left. It's really a debate about right and wrong.

And some of the things that are happening out there are just flat wrong. I mean, to hold people retroactively liable for things which they had nothing to do with, or, more importantly, that they did 20 years ago in good faith, I think in the view of at least myself and a growing number of members of this body that that's just plain wrong.

I want to thank you all for coming. Your testimony has been excellent. I apologize for the turnout of Members, but all of your remarks will become part of the permanent record. If you have other documents that you'd like to see inserted in the record, without objection I will make certain that they are put in the record.

In fact, if you have other things when you get back home that you realize that you should have given us, in terms of written documentation, if you will get them to us within the next week, I'll make sure that they're part of the record.

Again, thank you so much for coming forward to testify. I'm going to call forward the next panel. If I could get you all to please rise.

[Witnesses sworn.]

Mr. GUTKNECHT. The record will note that all witnesses answered in the affirmative. We welcome you today before this subcommittee.

First of all, Dr. Thomas Hopkins, who is the Gosnell Professor of Economics at the Rochester Institute of Technology. Mr. Hopkins.

STATEMENTS OF THOMAS HOPKINS, GOSNELL PROFESSOR OF ECONOMICS, ROCHESTER INSTITUTE OF TECHNOLOGY; LOWELL GALLAWAY, DISTINGUISHED PROFESSOR OF ECONOMICS, OHIO UNIVERSITY; AND MARK WILSON, REBECCA LUKENS FELLOW IN LABOR POLICY, HERITAGE FOUNDATION

Mr. HOPKINS. Mr. Chairman and members of the committee, I'm pleased to have this opportunity to present my views on the regulatory issues this subcommittee is addressing.

My name is Tom Hopkins. I am appearing in my capacity as Professor of Economics at the Rochester Institute of Technology.

With the Chair's permission, I'll summarize my written statement and submit it for the record. Regulatory burden is large, rising and distributed unevenly across American businesses, handicapping many smaller businesses.

Compliance with regulation absorbs resources that would be available for our purposes in the absence of regulation. This coerced shift of resources is not likely, in my view, to have a sizable effect on total employment, but it almost surely does result in less productive employment to the extent that regulations fail a benefit-cost test.

Available evidence suggests that much regulation does not pass such a test, and I think this creates a major public policy problem.

Indeed, half of all environment, health and safety regulations adopted since 1990 fail a benefit-cost test, which means that they mandate inefficient uses of resources.

Such findings would be of limited significance if regulatory compliance costs in the aggregate were small, but they are not. But my reckoning, some $670 billion annually is spent by those regulated to comply with all Federal regulations. That is over and above any costs paid by the Federal Government itself.

I define "regulation" broadly to include three groups of Federal requirements. Environmental and risk reduction regulations are mandates aimed as lessoning pollution, accidents and other societal risks. Price and entry control regulations are restrictions on rates and on who can do business. Paperwork regulations are mainly tax compliance procedures. The cost of paperwork regulation is largely the value of time that businesses and consumers must devote to paperwork.

Price and entry controls once dominated all regulatory burdens, but deregulatory efforts of the Carter and Reagan administrations shrank them considerably. Nonetheless, they still represent a third of our total regulatory burden.

Each of my three groups of regulations now accounts for roughly a third of total compliance costs, and that's what my first figure shows.

At the top is 1977 and now at the bottom, 1995, a substantial change in the relative importance of the types of regulations that we have.

Every American household in 1995 would have been billed nearly $7,000 annually—we look now at figure 2—in addition to taxes, if all Federal regulatory compliance costs were shared equally and collected directly.

So the bottom segment on that figure is the tax burden, the top segment on that figure is the regulatory burden per household.

In my view, since public debate primarily focuses on tax questions more so than on regulatory burden, we need to readdress that level and that mix of our burdens, since the burden of Government is just as real if it takes the form of taxes paid or time consumed or required business spending.

While it is the American households that ultimately feel the effects of regulation, initially, much of the regulatory compliance spending is done by businesses.

Ninety percent of all U.S. firms have fewer than 20 employees, and only .3 percent have 500 or more. So a focus on small firms' burdens has considerable relevance. The average small firm with under 20 employees, and let's look mainly at the very far to the right segment, U.S. totals, the average small firm with under 20 employees appears to spend about $5,500 per worker to comply with Federal regulations.

By contrast, large firms, with over 500 workers, spend a much smaller $3,000 per employee complying with Federal regulations.

Aggregate regulatory compliance costs, and we go on to the next slide now, were falling in real terms from 1977 to about 1988, but they have been rising ever since.

When total costs are expressed relative to GDP, the next slide, there also is a decline that shows up from 1977 to 1988. Then, costs rise as a percent of GDP to 1992 and subsequently have been stabilizing in the 9 percent range, a substantial segment of our GDP required to comply with Federal regulation.

Tax related paperwork and pollution control now rank at our single-most important components of regulatory burden. As merely one example, the tax staff at my home town company, Eastman Kodak, grew 65 percent larger over the past decade during a general period of downsizing, and Kodak's annual tax return doubled in weight to 35 pounds.

Cost size alone is by no means an indicator of the reasonableness of regulation, but it can serve to identify areas where close scrutiny could have a substantial payoff.

Indeed, any regulatory requirement that provides benefits to society in excess of its cost deserves support unless there is an alternative way to get these benefits more cheaply.

Regrettably, regulators rarely use this criterion as the basis for their decisions. Indeed, key sections of many of our statutes forbid balancing benefits against costs.

Society loses when we hamstring our decisionmakers in that fashion. Regulation has an important role to play in our economy, but that role is not likely to be played well until burdens and benefits are better tracked and better balanced than has been the case to date.

Thank you, Mr. Chairman, for this opportunity to be here.

[The prepared statement of Mr. Hopkins follows:]

Statement of
Thomas D. Hopkins
Rochester Institute of Technology
Rochester, New York

Before the

Subcommittee on National Economic Growth, Natural Resources and Regulatory Affairs, Committee on Government Reform and Oversight
Congress of the United States
House of Representatives

May 16, 1996

Mr. Chairman and Members of the Committee, I am pleased to have this opportunity to present my views on the regulatory issues this Subcommittee is addressing. My name is Thomas D. Hopkins, and I am appearing in my capacity as the Arthur J. Gosnell Professor of Economics at the Rochester Institute of Technology. My work in this area dates from my service in the Executive Office of the President 1975-84, where my responsibility was regulatory analysis.

Government regulation, however well-intentioned and effectively designed, necessarily imposes burdens on those who are regulated. Some of these burdens are obvious, but many are not, due in part to indirect effects that ripple through the economy. Identifying such burdens explicitly would make government more accountable, but the government itself has made little systematic effort to measure these hidden costs of its programs. Such estimates of regulatory burden as do exist are large and rising, which makes improved accountability for government intrusiveness into the private sector a pressing concern. Of equal significance, regulatory compliance costs are distributed unevenly across American businesses, handicapping many smaller businesses.[1]

Compliance with regulation absorbs resources that would be available for other purposes in the absence of regulation. This coerced shift of resources is not likely, in my view, to have a sizable effect on total employment, but it almost surely does result in less productive employment to the extent that regulations fail a benefit-cost test. Available evidence suggests that much regulation does not pass such a test, and I think this creates a major public policy problem. Indeed, Robert Hahn concludes that

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[1] For further detail, see Thomas D. Hopkins, "Profiles of Regulatory Costs--Report to the U.S. Small Business Administration," No. PB96-128038 (Springfield, VA: National Technical Information Service, November, 1995); a revised version of this report will appear as a June 1996 policy study of the Center for the Study of American Business, Washington University in St. Louis. The S.B.A. does not necessarily concur with the views expressed here; see Office of Advocacy, U.S. Small Business Administration, "The Changing Burden of Regulation, Paperwork, and Tax Compliance on Small Business: A Report to Congress," October 1995.

about half of all environment, health and safety regulations adopted since 1990 for which data are available fail a benefit-cost test, which means that they mandate inefficient uses of resources.[2] Such findings would be of limited significance if regulatory compliance costs in the aggregate were small--but they are not.

By my reckoning, some $670 billion annually is spent by those regulated to comply with all federal regulation.[3] That is over and above any costs paid by the federal government itself. I define regulation broadly to include three major groups of federal requirements. Environmental and risk reduction regulations are mandates aimed at lessening environmental and other societal risks. Price and entry control regulations are restrictions on rates and on business entry. Paperwork regulations include tax compliance procedures and paperwork requirements not having a direct social or economic function; the cost of paperwork regulation is largely the value of time that businesses and consumers must devote to paperwork.

Governmental controls on labor markets and on product prices and availability once dominated all regulatory burdens, but deregulatory efforts of the Carter and Reagan Administrations shrank them considerably. Nonetheless, they still represent roughly a third of total regulatory burden in the U.S. (and loom even larger in Western Europe). Each of my three groups of regulations now accounts for roughly a third of total compliance costs, quite a departure from the 1977 pattern (Figure 1).

The regulatory spending I report for price and entry controls (often called "economic" regulation) includes both a wealth transfer component (about two-thirds of the total) and a resource usage component (the remaining one-third). The former can be termed a "pick-pocket" effect, while the latter is a "featherbedding" effect. The pick-pocket effect is a transfer of spending power that absorbs no physical resources--for example, consumers pay higher prices to domestic producers as a result of textile import restrictions. The featherbedding effect, by contrast, is a mandate forcing producers to use more resources than they otherwise would in providing their products or services (recall the empty backhauls that in the 1970s plagued the trucking industry due to ICC regulation). While some contend that the pick-pocket effect should not be counted as a cost of regulation, it is sure to induce costly self-aggrandizing behavior by defenders of the regulation in the form of lobbying and other "rent-seeking" activities. Thus I include it.

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[2] Robert W. Hahn, "Regulatory Reform: What Do the Government's Numbers Tell Us?" American Enterprise Institute Conference Paper, Washington, DC, January 17, 1996.

[3] All of my estimates are stated in 1995 dollars. My work builds on the extensive searches of regulatory burden estimates completed for 1977 by R. Litan and W. Nordhaus (*Reforming Federal Regulation*, Yale University Press, 1983) and for 1988 by R. Hahn and R. Hird ("The Costs and Benefits of Regulation: Review and Synthesis," *Yale Journal on Regulation*, Winter 1991). These searches yielded aggregate cost estimates for the two years, detailed by type of regulation. Then as later and more adequate particular studies emerged, I used them to buttress and extend the earlier estimates.

Every American household in 1995 would have been billed nearly $7,000 annually, in addition to taxes, if all federal regulatory compliance costs were shared equally and collected directly (Figure 2). Most of the public debate about the cost of government focuses on taxes and simply ignores this regulatory burden altogether, even though federal taxes are not more than twice the total compliance cost of regulation. The burden of government on the private sector is just as real whether it takes the form of taxes paid, time consumed, or required business spending.

While it is the American household that ultimately feels the effects of regulation, initially much of the regulatory compliance spending is done by businesses. Ninety percent of all U.S. firms have fewer than 20 employees, and only 0.3 percent have 500 or more, so a focus on smaller firms' burdens has considerable relevance. Using plausible cost allocation assumptions, the average small firm with under 20 employees appears to have spent some $5,500 per employee to comply with federal regulations in 1992. By contrast, firms with 500-plus employees spent on average a much smaller $3,000 per employee. 1992 regulatory costs per employee appeared to be in the $4,000 range for trade and service sector firms with fewer than 20 employees; such small firms faced about 85 percent higher costs per employee than did firms employing 500 or more. Manufacturing firms employing 20-499 faced higher per employee costs than either smaller or larger manufacturers, and manufacturing firms of all sizes had higher costs per employee than firms in other sectors, ranging from $4,900 to $10,600. (See Figure 3.)

Aggregate regulatory compliance costs fell from 1977 to about 1988 and have been rising ever since (Figure 4). When total costs are expressed relative to GDP, a decline also occurred from 1977 to 1988. Costs as a percentage of GDP then increased through 1992 and subsequently stabilize in the nine percent range (Figure 5). Tax-related paperwork and pollution control now are our most costly individual components of regulatory burden. As merely one example, the tax staff at my hometown company, Eastman Kodak, grew 65 percent larger over the past decade (during a general period of downsizing), and Kodak's annual tax return doubled in weight to 35 pounds.[4]

Cost size alone is by no means an indicator of the reasonableness of regulation, but it can serve to identify areas where close scrutiny could have a substantial payoff. Indeed any regulatory requirement that provides benefits to society in excess of its costs deserves support, unless of course some alternative approach could secure these benefits in less costly fashion. Regrettably, regulators rarely use this criterion as the basis for their decisions. Indeed, "key sections of many environmental statutes forbid balancing benefits and costs."[5] When benefit-cost reasoning does not undergird decisionmaking, society loses out in two ways. Some regulatory programs fail

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[4] Testimony of R. Dobreski before Subcommittee on Oversight, Committee on Ways and Means, U.S. House of Representatives, December 9, 1994.

[5] P. Portney, "The Contingent Valuation Debate: Why Economists Should Care," *The Journal of Economic Perspectives*, Vol. 8, No. 4 (Fall 1994), p. 12.

to deliver results efficiently, and others fail to deliver as much benefit as they could for the costs incurred.

Actual regulatory burden probably exceeds my estimates, which mainly track only direct compliance spending. For example, the Environmental Protection Agency reports that "compliance cost estimates may understate substantially the true long-term costs of pollution control," a point with which economists generally agree.[6] Regulation forces change, altering what firms had adopted as the most profitable and productive means of doing business. Compliance spending estimates do not capture the resulting productivity decline, nor the adverse effects that any plant closings may have on consumers and workers. Moreover, regulation constrains innovation and growth, as evidenced by the behavior after basic deregulation of industries such as transportation.

Regulation has an important role to play in our economy. That role is unlikely to be well played from anyone's perspective, however, until burdens and benefits of regulation are better tracked and balanced than has been the case to date. Perhaps I can clarify this point through a brief comment on the White House regulatory review operation that has been in place for well over a decade and in which I once worked. Under Executive Order 12866 ("Regulatory Planning and Review") and its several predecessors, the Office of Management and Budget reviews each regulatory proposal likely to add $100 million or more compliance costs, utilizing a mandated agency analysis of benefits and costs. Strict adherence to these Executive Orders (in place since at least 1981), had it been achieved, would mean that the government easily should be able to assemble a systematic accounting of virtually all regulatory costs imposed since 1981.

This has not been accomplished to date, in part because a very large segment of regulatory costs is in practice beyond the reach of any Executive Order. As a rough approximation, independent agencies are responsible for most price and entry regulation, and most paperwork regulation is tax-compliance related; neither traditionally has received close scrutiny in the regulatory review process. The principal domain of OMB regulatory review is environmental and other social regulation, or just a third of all regulatory costs. Within this domain, agency cooperation with OMB review is tempered by the fact that many regulatory statutes as now worded are hostile at best to benefit-cost analysis. I by no means intend to belittle the value of OMB regulatory review, but merely to put it in a broader context and to note some of the handicaps under which it operates.

Thank you for the opportunity to participate in this hearing.

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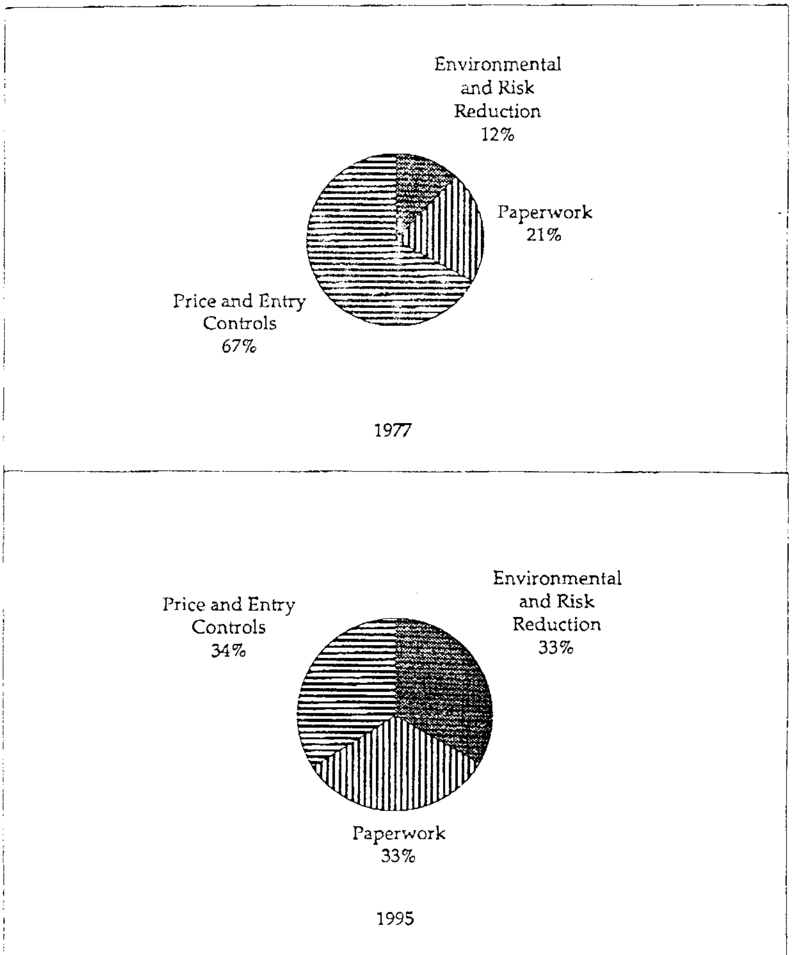
[6] EPA, "Environmental Investments: The Cost of a Clean Environment," EPA-230-12-90-084, December 1990, p. 1-3. Also see M. Cropper and W. Oates, "Environmental Economics: A Survey," *Journal of Economic Literature* (June 1992), p. 722.

Figure 1

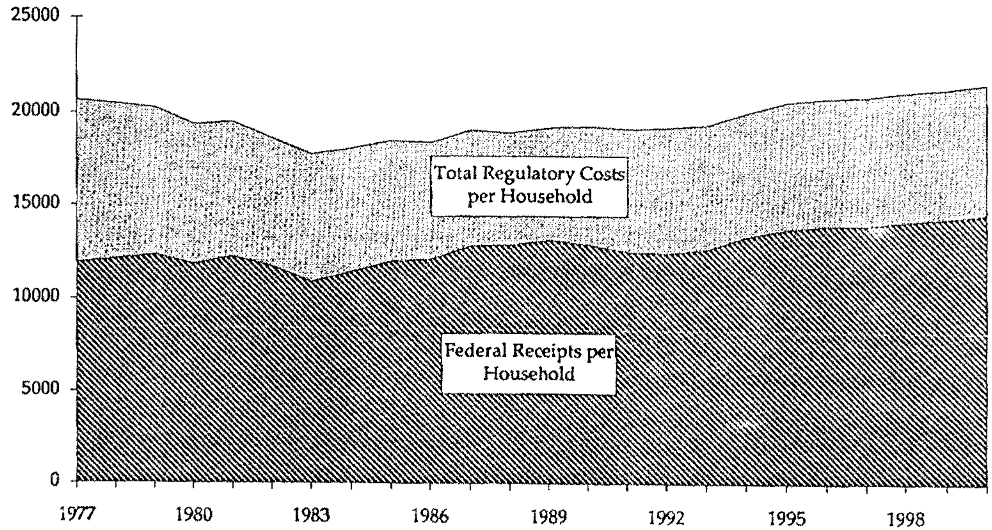
Percentage Distribution of Regulatory Costs



Based on T. Hopkins, "Profiles of Regulatory Costs," Report to SBA, NTIS #PB96-128038, November 1995

Figure 2

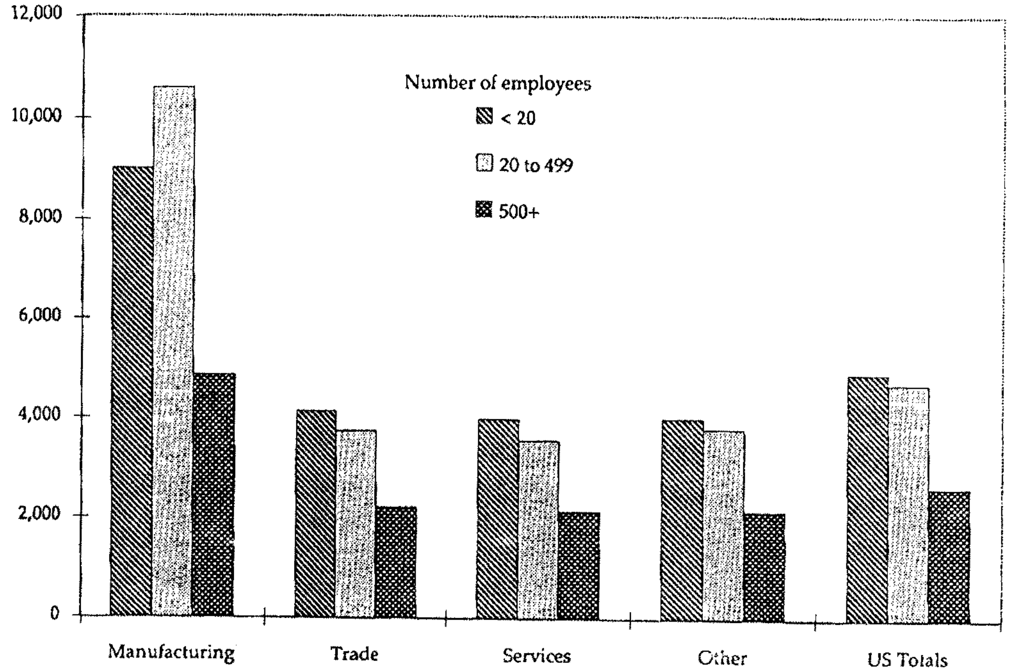
Federal Receipts and Regulatory Costs Per Household (1995 Dollars, in Billions)



Based on T. Hopkins, "Profiles of Regulatory Costs," Report to SBA, NTIS #PB96-128038, November 1995

Figure 3

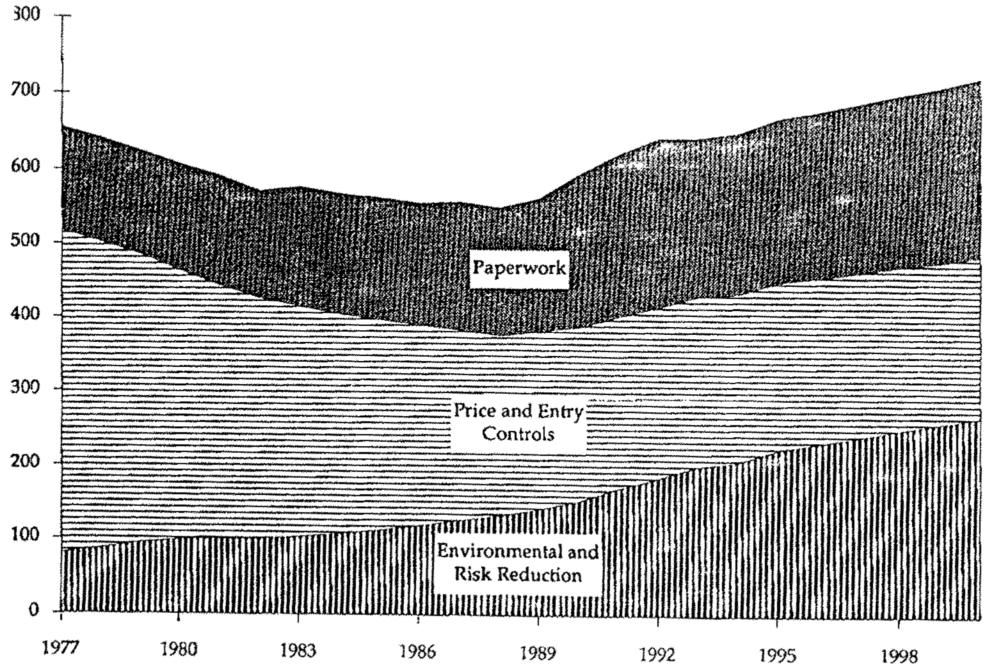
Regulatory Costs Per Employee by Firm Size, 1992 (1995 Dollars, in Billions)



Based on T. Hopkins, "Profiles of Regulatory Costs," Report to SBA, NTIS #PB96-128038, November 1995

Figure 4

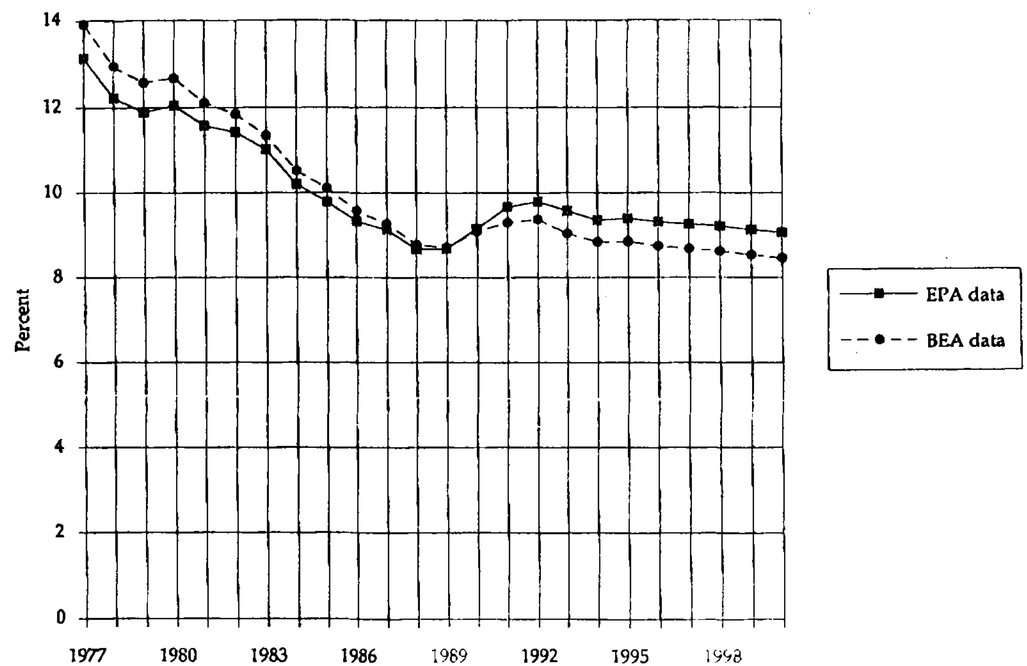
Total Regulatory Costs (1995 Dollars, in Billions)



Based on T. Hopkins, "Profiles of Regulatory Costs," Report to SBA, NTIS #PB96-128038, November 1995

Figure 5

Regulatory Costs as Percent of GDP



Based on T. Hopkins, "Profiles of Regulatory Costs," Report to SBA, NTIS #PB96-128038, November 1995

Mr. GUTKNECHT. Thank you, Professor Hopkins. The bells again that you heard, we're being called over to a vote. I'm going to try and move along here. We may be able to rotate chairmen so each of us can vote. I want to welcome Professor Gallaway now to the podium.

Mr. GALLAWAY. Thank you. It's a pleasure to be here. I will say right at the start, my testimony will lack the poignancy of some of the stories we heard from the previous panel, but that's just the curse of being an economist.

My name is Lowell Gallaway, Professor of Economics at Ohio University in Athens, OH. I thank you for the opportunity to testify this morning on the issues of employment and wages.

I say employment and wages because these phenomena are closely linked with one another. In recent decades, they have been substantially affected by actions of the Federal Government, especially Federal regulations and levels of Federal spending.

Unfortunately, the impacts have been largely negative. As evidence of this, I am submitting as an exhibit a recent analysis of the impact of levels of Federal spending on wage rates in the United States.

Co-authored with my Ohio University colleague Richard Vedder, it was prepared for the Joint Economic Committee of Congress. Its major conclusion is that excessive amounts of Federal spending have depressed American wage rates by 13 percent. I ask that this study be made a part of today's hearing record.

The impact of Federal Government actions on wage rates is a product of the inefficiencies that accompany them. These tend to reduce the productivity of labor in the American economy.

What are the sources of these inefficiencies? Now, a partial listing would include, one, a lack of economic incentives for efficiency in the public sector.

Managers of Government activities seldom receive rewards for initiating cost-reducing or output enhancing measures.

Government monopolies. For many governmental services, there is a single provider that does not view pressure to cut costs to meet competition from other providers of goods and services.

The lack of competition may explain why, by most measures, productivity has not risen rapidly in the provision of, for example, education and postal services.

Vested interest groups. As Government grows, efforts to use the political process to redistribute income from the general tax-paying public to specific individuals or groups intensifies.

Highway contractors promote infrastructure investment. Public employees seek large salary increases. Businesses lobby for subsidies, and still others favor public assistance of one form or another.

A fourth source is Government regulation. In a world without government, private entrepreneurs have incentives to raise productivity, to use fewer resources to produce a given want of output. Government regulation, if it is meaningful, interferes with this activity, leading to lower productivity. Last, the political process. In the public sector, legislators in particular think primarily in terms of the immediate future. They are attuned to the rhythm of electoral cycles.

In response to these cycles, they often will take actions that they perceive to be in their interest from the standpoint of being re-elected but which have adverse long-term effects on economic activity.

This is not to say that all Government activity is counter-productive. There are things that Government can do to enhance the functioning of an economy such as providing for the common defense, establishing a legal framework for resolving disputes, constructing a basic infrastructure and supervising some minimal safety net.

These are the positive benefits of Government. However, there are diminishing returns to Government activity, and as the Government enterprise continues to expand, the inefficiencies just described become more and more important. Particularly worth noting are the impacts of a wide variety of Government regulations on the Government labor market.

As already indicated, the general effect of Government regulatory activity is to increase the cost of producing goods and services.

These increases in cost have the same effect as imposing a tax on the employment of labor. Such taxes produce a variety of labor market adjustments.

In particular, they can lead to reductions in both the employment and earnings of labor in the United States. As a general proposition, every dollar of the implicit labor taxes produced by Government regulation leads to an 85 cent reduction in wages paid to workers.

In addition, there will be an impact on the level of employment. Every 1 percent net increase in labor cost, the regulatory tax minus the amount passed through to workers in the form of lower wages, will produce a decline in employment of about eight-tenths of 1 percent.

These are quite substantial impacts, given that some estimates, and I had in mind in particular Professor Hopkins' estimates, of the cost of Government regulations are in the neighborhood of 10 percent of GDP.

In the context of the current debate about raising the minimum wage, these are important considerations. In a minimum wage setting, any increase in labor cost cannot be passed on to workers in the form of reduced compensation.

However, it can have a profound affect on employment. The general evidence on this point is powerful. Every 1 percent increase in the minimum wage leads to a reduction in employment of three tenths of 1 percent in the affected areas.

These employment effects are primarily borne by the young and minorities. Balanced against this is the increase in earnings for those minimum wage workers who do not lose their jobs.

However, it would be quite possible to increase both the earnings and levels of employment of minimum wage workers by the simple device of reducing either the explicit or implicit taxes imposed on the employment of low wage workers in America.

Reducing the regulatory burden presently imposed on the employers of minimum wage workers, primarily small businesses, by

$1 an hour would lead to as much as an 85 cent an hour increase in the wages of these workers while increasing the number of jobs available to them.

This would be a much wiser public policy than increasing the present level of the Federal minimum wage. Thank you.

[The prepared statement of Mr. Gallaway follows:]

STATEMENT

Hearing on "The Impact of Regulations on Employment"

House Subcommittee on National Economic Growth, Natural Resources, and Regulatory Affairs

May 16, 1996

Presented by

Lowell Gallaway
Distinguished Professor of Economics
Ohio University
Athens, Ohio 45701

My name is Lowell Gallaway, Distinguished Professor of Economics at Ohio University in Athens, Ohio. I thank you for the opportunity to testify this morning on the issues of employment and wages I say employment and wages because these phenomena are closely linked with one another. In recent decades, they have been substantially affected by actions of the Federal government, especially Federal regulations and levels of Federal spending. Unfortunately, the impacts have been largely negative. As evidence of this, I am submitting as an exhibit a recent analysis of the impact of levels of Federal spending on wage rates in the United States. Co-authored with my Ohio University colleague, Richard Vedder, it was prepared for the Joint Economic Committee of Congress. Its major conclusion is that excessive amounts of Federal spending have depressed American wage rates by 13 percent. I ask that this study be made a part of today's hearing record.

The impact of Federal government actions on wage rates is a product of the inefficiencies that accompany them. These tend to reduce the productivity of labor in the

American economy. What are the sources of these inefficiencies? A partial listing of them would include:

(1) A lack of economic incentives for efficiency in the public sector: Managers of government activities seldom receive rewards for initiating cost-reducing or output-enhancing measures. Indeed, in some cases, increases in productivity may mean the manager in question has a smaller budget and also must incur the wrath of fellow employees who suffer from the changes which generated the increase in output per worker.

(2) Government monopolies: For many governmental services, there is a single provider that does not feel pressure to cut costs to meet competition from other providers of goods and services. The lack of competition may explain why, by most measures, productivity has not risen rapidly in the provision of, for example, education and postal services.

(3) Vested interest groups: As government grows, efforts to use the political process to redistribute income from the general taxpaying public to specific individuals or groups intensifies. Highway contractors promote "infrastructure investment," public employees seek large salary increases, businesses lobby for subsidies, and still others favor public assistance of one form or another. Mancur Olson calls these groups "distributional coalitions" and argues persuasively that they impair economic growth.[1]

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[1] Mancur Olson, **The Rise and Decline of Nations** (New Haven: Yale University Press, 1982).

(4) Government regulation: In a world without government, private entrepreneurs have incentives to raise productivity - to use fewer resources to produce a given quantity of output. Government regulation, if it is meaningful, interferes with this activity, leading to lower productivity. While some regulation may be needed, it can become excessive and generate more costs than benefits.

(5) The political process: In the public sector, legislators, in particular, think primarily in terms of the immediate future. They are attuned to the rhythm of electoral cycles. In response to these cycles, they often will take actions that they perceive to be in their interest from the standpoint of being re-elected, but which have adverse long-term effects on economic activity.

This is not to say that all government activity is counter-productive. There are things government can do to enhance the functioning of an economy, such as providing for the common defense, establishing a legal framework for resolving disputes, constructing a basic infrastructure, and supervising some minimal safety-net. These are the positive benefits of government. However, there are diminishing returns to government activity and, as the government enterprise continues to expand, the inefficiencies just described become more and more important.

Particularly worth noting are the impacts of a wide variety of government regulations on the American labor market As already noted, the general effect of government regulatory activity is to increase the cost of producing goods and services.

These increases in costs have the same effect as imposing a tax on the employment of labor. Such taxes produce a variety of labor market adjustments. In particular, they can lead to reductions in both the employment and earnings of labor in the United States. As a general proposition, every dollar of the implicit labor taxes produced by government regulation leads to an 85 cent reduction in wages paid to workers. In addition, there will be an impact on the level of employment. Every one percent net increase in labor costs (the regulatory "tax" minus the amount passed through to workers in the form of lower wages) will produce a decline in employment of about eight-tenths of one percent. These are quite substantial impacts given that some estimates of the costs of government regulation are in the neighborhood of ten percent of GDP.

In the context of the current debate about raising the minimum wage, these are important considerations. In a minimum wage setting, any increase in labor costs cannot be passed on to workers in the form of reduced compensation. However, it can have a profound affect on employment. The general evidence on this point is powerful. Every one percent increase in the minimum wage leads to a reduction in employment of thre-tenths of one percent in the affected areas. These employment effects are primarily born by the young and minorities. Balanced against this is the increase in earnings for those minimum wage workers who do not lose their jobs. However, it would be quite possible to increase both the earnings and levels of employment of minimum wage workers by the simple device of reducing either the explicit or implicit taxes imposed on the employment of low-wage workers in America. Reducing the regulatory burden presently imposed on the employers of minimum wage workers, primarily small businesses, by a dollar an hour would lead to as much as an 85 cent an hour increase in the wages of these workers while increasing the number of jobs available to them. This would be a much wiser public policy than increasing the present level of the Federal minimum wage.

THE IMPACT OF THE WELFARE STATE ON WORKERS

Executive Summary

This is the second study in a series I have commissioned on the impact of the welfare state on various aspects of the American economy. The first study, ***The Impact of the Welfare State on the American Economy***, examined the drag on economic growth resulting from excessive levels of federal spending. The second study, ***The Impact of the Welfare State on Workers***, analyzes the relationship between the size of the federal government and recent trends in income and compensation.

The first section of this study debunks the myth advanced by Labor Secretary Robert Reich that seeks to blame the income stagnation under the Clinton Administration on a recovery in business profits. This study refutes the notion that business profits cause income stagnation, and instead demonstrates that healthy business profits tend to generate compensation gains for American workers. This section of the study also shows that when appropriate inflation measures are used, hourly wages and benefits received by the typical worker increased about 26 percent between 1973 and 1994, after adjustment for inflation. This study demonstrates that there was a very close relationship between productivity and compensation growth during this period.

The second section of the report focuses on the relationship between excessive federal spending, productivity, and compensation. Among the conclusions of the study are the following:

- When federal spending as a share of GDP exceeds a level of 17.4 percent, additional federal spending becomes literally counterproductive, with negative effects on productivity and compensation growth.

- At present levels of federal spending as a share of GDP, restraining federal spending by one dollar during the current year would yield an increase of 26 cents in total wages and benefits. Sustaining this budget restraint over a seven year period would produce cumulative gains of $1.68.

- Over time, the drag of excessive federal spending on productivity and compensation growth are striking. If federal spending had been held constant at its 1965 share of 17.6 percent of GDP, and federal taxes adjusted accordingly, the present value of the gains to the typical worker over the period 1973-1994 would have amounted to $106,800, enough to purchase a median priced new home.

This study provides a public service by quantifying the sizable costs of excessive federal spending to the average worker in the U.S. I am pleased to make this study available to the Congress and public, and hope it contributes to an informed debate about the counterproductive effects of excessive federal spending in America.

Jim Saxton
Vice-Chairman
Joint Economic Committee

THE IMPACT OF THE WELFARE STATE ON WORKERS

by
Lowell Gallaway and Richard Vedder

PROLOGUE

This is the second in a series of studies designed to explore the question of whether the federal government in the United States is **too large**. In the first study, the general issue of the effect of the size of the federal government, measured as a percent of Gross Domestic Product (GDP), on the level of GDP is analyzed. Our major finding in that study is that beyond a level of federal spending amounting to 17.57 percent of GDP, additional federal expenditures have a **negative** impact. At current levels of spending and GDP, restraining federal spending by a dollar will add 38 cents to GDP.

In this study, we pursue this question at a more disaggregated level, focusing on the impact of an oversized government on the real compensation of workers in the United States. What we discover is a set of relationships that is quite consistent with our earlier findings. Specifically, we find that restraining current federal spending by one dollar will lead to a 26 cent increase in the real compensation of workers. The details of our analysis follow. The first section examines measurement issues and the relationship between productivity and compensation growth. The second section statistically examines the effects of an excessive federal government on wages and benefits.

I. THE LABOR INCOME GROWTH PROBLEM

"It was the best of times, it was the worst of times."
Charles Dickens,
A Tale of Two Cities

Charles Dickens did not have the American labor market in mind when he penned those famous words. However, with modest rewording to read, "Was it the best of times or the worst of times," they rather accurately describe the current controversy centering on the pattern of growth (or lack of growth) of the real economic rewards to workers in the United States. Depending on how one defines the pay of workers, and which price index is used to convert from nominal to real terms, almost any story can be told.[1] Figure 1 illustrates the extreme versions of the possible scenarios that may be sketched. The solid line describes average weekly earnings for the private sector of the economy deflated by the official consumer price index. The data are in index number form, with 1973 set equal to 100.[2] This data series shows an increase from 62.4 in 1947 to 100 in 1973 and, then, a decline to 79.3 in 1994.

On the other hand, the broken line in Figure 1 describes movements in worker compensation per hour deflated by the Gross Domestic Product deflator for the non-financial corporate business sector of the American economy. It stood at 49.9 in 1948, rose to 100 in 1973, and increased further to 137.7 in 1994, quite a different picture than that provided by the weekly earnings series.

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[1] Karl Zinmeister summarizes this controversy quite well in, "Coming this Year: Marx for Dummies," **Wall Street Journal**, January 25, 1996, p. a22.

[2] 1973 is used as the base year because it is a business cycle peak and many of the real wage series we will refer to also peak at that time.

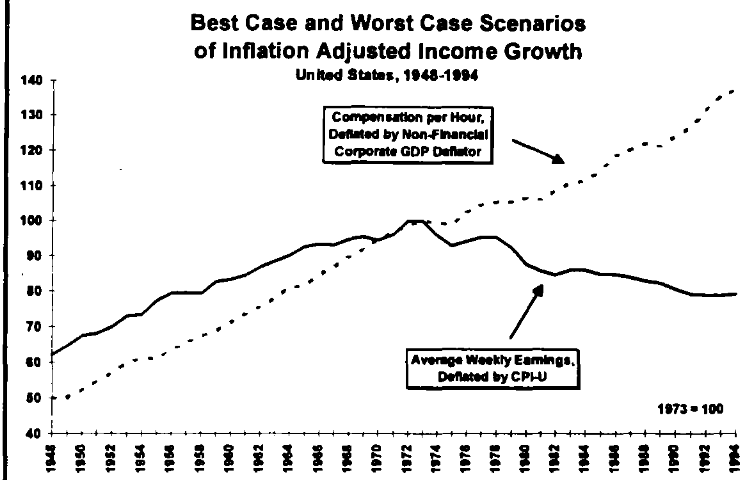

Figure 1

The Wage Measurement Problem

Two factors account for the widely disparate views of the world described graphically in Figure 1. First, the average weekly earnings series does not take into account changes in the number of hours worked per week, and second, it ignores the increasing importance of fringe benefits as a part of the payment package available to workers. Hours of work have been systematically declining throughout the post-World War II era.[3]

The negative impact of this decline on average weekly earnings is illustrated in Figure 2. Three series are presented there, average weekly earnings, average hourly earnings (both for the private sector of the economy), and average workers compensation per hour for the business sector of the American economy. All are deflated by the official consumer price index (CPI-U). A comparison of the weekly and hourly earnings series shows that, in 1947, the weekly index exceeded the hourly index by 9.1 percent. However, in 1994, the situation was reversed. The hourly series was larger than the weekly by 6.8 percent. Thus weekly and annual earnings averages understate wage growth because these measures are not adjusted for the decline in hours during the period.

[3] Between 1973 and 1994, average weekly hours in the private sector of the economy fell from 36.9 to 34.7, a decline of 6.0 percent. Source: Department of Labor, Bureau of Labor Statistics, as reported in **Economic Report of the President, 1995** (Washington, DC: Government Printing Office, 1995), Table B-45, and **Economic Indicators** (Washington, DC: Government Printing Office, 1995), November 1995, p. 15.

Three Measures of Inflation Adjusted Labor Income
United States, 1947-1994
(Deflated by CPI-U)

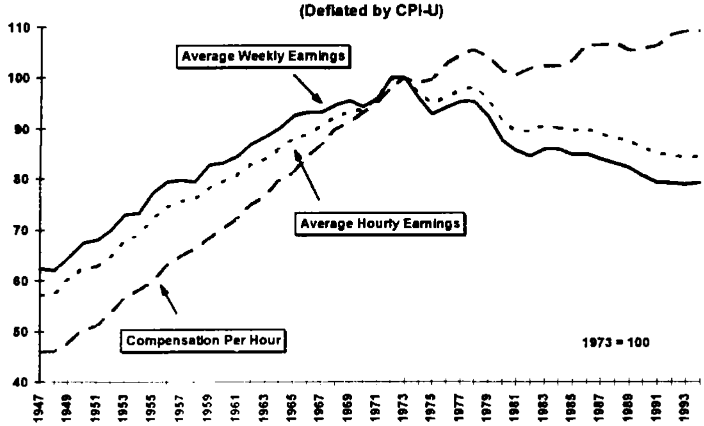

Figure 2

Even more important is the increasing importance of fringe benefits. In 1947, the compensation per hour index was 19.7 percent less than the hourly earnings series. By 1994, it was 28.1 percent **greater**. Moving from a simple hourly earnings to an hourly compensation analysis makes a tremendous difference. It changes the story from one of major declines in economic rewards to employees since 1973 to one of modest increases.

The Price Index Problem

Definitional distortions are only one part of the problem of assessing the growth pattern in the real value of the package of economic payments received by workers. The choice of a price index to convert nominal to real values is crucial. To illustrate the importance of the price index issue, the behavior over time of four such indices is shown graphically in Figure 3.[4] The four indices are:

[4] The price index issue has been moving to the forefront in recent years. The Boskin Commission report argues that the problem is even more acute than suggested here. However, we have confined our discussion to a series of currently published official indices.

1. The official consumer price index (CPI-U),
2. A special price index series disseminated by the Bureau of Labor Statistics known as the CPI-U-X1,
3. The price deflator for Gross Domestic Product, and
4. The price deflator for the corporate, non-financial, business sector of the economy.

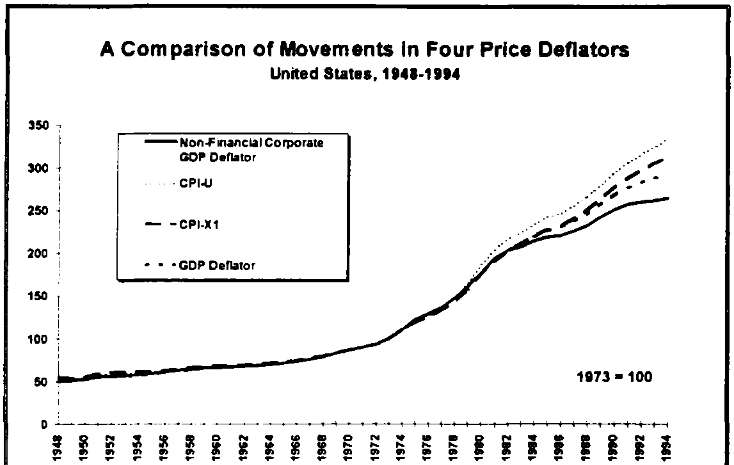

Figure 3

A few words are in order concerning the first two of these indices. The CPI-U-X1 was developed by the Bureau of Labor Statistics in response to criticisms of the determination of the CPI-U. It is widely recognized that the CPI-U developed a pronounced upward bias circa 1980 due to the manner in which it was treating housing sector costs. The official Census Bureau position on the use of this index is as follows:[5]

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[5] U. S. Department of Commerce, Bureau of the Census, **Measuring the Effect of Benefits and Taxes on Income and Poverty: 1979 to 1991**, Current Population Reports, **Consumer Income**, Series P-60, No. 182RD (Washington, DC: U. S. Government Printing Office, 1992), page H-1.

> *The Bureau of Labor Statistics (BLS) developed an experimental Consumer Price Index (CPI-U-X1) for researchers who wish to make historical comparisons with the current Consumer Price Index for All Urban Consumers (CPI-U) which uses the rental equivalence approach to measuring shelter services. Prior to 1983, the measurement of homeowner costs included changes in the asset value of homes. ... This rental equivalence approach is a methodology that isolates the shelter services component and, therefore, is a superior measure . . .*
>
> *Therefore, BLS recommends the use of CPI-U-X1 to those who need a CPI series that treats homeowner costs consistently over time.*

Prior to the late 1970s, there is little problem with the price indices (see Panel A of Figure 3). For the most part, they move in unison. However, since than, there has been a substantial divergence in the four price indices we have described. By 1994, the CPI-U is 24.2 percent higher than the GDP deflator for the corporate, non-financial, sector of the economy (see Panel B of Figure 3). Such variation is capable of producing greatly disparate perceptions of what has been happening to the wages and compensation of workers in America. With three different wage and compensation measures and four different price indices, there are twelve possible variants of wage and compensation data. Values for these twelve wage and compensation indices are shown in Table 1 for 1947 (or, in some cases, 1948), 1973, and 1994.

Our preferred set of indices is that which describes the behavior of compensation per hour for workers. It more nearly measures the total per unit cost of labor to employers, as well as the total value of all money wages and various fringe benefits received by each unit of labor supplied in the market place. The four different versions of the real compensation per hour data series are shown in Figure 4. The differences are dramatic. Using the CPI-U, the real compensation shows a value of 109.3 (1973=100) in 1994. With the CPI-U-X1, it is 116.7; with the GDP deflator 124.2; and with the non-financial corporate business deflator 137.7

Table 1

Selected Values, Various Indices of Wage and Compensation Payments,
United States, 1947-1994

Wage or Compensation Measure	Price Index	1947	1973	1994
Average Weekly Earnings	CPI-U	62.4	100	79.3
Average Weekly Earnings	CPI-U-X1	61.1	100	84.3
Average Weekly Earnings	GDP Deflator	64	100	89
Average Weekly Earnings	GDP Deflator Corp. Non-Fin.	67.2	100	99.9
Average Hourly Earnings	CPI-U	57.2	100	84.6
Average Hourly Earnings	CPI-U-X1	55.9	100	89.9
Average Hourly Earnings	GDP Deflator	58.6	100	96.1
Average Hourly Earnings	GDP Deflator Corp. Non-Fin.	62	100	106.5
Compensation per Hour	CPI-U	45.9	100	109.3
Compensation per Hour	CPI-U-X1	44.9	100	116.7
Compensation per Hour	GDP Deflator	47.1	100	124.2
Compensation per Hour	GDP Deflator Corp. Non-Fin.	49.9	100	137.7

Source: Authors' Calculations

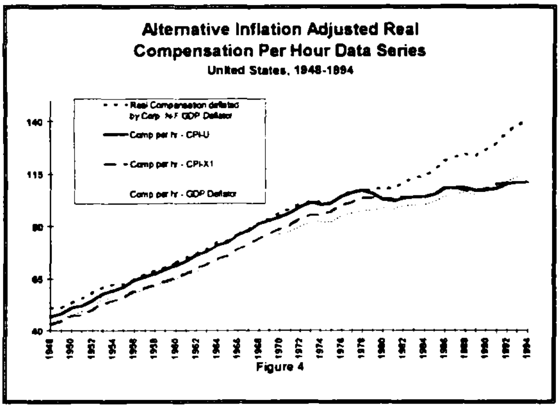

Figure 4

Notice that none of these data series substantiate the worst-case horror stories of sharply declining real economic returns to workers since 1973. Choosing among them is a difficult task. Only one can be rejected out of hand, that using the CPI-U. Beyond that, a case can be made for each of the other three, depending on whether you wish to focus solely on consumer goods or on some broader measure of goods and services produced in the American economy. Our solution to this problem is to use an average of the three data series derived by using the CPI-U-X1 and the two price deflators. The resulting real compensation series is shown in Figure 5. It shows a level of compensation in 1994 of 126.0.

The Compensation Growth Issue

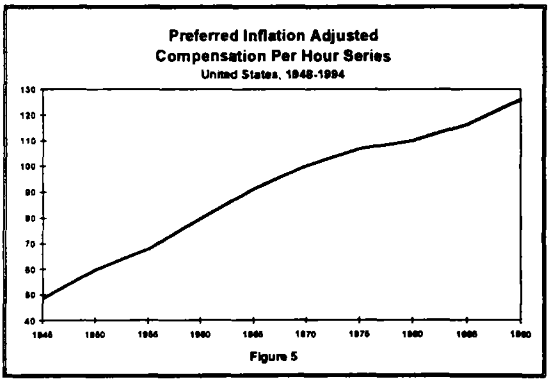

Figure 5

While the real compensation series shown in Figures 4 and 5 all indicate an increase in the hourly compensation of workers since 1973, a comparison of that growth with what occurred earlier in the post-World War II era clearly indicates a decline in the rate of growth in more recent years. Table 2 shows the annual growth rate in real wages or compensation for all twelve variants of the wage and compensation series reported in Table 1 plus that shown in Figure 5 for both the pre-1973 and post-1973 periods. In all twelve cases, the rate of growth is much greater in the pre-1973 period. In fact, in the first seven variants, growth is substantial and positive prior to 1973 and negative in the years following. It is only in the last six that growth is positive in both of these periods. In the case of the five variants of the real hourly compensation series, it more than doubles in the years 1947-1973. After 1973, the best rate of growth shows more than a one-third increase and our preferred measure increases by just a little more than one-fourth. This pronounced slowdown in the rate of growth in real hourly compensation needs to be explained.

The Reich Hypothesis

Secretary of Labor Robert Reich has offered an explanation of this phenomenon. In a Department of Labor press release,[6] he states, "There is something wrong with rising profits, rising productivity and a soaring stock market, but employment compensation heading nowhere." The thrust of Reich's claim is that increases in profits imply decreases in compensation.

The Reich hypothesis can be evaluated quite simply. Standard data sources provide information on the share of the total value of output that is accounted for by corporate profits. One such source contains data for the non financial corporate business portion of the economy.[7] From it, the share of the total value of output attributable to after-tax corporate profits can be calculated. We then used this data series in an attempt to explain variations in the real compensation per hour data series shown in Figure 5. Specifically, we explored the relationship between year-to-year changes in the corporate profits measure and year-to-year changes in real hourly compensation.

Table 2

Annual Growth Rates, Various Indices of Wage and Compensation Payments

United States, 1947-1973 and 1973-1994

Wage or Compensation Measure	Price Index	Annual Rate of Growth (%) 1947-1973	Annual Rate of Growth (%) 1973-1994
Average Weekly Earnings	CPI-U	1.8	-1.0
Average Weekly Earnings	CPI-U-X1	1.9	-0.7
Average Weekly Earnings	GDP Deflator	1.7	-0.5
Average Weekly Earnings*	GDP Deflator Corp. Non-Fin.	1.6	0.0
Average Hourly Earnings	CPI-U	2.2	-0.7
Average Hourly Earnings	CPI-U-X1	2.2	-0.5
Average Hourly Earnings	GDP Deflator	2.1	-0.2
Average Hourly Earnings*	GDP Deflator Corp. Non-Fin.	2.0	0.3
Compensation per Hour	CPI-U	3.0	0.4
Compensation per Hour	CPI-U-X1	3.1	0.7
Compensation per Hour	GDP Deflator	2.9	1.0
Compensation per Hour	GDP Deflator Corp. Non-Fin.	2.8	1.5
Compensation per Hour*	Avg. of CPI-U, CPI-U-X1, and CNF Deflator	2.9	1.1

* Data available beginning with 1948 — Source: Authors' Calculations

The results are reported in Table 3 for two different versions of the relationship and two different time periods. One version analyzes the linkage between changes in the corporate profits statistic and changes in compensation in the same period. The other looks at the same relationship, but asks the question, "Do changes in the corporate profit share this year affect the change in compensation between now and next year?" The two time periods used are 1948-1994 and 1973-1994.

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[6] Department of Labor press release, statement by Secretary Robert Reich, June 22, 1995.

[7] Data are obtained from **Economic Report of the President, 1995** (Washington, DC: Government Printing Office), B-14, p. 291, and **Economic Indicators** (Washington, DC: Government Printing Office), November 1995, p. 3.

Table 3

Regression Results, Analysis of Change in Real Compensation
Per Hour, United States, 1948-1994

Independent Variable	Time Period	Regression Coefficient	t-Statistic	Adjusted R^2	D-W Statistic
Change in After-Tax Profit Share	1949-94	-19.97	-1.29	0.0319	1.99
Change in After-Tax Profit Share	1973-94	2.52	0.09	-0.10	2.00
Change in After-Tax Profit Share (Lagged One Period)	1949-94	24.73	1.60	0.04	1.99
Change in After-Tax Profit Share (Lagged One Period)	1973-94	53.28	2.12	0.1174	2.04

Note: All regression equations have Arima adjustment = (0,2) Source: Authors' Calculations

Two rather clear findings emerge from the information contained in Table 3. First, there is no evidence of a significant relationship between changes in the corporate profit share of the value of output and changes in real compensation in the same year. The Reich hypothesis is **not** confirmed. Second, and more important, changes in the corporate profit share this year and changes in real hourly compensation next year are somewhat related (in a statistical sense)[8] to one another. However, the direction of the relationship directly contradicts the Reich hypothesis, being positive in nature. Increases in the corporate profit share this year are associated with increases in real hourly compensation next year. Interestingly, the relationship is more statistically significant in the post-1973 period. It seems clear that the Reich hypothesis makes no useful contribution to explaining the slowing of the rate of growth in real hourly compensation since 1973. It, along with its "class warfare" overtones, should be rejected. Any insights into the reasons for the compensation slowdown must come from elsewhere.

The Productivity Hypothesis

An alternative to Robert Reich's conjectures is to examine the behavior of the productivity of labor when seeking to explain variations in real compensation through time. Historically, levels of labor compensation have moved very closely with advances in the productivity of the labor input into the productive process.[9] Thus, perhaps the slower growth in labor compensation in recent years is merely a product of a lack of growth in the productivity of labor. A strong case can be made that this is so. The importance of productivity in this respect is illustrated quite vividly by Figure 6. It shows the pattern of behavior of average productivity per hour in the business sector and our preferred real hourly compensation series since 1947. The correspondence between the two is almost perfect.

[8] For the entire period, the relationship is significant at about the ten percent level. However, for the years 1973-1994, it is significant at the five percent level.

[9] For a discussion of the relationship between real wages and productivity, see our **Out of Work: Unemployment and Government in Twentieth Century America** (New York and Oakland, Calif.: Holmes and Meier and Independent Institute, 1993), particularly Chapter 11.

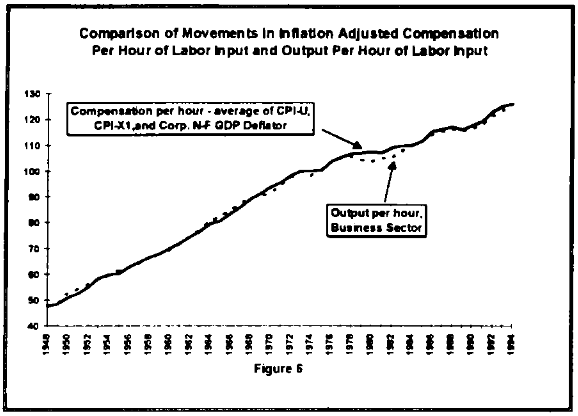

Figure 6

The graphic evidence shown in Figure 6 indicates that the observed retardation in the growth of real compensation in the United States can be traced to a similar retardation in the rate of productivity growth in the United States. Why the slowing in productivity growth? A reasonable hypothesis is that productivity growth is influenced in some fashion by governmental activities.

II. THE SIZE OF GOVERNMENT AND PRODUCTIVITY GROWTH

The increased command of government over scarce resources may have lowered productivity in America by shifting some resource allocation decisions from the relatively productive private sector to the less productive public sector. Why, however, is the public sector less efficient, less capable of producing high levels of output per worker? Six factors are key to understanding the government's negative role in productivity growth: behavioral incentives, monopoly, rent-seeking, regulation, benefit-cost asymmetry, and the shortsightedness effect.

Incentives

In the market-driven private sector, managers have a strong incentive to raise outputs in relation to inputs used to produce those outputs. Higher productivity means greater profits, as costs fall in relation to revenues. Greater profits, in turn, usually mean higher rewards to the managers and other employees considered responsible for the enhancement of productivity. Greater rewards might come in form of higher prices on company stock (particularly valuable when employees have stock options or are in a ESOP plan), profit sharing bonuses, or simply higher salaries. Market prices convey information that make decision-making relatively easy, easing resource allocation decisions. Ultimately, profits are generated by satisfying the needs of consumers. Profits serve as a measure by which managers of businesses can be held accountable by their bosses, the stockholders.

By contrast, in the public sector, managers seldom receive any rewards for enacting cost-reducing or output-enhancing measures. Indeed, in some cases, increases in productivity merely mean the manager in question has a smaller budget, and also must incur the wrath of fellow employees who may suffer from the changes which provided the advance in output per worker. The lack of profit signals makes it difficult to evaluate performance and thus hold managers accountable.

All of this explains why corporate downsizing by large, profitable companies such as IBM, ATT and Eastman Kodak is commonplace as firms try to enhance efficiency and thus shareholder value. Government downsizing, however, is far less common despite the fact that already the public sector is, on average, already less productive than the private one.

Monopoly

For most governmental services, there is a single provider. The government has a monopoly on the provision of the service. A government bureaucracy does not feel pressure to cut costs to meet competition from competing providers of goods or services. In general, that is not the case typically with providers in the private sector, who face competition from one or more firms anxious to offer a better product at a lower price. Competition prods firms into efficiencies and into offering improved products. The lack of competition may explain why, by most measures, productivity has not risen rapidly in the provision of, for example, education and postal services.

Rent-Seeking Behavior

As government grows, efforts to use the political process to redistribute income from the general taxpaying public to specific individuals or groups also intensify. Highway contractors promote "infrastructure investment", public employees seek large salary increases, businesses seek subsidies, still others favor public assistance of one form or another. When a group receives a payment without providing anything in return, it collects "economic rent." By any measure, most of the increase in real federal government expenditures in the past generation have gone for "transfer payments" - money being taken from the general taxpaying public and given to favored groups.

Mancur Olson calls these groups "distributional coalitions" and argues persuasively that they impair economic growth.[10] A host of studies have argued that rent-seeking behavior negatively impacts on growth.[11] The return to productive activity by ordinary citizens is reduced by taxes used to cover transfer payments.[12] On the other hand, the receipt of transfers is often contingent on the recipient showing a lack of productivity. Payments are given for not working (unemployment insurance, disability payments, welfare). The availability of alternative sources of income reduces incentives to work, reducing aggregate output.

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[10] Mancur Olson, **The Rise and Decline of Nations** (New Haven: Yale University Press, 1982).

[11] For example, see Richard Vedder and Lowell Gallaway, "Rent-Seeking, Distributional Coalitions, Taxes, Relative Prices and Economic Growth," **Public Choice**, vol 51, 1986, pp. 93-100.

[12] For a recent study citing dozens of papers demonstrating the adverse effects of taxes on economic growth, see Richard Vedder, **State and Local Taxes and Economic Growth: Lessons for Federal Tax Reform**, Staff Study, Joint Economic Committee of Congress (Washington, DC: Joint Economic Committee, 1995).

Regulation

In a world without government, profit-maximizing private entrepreneurs have every incentive to raise productivity - to reduce the use of inputs for any given quantity of output. Government regulation, if it is meaningful, interferes with this process. Governmental constraints limit the ability of firms to use resources as they like. If Machine A is used, government rules may specify how the equipment can be used. Labor laws regulate compensation of employees (e.g., minimum wage laws, the Davis-Bacon Act), sometimes reducing employment and thus output. In short, if it is correct that, other things held the same, cost-minimizing firms try to maximize output per worker, any government rule that forces behavioral changes will, almost by definition, lead to lower productivity. The cost of regulation may well reach into the hundreds of billions of dollars annually or beyond.[13] Of course, some regulation may be needed, but this can become excessive and generate more costs than benefits.

Concentrated Benefits/Disbursed Costs and Rational Ignorance

The quality of public sector decision making is distorted by the fact that when benefits of government action are concentrated among a relatively small proportion of the population, but costs are widely disbursed among all taxpayers, many projects are undertaken that would not otherwise survive objective scrutiny. "Pork barrel" projects are typically public works schemes benefiting thousands of people but paid for by millions. The beneficiaries see significant benefits per recipient from the project, so campaign hard for its enactment. Non-benefiting taxpayers who are paying for most of the project typically find its cost very low, so they are not likely to protest.

A hypothetical example demonstrates the point. Suppose the people of a community talk their influential congressman into slipping a new project into an appropriations bill. Let us say the project provides $200 million in benefits to the one million persons of the community receiving the improvement - $200 per person or $800 for a typical household of four. People in that community will clamor for the project, as the benefits are big enough to provoke serious lobbying. Suppose the project cost the 260 million American taxpayers $300 million - $1.15 a person or less than five dollars for a family of four. The costs are so small that the typical taxpayer is not going to expend time and resources fighting the marginally harmful project. The average taxpayer is "rationally ignorant" about the project. Yet the costs to society ($300 million) are greater than the benefits ($200 million), so the investment is clearly one with a negative return to society. Yet the asymmetrical lobbying on the project will typically lead to it being undertaken. This principle is at work literally hundreds, if not thousands, of times annually in various types of special interest legislation.

The Shortsightedness Effect

Many investments that raise productivity take several years to complete. The costs of the project come quickly, but the benefits largely accrue many years in the future. In the private sector, investments of this type are undertaken since firms know that such investment is vital to maximizing the present value of future profit streams. In the public sector, however, payoffs received even two or more years from now from expenditures made today are politically irrelevant, since congressmen must face re-election within a very few years of the date

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[13] Professor Vedder is completing a study for the Center for the Study of American Business at Washington University in St. Louis that demonstrates this point using time-series data on productivity and regulatory effort (as measured by spending on regulation). The tentative title is **Federal Regulation's Impact on the Productivity Slowdown**.

the decision is made to proceed with the expenditure. There is a bias, then, to make decisions that have immediate benefits and deferred costs, when in fact some of those decisions are socially undesirable, since the present value of those future costs exceed the value of the benefits. The costs, however, are largely disguised from the voters, while the benefits are obvious. Similarly, some worthwhile expenditures are not undertaken even where the present value of benefits exceed costs simply because the benefits are in the future and the political value of those benefits to existing congressmen are minimal.

Thus the political process promotes "shortsighted" decisions, and leads to such fiscal policy strategies as large deficit financing (spend today and derive political benefits financed in the future by disguised taxation). The shortsightedness effect is one factor in explaining the persistence of budget deficits. When new social programs are begun, typically they are structured so first or second year costs are moderate, but "out year" expenditures soar. Politicians than can claim "I helped get you new program A" and derive political benefits for programs that may have, net, greater financial costs than benefits.

An Empirical Evaluation of Government's Impact on Productivity

The preceding argument has emphasized the negative side of government activities. However, not all government actions are counterproductive. There are things that government can do that improve the functioning of the economy, such as providing for national defense, maintaining a system of laws that assist in settling contractual disputes and provide for the safety of individuals and their property, providing a basic infrastructure, and establishing a minimal safety-net for its citizens. In the strictest economic sense, the positive effects of government tend to reduce the costs of producing goods and services, thereby raising productivity and lowering prices. What is critical in evaluating the impact of the Federal government on the average productivity of labor is the net effect of its positive and negative contributions. When government is small, additions to it are more likely to improve the nation's economic performance. However, as it becomes larger and larger, it tends to stray off more and more into programs that produce the kinds of inefficiencies previously described. What this indicates is a systematic relationship between the size of the Federal government and the average productivity of labor. At low levels of government spending and activity, the contributions to enhancing levels of productivity are positive, but at high levels, they are negative.[14]

The availability of numerical data detailing levels of federal government expenditures, expressed as a percent of GDP, and the average productivity of labor allow a statistical evaluation of the suggested relationship between the size of government and the productivity of labor. To do this, we estimated a statistical relationship of the form:

$$(1)\ PR = a + bG - cG^2 + dT + e$$

where PR represents the annual average productivity of labor, T delineates the passage of time, G is federal government spending as a percentage of Gross Domestic Product, and G^2 is the square of the variable G. The variable T is included to control for the long term growth in the average productivity of labor. The statistical results are reported in Table 4. All of the independent variables are statistically significant at commonly accepted levels. Also, the signs of the variables indicate that the hypothesis that beyond some size growth in the magnitude of government adversely affects the productivity of labor is confirmed. Interestingly, the value of G beyond

[14] The relationship described here is an extension of the Armey curve concept explored in our earlier study for the Joint Economic Committee, **The Impact of the Welfare State on the American Economy** (Washington, DC: December, 1995).

which growth in government begins to exert its negative effects is a Federal government share of Gross National Product of 17.42 percent, almost exactly the same value found in our earlier analysis of the impact of government on real Gross Domestic Product.[15]

To firmly establish the quantitative linkage between the size of the Federal government and the compensation of labor, a statistical estimate of the productivity-compensation relationship is also reported (see Table 5).[16] As expected, on the basis of Figure 6, the average productivity of labor and real compensation are powerfully related. This indicates that the already observed effect of the size of government on labor productivity is directly transferable to real compensation, indicating that growth in the size of the Federal government beyond the optimal level of 17.4 percent has operated to reduce the level of real compensation per worker in the American economy.

Table 4

Regression Results, Analysis of Change in Average Output Per Hour of Labor Input
United States, 1947-1994

Independent Variable	Regression Coefficient	t-Statistic
Federal Government Expenditure as Percent of GDP	4.18	4.16
Square of Federal Government Expenditure as Percent of GDP	-0.12	4.18
Time	1.62	42.81

Note: Other regression statistics: Adjusted R^2 = .9942, D-W = 1.47, Arima Adjustment = (0,2).
Source: Authors' Calculations

Further insight into the magnitude of the impact of the growth of government on wage levels in the United States can be obtained by asking the question, "What would have happened if the size of government had remained stable at some lower level, as opposed to the increase reflected in the actual historical record. Making such an assumption permits calculating a hypothetical productivity and real wage series that then can be compared with the actual. A good point of departure for this purpose is the year 1965, at which time federal government spending stood at 17.6 percent of Gross Domestic Product, very close to the optimal level of Federal government spending as a

Table 5

Regression Results, Analysis of Relationship Between Productivity and Real Compensation Per Hour
United States, 1948-1994

Independent Variable	Regression Coefficient	t-Statistic
Average Output Per Hour of Labor Input	1.0068	517.47

Note: Other regression statistics: Adjusted R^2 = .9993. Since real compensation would be zero if average product of labor were zero, the regression equation is constrained to pass through the origin.
Source: Authors' Calculations

[15] See our **The Impact of the Welfare State on the American Economy**, Joint Economic Committee study (Washington, DC: Joint Economic Committee, 1995).

[16] This regression equation is constrained to run through the origin. The basis for this is the **a priori** expectation that at a zero level of average productivity of labor, real compensation would be zero.

Table 6

Comparison of Actual and Hypothetical Real Compensation Per Hour
United States, 1973-1994

Year	Hypothetical Real Compensation Per Hour (1973=100)	Average Real Compensation Per Hour (1973=100)
1973	100.0	100.0
1974	102.0	100.0
1975	104.0	100.1
1976	106.1	103.6
1977	108.1	105.3
1978	110.1	106.7
1979	112.1	106.9
1980	114.1	107.4
1981	116.2	107.0
1982	118.2	109.0
1983	120.2	109.7
1984	122.2	110.1
1985	124.2	111.7
1986	126.3	115.4
1987	128.3	116.3
1988	130.3	117.2
1989	132.3	116.1
1990	134.3	117.8
1991	136.3	119.4
1992	138.4	122.9
1993	140.4	125.1
1994	142.4	126.0

Source: Authors' Calculations

share of Gross Domestic Product that we have estimated. When the necessary calculations are made, the results shown in Table 6 (and displayed graphically in Figure 7) are obtained. Since our primary interest is in explaining the retardation of the growth in real compensation since 1973, the actual and hypothetical compensation series have been indexed on 1973 (=100). What we find is that holding the level of federal government spending constant at 17.6 percent of Gross Domestic Product since 1973 would have produced a level of real compensation in 1994 some 13 percent higher than what actually occurred.

The picture of how large government negatively influences the level of economic activity in the American economy is now clear. When government grows beyond the level that optimal for the economy, it introduces inefficiencies that increase the cost of producing goods and services and reduce the real returns to labor. The cumulative impact of these inefficiencies over a substantial period of time is immense. Using the actual estimates of compensation per hour in the non-financial corporate business sector and the data describing the average number of hours worked per week in the private non-agricultural sector, we have estimated the present value of the annual losses per worker (measured in 1994 dollars) of oversized government in the years since 1973 (through 1994). In 1994 alone, the total loss of compensation amounted to \$4132, some \$344 per month. Over a longer period of time, for someone who had worked the typical workweek and earned the typical compensation during those years, the present value of the cumulative cost of the excessive federal government totals \$71,200.

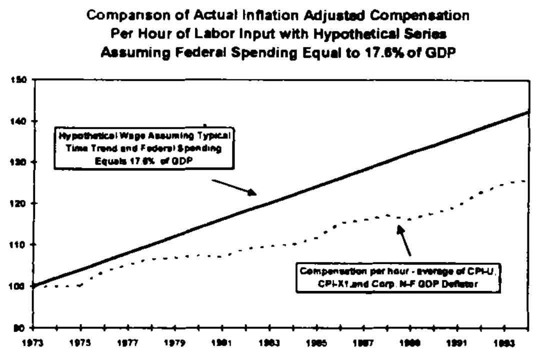

Figure 7

There also would be gains from the reduction in federal taxes that almost certainly would have followed in the wake of holding federal spending at 17.6 percent of GDP. During the period 1973-1994, federal government revenues averaged 18.7 percent of GDP. If the revenue share would have fallen by 1.1 percentage points (the difference between 19.7 and 17.6 percent) in this interval, the increase in after-tax compensation would have been about half the gain attributable to the productivity increases that would have ensued as the result of restraining government spending.[17] Increasing the $71,200 figure by fifty percent gives an estimate of $106,800, exactly the median price of a home in the United States in 1993.[18] Roughly speaking, an oversized government in the years 1973-1994 has cost the average worker the value of a typical home.

The Future of Real Compensation

What is done is done. The question that remains is, "What about the future?" "What can be done to rectify this situation in the years ahead?" The obvious answer is to impose restraint on federal government spending. Using the relationships we have developed, it is possible to estimate the marginal effect of restraining spending growth on levels of real compensation. Assuming 1994 levels of GDP and federal spending, restraining spending by $100 billion would result in about a 1.5 percentage point reduction in federal spending as a percent of GDP (from 22.0 to 20.5 percent). Using the statistical results reported in Table 4, this would produce an 0.8 percent increase in both productivity and compensation of workers. When that rate of increase is applied to the business sector total compensation data contained in the National Income and Productivity Accounts, a total increase in compensation of $26 billion is indicated. Thus, $100 billion of federal spending restraint would produce a $26 billion increase in total real compensation of workers, 26 cents per dollar of spending restraint.

Replicating an analysis reported in our earlier study of the impact of oversized government on GDP, we estimate that a dollar of spending restraint this year that is maintained over the following six years will generate $1.68 of additional total real compensation for workers.

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[17] The reduction from 1994 levels of federal spending to the 17.6 percent level would have increased the average output per hour of labor by 2.1 percent.

[18] **Statistical Abstract of the United States, 1994** (Washington, DC: Government Printing Office, 1995), Table 1208, p. 732.

CONCLUSION

Several striking conclusions emerge from this study:

1. The worst-case horror stories of declining real income payments to workers since 1973 are not true. When appropriately defined and deflated to take into account changes in price levels, there has been a meaningful increase, some 26 percent, in the real compensation package received by the typical worker for an hour's labor.

2. While there has been growth in real compensation per hour since 1973, the rate of increase has slowed perceptibly when compared with the pre-1973 post-World War II period.

3. Secretary of Labor Robert Reich's "excessive profits" explanation for the retardation of real compensation growth is contradicted by the available evidence.

4. The pattern of growth in real compensation over time almost exactly mirrors the behavior of the average productivity of labor. Consequently, growth in both real compensation and labor productivity slowed in the post-1973 era.

5. The average productivity of labor is significantly affected by the percentage federal expenditures are of GDP. Beyond a federal government share of GDP of 17.4 percent, additional spending impacts adversely on average output per hour of labor services employed. Of course, this translates into a similar impact on the real hourly compensation of workers.

6. If federal spending had been held constant at its 1965 share of 17.6 percent of GDP, and federal taxes adjusted accordingly, the present value of the gains to the typical worker over the period 1973-1994 would have been $106,800, an amount sufficient to purchase a typical home in the United States.

7. At present levels of federal spending and GDP, restraining federal spending by a dollar during the current year will yield an increase of 26 cents in total worker compensation. Sustaining that restraint over a seven year period would produce cumulative gains of $1.68 in total compensation.

What these findings strongly indicate is that spending restraint at the federal level is critical to enhancing the level of worker compensation in the United States. Every dollar of such restraint eliminates 26 cents of the deadweight burden imposed on workers by the inefficiencies created by a federal government that has become too large.

The authors, Lowell Gallaway and Richard Vedder, are professors of economics at Ohio University in Athens, Ohio.

Mr. GUTKNECHT. Thank you, Professor Gallaway. I'm going to have to run over and vote. Congressman Shadegg went over early, and he should be back in just a matter of minutes. So we will recess, hopefully, no more than about 5 minutes and come back to Mr. Wilson and then some questions. Thank you so much.

[Recess.]

Mr. SHADEGG [presiding]. Gentlemen, I want to apologize for that brief interlude and call back to order the hearing of the Subcommittee on National Economic Growth, Natural Resources, and Regulatory Affairs. I appreciate your indulgence in our absence during the vote.

And I believe, Mr. Wilson, we are to your testimony.

Mr. WILSON. Thank you. It's my pleasure to be here. Thank you for inviting me today. Let me say at the outset that the views I'm expressing are my own and not necessarily those of the Heritage Foundation.

With your permission, I'd like to submit for the record my prepared statement and a paper that I recently co-authored with Angela Antonelli on how to raise the take-home pay of workers without destroying jobs.

It details how Government, essentially, raises the cost of hiring and maintaining workers on their payroll and reduces take-home pay.

I'd, sort of, like to briefly summarize. Everybody is hungry. It has been a long morning, and I'd like to just, sort of, briefly summarize those points and then offer up a few recommendations.

The problem with stagnating wages is called, in part, but increasing Federal taxes, mandates and regulations that have driven a larger and larger wedge between the cost of labor to an employer and what those workers take home.

The previous panel very clearly articulated the problems, and the two gentleman here that preceded me clearly articulated the problems of regulations and how those increased the cost.

I'd like to talk about the direct cost, as opposed to regulations, which is more of an indirect cost on labor and businesses.

The hourly wage that employers pay is not what workers take home, nor is it the total cost of labor to businesses. To the hourly cash wage rate that businesses pay to workers, employers must also pay Social Security, Medicare taxes, Federal, State unemployment insurance taxes and Workers' Compensation premiums.

From the wages and salaries employees receive in their paychecks, workers must pay additional Social Security and Medicare taxes and Federal and State income taxes.

The difference between this cost to labor, cost of labor to employers—cash wages plus mandated taxes and benefits—and the take-home pay of workers, which is cash wages minus payroll and income taxes, is what I'll refer to as a tax wedge.

It has been growing, and it's liable to get larger if we don't do something about it. It's important to point out, I think, that legally mandated benefits, as Dr. Gallaway pointed out, such as unemployment insurance, Workers' Compensation are not free to the worker, as many employees assume.

A range of studies indicates that, on average, about 88 to 85 percent of the cost of employer-paid Government-mandated benefit taxes are shifted to workers in the form of lower real wages.

In 1995, the Bureau of Labor Statistics reports that it costs all private industry employers an average of $17.10 per hour to hire and keep workers on their payrolls, and this doesn't count the cost of recruiting and training, initially training these workers.

After the cost of Government-mandated benefits and taxes and optional benefits that employers pay are deducted, workers take home an average of about $9.84 an hour, or 42 percent less than the total expense of employing them.

Now, not all of this is Government-generated, loss to the employee. Nineteen percent is an optional fringe benefit that's provided to employers that are paid on their behalf.

However, the average, the total tax wedge, the total cost of Government, direct Government taxes and mandated benefits to the employee is $4 an hour, or 23 percent of their total compensation, and that doesn't even include the gas tax, the retail sales tax, and the property tax that they have to turn around and pay out of their after-tax take-home pay.

In 1995, it costs a typical employer at least $4.76 an hour to hire a minimum wage worker because of these additional Social Security, payroll taxes that I mentioned before.

That average minimum wage worker takes home of that $4.76 only $3.73. Even counting the earned income tax credit, the government takes $1.03 away from a minimum wage worker per hour.

In addition, in recent years, there has been a significant increase in the cost of mandated benefits and mandated benefits in general.

In 1994, the cost of Government-mandated benefits accounted for 8.9 percent of all employer payrolls, according to the U.S. Chamber of Commerce in a survey of employee benefits that they do on an annual basis, as an increase of 3.5 percent in 1951. It went to 6.3 percent in 1971. It now stands at 8.9 percent.

Government taxes and fees are taking an ever increasing bite out of personal income. In 1994, Federal, State and local governments took an average of $2,800 from every person, an increase of 150 percent since 1959.

If Congress proceeds with the proposed 90 cent increase in the minimum wage, it will cost consumers and workers about $2.2 billion per year as the higher costs of entry level jobs are passed on through higher prices and lower real wages.

The minimum wage, raising the minimum wage is not free. There is a cost to it. It's about $2.2 billion a year. And if you agree with the former chief economist of the U.S. Department of Labor, Alan Kruger, which I don't necessarily agree with, that there is no or there is only a negligible employment effect, then it has to come from either two places, profits or higher prices.

Most of the minimum wage employers out there, employers that hire the minimum wage workers are not the Fortune 500 companies with their million dollar CEOs. They're the small businesses, as our previous panel indicated.

They're working very long hours, and their profit margins are not very high. I suspect that they will be required to either lower employment, which is, obviously, one adjustment, or raise prices, or some combination of the two, which is the most likely case.

Going on further, the Medicare program is also on the brink of insolvency. To put it on sound financial condition without reforming or improving the way the program operates could mean adding as much as 3.5 percentage points to the payroll tax right now.

So we're looking on into the future. Mandated employer taxes and benefits costs have increased and are likely to increase. Stagnating take-home pay is not caused by greedy employers.

Businesses do not, indeed cannot keep down the wages of their employees. Employers as well as employees operate within a competitive labor market in which wages broadly reflect the productivity of those workers less the cost of Government-imposed mandates, taxes and regulations associated with employing those workers.

The more productive a worker is, the more that work will be paid, but the larger the Government mandate and tax wedge becomes, the less cash workers take home.

I'd like to turn to some recommendations. Obviously, one of these is to cut payroll taxes. They need to be cut across the board not for just minimum wage workers, not for low income workers, for all workers.

We need to cut the capital gains tax. Study after study has shown that lowering capital gains will increase investment in future productivity and raise the real wages of all workers in the United States.

We need to enact significant regulatory reform. I think that's quite obvious, given the previous panel at this point in time, the testimony of Dr. Hopkins and Dr. Gallaway.

Congress should strengthen White House oversight of the executive branch agencies. They need to establish a set of principles, including cost-benefit analysis, to guide regulatory decisionmaking.

They need to establish a regulatory budget. They need to require Federal agencies to review all existing regulations to get the junk off the books that's on there right now and to ensure that they meet sound regulatory principles.

Last, I'd like to recommend that we need to improve the skills of the work force, improving basic education through school choice, strengthening core curriculum, enabling local educators to improve discipline and set high expectations of their students.

Thank you, Mr. Chairman. I'd be happy to take any questions.

[The prepared statement of Mr. Wilson follows:]

United States House of Representatives
Committee on Government Reform and Oversight, Subcommittee on National Economic Growth, Natural Resources, and Regulatory Affairs

May 16, 1996

Testimony of Mark Wilson

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Mr. Chairman, Members of the Subcommittee, thank you for inviting me here today to comment on the impact of government regulations, mandates, and taxes on the cost of hiring employees and workers' take-home pay. Let me say at the outset that the views I am expressing today are my own and do not necessarily reflect those of The Heritage Foundation.

With your permission, I would like to submit for the record my prepared statement and paper that I recently co-authored with Angela Antonelli on how government raises the cost of hiring workers and reduces take-home pay, briefly summarize its two main points, and provide some recommendations.

1. The problem of stagnating wages is caused in part by increasing federal taxes, mandates, and regulations that have driven a larger and larger "wedge" between the cost of hiring employees and workers' take-home pay.

The hourly wage that employers pay is not what workers take home, nor the total cost of labor to businesses. To the hourly cash wage rate businesses pay workers, employers must also pay social security/medicare taxes, federal and state unemployment insurance taxes, and workers' compensation taxes. From the wages and salaries employees receive in their paychecks, workers must pay additional social security/medicare taxes, and federal and state income taxes. The difference between this cost of labor to employers (cash wages plus mandated taxes and benefits) and the take-home pay of workers (cash wages minus payroll and income taxes), is the tax wedge.

Moreover, legally mandated benefits, such as unemployment insurance and workers' compensation, are not "free" to the worker, as many employees assume. A range of studies indicates that, on average, the cost of 88 percent of all employer-paid government mandated benefit taxes are shifted to workers in the form of lower real wages.

- In 1995, it cost all private industry employers an average $17.10 per to hire and keep workers on their payrolls. After the cost of government mandated benefits, taxes, and optional benefits are deducted, workers take home an average $9.84 per hour, 43 percent less than the total expense of employing them. The total tax "wedge" cost workers an average $4.00 per hour, or 23 percent of their total compensation.

- In 1995, it cost a typical employer at least $4.76 per hour to hire a minimum wage worker. After the cost of government mandated benefits and taxes ($1.03) are deducted, however, an average minimum wage worker takes home only $3.73 per hour, or 22 percent less than the total expense of employing them, and 12 percent less than their cash wage of $4.25.

In addition, in recent years there has been a significant increase in mandated benefits, and it stands to get much worse. For example,

- Over the years, more and more mandates and higher and higher taxes have increased the cost of hiring workers. In 1994, the cost of government mandated benefits accounted for 8.9 percent of total employer payrolls, up from 6.3 percent in 1971 and 3.5 percent in 1951.

- Government taxes and fees are taking an ever-increasing bite out of personal income (Chart 2). Although, personal income per person increased 121 percent from 1959 to 1995, government taxes and fees paid per person increased 155 percent over the same period. In 1994, federal state and local governments took an average $2,800 (in 1992 dollars) from every man, woman, and child.

- If Congress proceeds with a proposed 90 cent increase in the minimum wage, for example, it will cost consumers and workers about $2.2 billion per year as the cost of entry level jobs is passed on through higher prices and lower real wages. It also will cause employers to create over 200,000 fewer entry level jobs each year until 1999.

- The Medicare program is on the brink of insolvency. To put it on sound financial condition, without reforming and improving the way the program operates, could mean as much as a 3.52 percent increase on top of the current 2.9 percent Medicare payroll tax. Workers earning $45,000 per year would have to pay an additional payroll tax of $1,584 per year.

Stagnating take-home pay is not caused by greedy employers. Businesses do not -- indeed, cannot -- unfairly keep down the wages of their employees. Employers, as well as employees, operate within a competitive labor market in which wage rates broadly reflect the productivity of workers -- *less* the costs of government-imposed mandates, taxes, and regulations associated with employing a worker. The more productive a worker is, the more that worker will be paid. But the larger the government mandate and tax wedge becomes the less cash workers take home.

2. Taxes and mandated benefits are not the only government policies that drive a wedge between the cost of hiring an employee and that employee's take-home pay. Regulations also increase the cost of employing workers.

For example, environment and workplace safety regulations impose costs that take the form of such things as compliance expenditures for equipment purchases and training, time lost due to paperwork requirements, and attorneys fees incurred in regulation-related litigation. For the smallest businesses, the costs of tax compliance and payroll recordkeeping are the largest components of their regulatory burden.

Regulation imposes the heaviest burden on small and medium sized businesses because they find it harder to spread the high overhead costs of paperwork, attorney and accountant fees, and staff time needed to negotiate the federal regulatory maze.

- For firms with fewer than 20 employees, the regulatory costs per employee is estimated to be about $5,500. For the largest firms (those with more than 500 employees), the cost is about $3,000 per employee. Unfortunately, Congress has responded to the disproportionate burden on small business by exempting different sizes of companies from different regulatory statutes. The effect of this approach has been to discourage companies near an established threshold from hiring new employees.

- The business regulatory burden also varies considerably by industry. For example, the average cost of regulation per employee in the manufacturing industry is in the range of $5,000 to $7,000, where regulatory costs are the highest, while it is in the range of $2,000 to $3,000 for the service industry, where regulatory costs are the lowest. These average costs are equal to a range of approximately $1.00 to $3.00 per hour per worker.

Although regulation imposes costs on businesses, ultimately they are passed on to individual Americans often through lower wages. Moreover, mandated requirements, such as family and medical leave, directly affect an employer's decisions about whether and when to hire a worker, which worker to hire, how much cash to pay the worker, and how long to keep that worker. The rise in mandated labor costs paid by employers is one of the most important forces leading companies to lay off workers, as well as the utilization of part-time, temporary, and contract labor.

Recent studies also suggest that in addition to the costs of compliance with regulation, there are longer-run costs in the form of reduced productivity. When a business must devote resources to implementing regulatory mandates, those resources are used in a less efficient manner because firms are forced to use more costly, less productive, methods of production. Since productivity and workers' pay and benefits rise together, government regulations are therefore directly responsible for some part of the slowdown in wage growth and take home pay.

RECOMMENDATIONS

Congress and the Administration should focus on policies that will increase wages and job opportunities for Americans by improving labor productivity and reducing the cost of employing workers. Specifically, Congress and the Administration should:

Cut payroll taxes. Taxes and government mandated benefits costs the average worker over 21 percent of their total compensation, 13.8 percent for minimum wage workers. Instead of imposing more mandates, such as increasing the minimum wage, cutting payroll taxes will directly increase take home pay.

Cut the capital gains tax. The U.S. tax code punishes capital investment by taxing investment income more than once. Twice by taxing corporate and individual income, and then a third time by taxing capital gains. Lowering the capital gains tax will increase investment in the U.S. and provide an incentive for both American and foreign firms to put their capital to work here with American workers. A capital gains tax cut also will make more venture capital available for emerging technologies and for research and development that will improve future productivity.

Enact significant regulatory reform. The explosion of new regulations since 1988 has raised the cost of labor and capital, created barriers to the formation of new companies and jobs, and raised the cost of employing Americans. This higher cost of employment in turn means that in a competitive economy, the return to labor in the form of wages is reduced. The regulatory burden needs to be rolled back, not only to allow wages to rise, but also to decrease the cost of hiring workers. Congress should strengthen White House oversight of executive branch agencies; establish in statute a set of principles, including cost-benefit analysis, to guide regulatory decisionmaking; establish a regulatory budget; and require federal agencies to review existing regulations to ensure that they meet sound regulatory principles.

Increase the skills of the workforce. What is needed is fundamental change aimed at improving basic education through school choice, strengthening core curricula, and enabling local educators to improve discipline and set high expectations. Congress also should consider tax-deferred or tax-free education savings accounts similar to individual retirement accounts, or enabling states and individuals to use lump sum unemployment insurance benefits for education and training.

Thank you, Mr. Chairman. I will be pleased to answer any questions you may have.

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Mr. SHADEGG. Thank you. Let me start briefly by asking Professor Gallaway, your study that you conducted with Professor Vedder before the Joint Economic Committee last month, is that the study that produced this?

Mr. GALLAWAY. Yeah. That's one of the studies. It's a series of studies that we've been doing exploring an idea advanced by the House majority leader, the concept of an RV curve, implying that there are optimal levels of Federal spending.

Mr. SHADEGG. Senator John Kyl, whose seat I took, is a great proponent of a spending cap on Government spending that would be written into the Constitution which would say that spending by the Government couldn't go above a certain level, tying it to Gross Domestic Product.

My understanding of your testimony, at least what I've been able to gather, is that were we to have done that America would be in dramatically better shape, including workers at every wage scale. Is that the essence of what you're telling us?

Mr. GALLAWAY. The data we've used have been average compensation levels in general, not broken out by particular levels of wages.

Mr. SHADEGG. Maybe you should explain what the implications of the chart are.

Mr. GALLAWAY. Well, what we found in the statistical analysis was that when Federal Government spending gets much beyond 17½ percent of GDP, it starts exerting a very substantial negative drag.

Mr. SHADEGG. If I could just interrupt you right there, we're well above 17.6 at this point.

Mr. GALLAWAY. The 1994 level was 22 percent. I think we may be down slightly below that now. We're well above it now, and the extent of the drags roughly lead to this.

At current levels of spending every time that Congress votes for another dollar of spending it exerts a 38 cent negative effect on GDP, 26 cents on the compensation of workers for every extra dollar at this point.

Working with those numbers, we constructed, did some simulations to show what the compensation of workers would be if we had held Federal Government spending at 17.6 percent of GDP since 1973.

And by the time we get to the present we find that both productivity, the average productivity of workers, which is what drives the wage rate, both of productivity of workers and wages would be 13 percent higher.

Mr. SHADEGG. Is it fair to say, then, that the anemic nature of our economy at this point, growing at something around 2 percent, can you conclude from what you've studied that we could be, in fact, growing at a more dynamic rate if we could, in fact, check Government spending, Federal Government spending?

Mr. GALLAWAY. I have no argument with that interpretation.

Mr. SHADEGG. Thank you very much. Professor Hopkins, you brought forward some testimony with regard to cost-benefit analysis and a study done by Robert Hahn which estimates that any reasonable cost-benefit test applied to a great deal of environmental regulation, that regulation would fail.

Are you familiar with how Dr. Hahn came up with that estimate?

Mr. HOPKINS. Yes. Dr. Hahn, essentially, reviewed the economic analyses provided by the regulatory agencies themselves.

Even when you take the agencies own data on the benefits they anticipate from particular regulatory decisions and the costs of compliance that they anticipate, it still turns out that about half of the new regulations over the past 5 or 6 years have flunked that test. They're adopted even though they lessen economic efficiency.

Mr. WILSON. If I might, I'd like to point out that that really calls for the need to have these types of studies that are done by the agencies peer reviewed by others in the academic community before these regulations are allowed to be published as final.

Mr. SHADEGG. It amazes me that only inside the beltway surrounding Washington, DC, is the notion of risk assessment or cost-benefit analysis at all controversial.

Every single human being, every time they wake up in the morning and make a decision whether to put their foot out of the bed and down on the floor, makes a cost-benefit risk assessment analysis, and they do that as they go through every step of the day, including getting in their car and driving to work and all of that.

As they bite into their Cheerios, they make a cost-benefit risk assessment analysis, but that's too controversial a notion for us to apply to regulatory rulemaking. I'm amazed by it.

Mr. Wilson, I want to ask you, I think there is a common perception out there in America, trying to be sold to Americans and maybe also being accepted to some degree that the fact that wages seem to have stagnated while corporate profits are going up, at least according to the books, quite dramatically is as a result of corporate greed.

Do I understand you to say that it indeed is not corporate greed, but it is rather this whole morass of a regulatory burden imposed on the economy, or is that too much of a simplification?

Mr. WILSON. It's in part caused by the Federal Government. It's not all that's going on. Wages appear to be stagnating as corporate profits are rising, but it's not the total pay the workers receive.

You have to think in terms of compensation, benefits plus mandated taxes, total cost of labor. If one looks at profits and compensation, they track fairly closely.

They don't sit right on top of each other, but when profits rise, compensation rises. When profits level off, compensation levels off. If it declines, it declines. They track fairly well. There is a little bit of a lag, but they do track fairly well.

Most Americans, when they get their pay stub, only see what they pay. They're not aware of the cost, the hidden cost, of Government with the regulatory burden as well as the direct payroll taxes that are paid on behalf of them by their employers.

If an employer paid their workers in cash and then before that worker left was required to pay $100 out of whatever the amount is out for every State unemployment insurance, Federal unemployment insurance, Medicare, Medicaid and then take the rest home, I can guarantee you that we would not have as large a Government as we have today.

And it's growing, unfortunately, at this point in time, and it will continue to grow unless we can turn it around.

Mr. GALLAWAY. Congressman Shadegg, could I add something on the corporate profit thing?

Mr. SHADEGG. Certainly.

Mr. GALLAWAY. In the same study in which that chart came, we reported some statistical results which indicated just as Mr. Wilson said.

With a one period lag, corporate profits, changes in corporate profits and wage rates are positively related. When corporate profits go up this year, wage rates are going to go up next year and, since incidentally, so is employment. So that the notion that wages are stagnating because corporate profits are high is, to put it politely, a canard concocted by the Secretary of Labor.

I would also point out that corporate profits, as a share of national income, were much higher in the 1960's than they are today. The long-term trend in corporate profits as a share of national income has been downwards in the post-World War II period.

Mr. SHADEGG. I thank you very much for that information. I was unaware of that, and I think most Americans are unaware of it. They're of this belief that they're at record all-time highs.

With the indulgence of my colleague, let me just make one quick comment. My belief is that if we can't succeed in passing a law to require that all employees be paid as though they were independent contractors and have to write checks back for each of these Government services—which is one of the things I'd like to see us do, and I believe we'd have a revolt over the size and scope of Government overnight—one of the ideas I thought we ought to do is simply require that that be the law for every Member of Congress and for all congressional employees.

If you just did it for that group, I think you would suddenly see a change of attitude here. Let me ask, again with brief indulgence, if you would each either comment on this or tell me how I might ultimately get an answer.

I was at a breakfast this morning where we were discussing various policies of the U.S. Government and the issue of tax cuts and the whole question of balancing the budget.

I made the point that I felt it was critical that we cut taxes and get this economy growing at a pace faster than the 2 percent or so than it's growing right now.

I commented that it used to grow at a pace of about 4 to 5 percent and that the Chilean economy is growing at 7 percent.

One of my colleagues said, "Well, the Chilean economy is growing at 7 percent only because they have privatized Social Security." I doubt that. I suggest that they're growing at a dramatically better rate in part because they have privatized Social Security and probably also because they have not created the huge regulatory war tax burden that we have beyond the privatization of their Social Security system.

I wonder do any of you have any information on that topic or would know where I would go to get an answer?

Mr. GALLAWAY. Do you want to go first, or shall I?

Mr. HOPKINS. Just a brief comment. I have not looked with any care at the Chilean experience, but my impression is that they have substantially deregulated that economy and have substantially less regulatory burden than most other Latin American countries, and that would help to contribute to their growth. So I suspect you're right.

Mr. SHADEGG. Professor Gallaway.

Mr. GALLAWAY. I don't have the specifics of Chile at hand, but I've just been looking at, in general, international comparisons.

And the literature on that more and more is showing a very powerful negative effect of the size of Government on economic growth.

For example, if you relate just the percentage that taxes are of GDP in countries to a, sort of, longer term growth rate, you'll find that relatively low tax countries will have relatively high growth rates.

I guess the only thing that calls to mind is our acceptance of 2 percent, 2½ percent growth as somehow being vigorous and dynamic.

It calls to mind the 1960 Presidential election campaign in which Richard Nixon raised the issue of economic growth and made the fatal mistake of producing the first offer in which he said, "I'll give you 4 percent economic growth." And John Kennedy came back and said, "Four percent? Hell, I'll give you 5."

It just says something about what the expectations were at that time, and now we have people talking about how great, this is how dynamic the economy is with this 2½ percent growth, which is 30 percent below the long-term historic growth rate in the U.S. economy of 3.6 percent, which held up for 200 years.

Mr. SHADEGG. Thank you very much. Mr. Gutknecht.

Mr. GUTKNECHT. Thank you, Mr. Chairman. I want to thank all the panelists. Personally, I've been a fan of all of you for quite some time. Professor Hopkins, you are widely quoted on this committee, whether you know it or not. We thank you for all the work that you have done relative to regulatory reform.

Earlier, Mr. Shadegg said that everywhere outside of the beltway risk versus benefit analysis made perfect sense. I would have to correct you. I have been to a couple of college campuses back in my home State where I have been questioned rigorously about that whole issue, whether or not that was good sense or not.

It leads me to offer this observation. A couple of the earlier people who testified, and I think we frequently say, when we talk about some of these regulations, that the people who originally started down that path did so with the best of intentions.

And it's interesting how people who now want regulatory reform are willing to acknowledge that the people who got us into this morass in the first place so that in order to start a business today you have to comply with 39 different sets of regulations and forms from the Federal Government alone, we always say that they got us into this situation with the best of intentions.

But the interesting thing to me is that now that we're trying to do something to reform that, whether we're talking about reforming tort liability, whether we're talking about other regulatory reform, cost versus benefit analysis, the interesting thing is the other side, the people who got us into this mess, always question our motives.

I mean, if you listen to the debate on the House floor. If you listen to 1 minute special orders, if you listen to what happens on Nightline and all of the news talk shows and so forth, our motive is simply because we want to help our rich friends.

And frankly, one of the benefits, at least, of these hearings has been to demonstrate that a lot of the people that we're really talking about, the ones who bear the brunt of this regulatory environment that has been created are not the big, fat rich business guys, you know, the guys making seven figures living in big Manhattan apartments.

We're really talking about people who work at the local drycleaner shop and the people who manage the local Standard Oil station and so forth.

One of the most frustrating things—I have two real frustrations about this whole debate about regulatory reform. The first is that no matter what we try to do our motives are questioned, and that's something there is nothing you can do about.

But the second thing is that our adversaries in this debate are not bothered by the facts. They do not allow the facts to get in the way of their particular point of view.

So you have been extremely helpful. I guess my question for all of us, what can we do from our perspective, and this is from my frustration, to do a better job of getting the facts out to the American people of what the real costs of regulation are?

I think as a society we bought into the notion even on the minimum wage. Eighty percent of the American people think we ought to raise the minimum wage even though 75 percent of them don't know what it is.

I think there is this notion that somehow by Government fiat we can give everybody a pay raise and that there is no consequence to that.

And the same is true with an awful lot of our regulations. The American people seem to have bought into the notion that there is not a consequence to all of these endless regulations.

It is so frustrating to me because we're constantly looking for common sense. If you have any advice as to how we can do a better job of getting the facts out to the American people.

I do believe, and I quote Jefferson often. I quoted him yesterday, and I'll quote him again. He said, "Give the people the truth, and the Republic will be saved."

The problem we have is getting the truth to the American people, because if they understood the tremendous cost of regulation, the tremendous cost of taxes, the tremendous cost of just changing the minimum wage 50 cents or $1 an hour, whatever it happens to be this time, how can we do a better job of getting the American people the truth?

Mr. WILSON. Let me go first on that. Well, first of all, I think it's important to get out of Washington to town hall meetings, to actually get out and communicate as much with the public as possible, to communicate these ideas as much as possible.

Mr. GUTKNECHT. So you don't think we can get it out through the nightly news?

Mr. WILSON. No. This is too isolated, too insulated inside the beltway here. The other thing is that I think we need to actually try to encourage local businessmen, small businessmen, those folks that only have one or two establishments, four or five employees and one establishment to write letters to the editor, to write stories, to try to do these kinds of things in the local newspapers to try to get that message out.

The first panel here, essentially, that was here, these people told very eloquent stories. If that could be communicated as effectively in letters to the editors in some of the local newspapers, that would, perhaps, help.

I think, to the extent that we can encourage employers to modify their payroll forms voluntarily, of course—I'm not advocating any sort of mandate here—so that employees are more clearly aware of the taxes, the mandated benefits that they pay on top of the taxes that the employee pays before they even take home that paycheck, I think that that will help.

Mr. GALLAWAY. I think part of the problem is that big business doesn't mind this stuff. Look at Tom's numbers. What were the regulatory costs per worker for a small business? Almost twice what they were for a big business.

Big business people like this, their economies of scale, their lawyers and so on, and it keeps little businesses from becoming big businesses.

Now, asking me how can you get the truth out, I can't get it out to 19- and 20-year-old undergraduates, and I'm supposed to know something about how to teach those people.

Mr. HOPKINS. Congressman, I agree completely with your comments and share your concerns and having nothing terribly profound to offer but just one thought.

That is we've had on the books now for well over a decade Executive orders issued by administrations of both parties that there must be a labeling of major new regulatory initiatives with costs and benefits.

That Executive order is sometimes complied with more effectively and thoroughly than others, but nonetheless, a track record or the basis for a track record has existed.

And I think it would be helpful if the Congress were to ask the administration to provide an annual story. Since they have been collecting these analyses of costs and of benefits every year of every major regulation since 1981, I think an annual accounting of what are the costs that are being imposed this past year and how do they stack up against the benefits.

That's just an accountability question. That's just providing facts. That's not saying we're going to use this information as an absolute go, no-go criterion for issuance of regulation.

I think there is a vast contribution that could be made by simply publicizing information about the effects of these actions and then later on worry about control mechanisms that will actually use that.

You at least can't be accused of trying to poison children in the streets because of holding up regulations. All you're asking for is a clearer accounting in a consistent aggregate annual fashion of these costs and benefits.

Mr. WILSON. Including the paperwork burdens.

Mr. GALLAWAY. One other thing. I don't know if it's particular germane here, but which I think might be useful is every regulatory act should have a sunset provision in it.

To just demonstrate the beauty of Sunset provisions, this country was saved from disaster in 1946 by Sunsetted laws and regulations, all the rules that we put in during World War II.

After the war, there was the great debate should we relax the rules. Bob Taft wanted to ease up on them. Harry Truman wanted to keep them where they were. Truman won the political debate, and Taft's forces weren't able to override his veto of regulation easing legislation.

This was in late June 1946, and the President got up on July 1, 1946 and looked around and found that he didn't have any regulations because they had been sunsetted.

Mr. GUTKNECHT. I think you've offered some excellent advice. I see my time has expired. The one thing that is showing in the advice of the town meetings, I have had 62 town meetings back in my district, and frankly, they're very constructive for me, I think, and for the constituents as well because we do hear from real people about real problems. And generally speaking, the local press is pretty much obliged to report those stories. I think it starts to bring home the dimensions of the problem, and it localizes.

Mr. WILSON. Personalizes it as well.

Mr. GUTKNECHT. And personalizes, that's right.

Mr. WILSON. These are people that everybody knows in the community.

Mr. GUTKNECHT. Well, the one thing that's showing up in our polling and in our town meetings and everywhere is there is an American anxiety, and they don't understand that there is this consequence out there to higher taxes and more regulations and more bureaucratic burdens.

But they do understand it. I mean, they don't make the correlation, they don't make the connection yet, but they understand that they're working harder and keeping less.

In fact, somebody around here coined a phrase, "It's the paycheck, stupid." And I hear this in some of my town hall meetings and so forth.

Folks who work in factories and folks who work in offices and so forth, they understand that it's more difficult today for them to take their kids to a baseball game.

It costs more for them to take their kids to the county fair, to ride the rides and buy the bratwurst and everything. And again, they don't quite make the connection, but at the end of the week they're working harder, and they have less of what they've earned to spend on things that they used to be able to buy.

They want to go out and buy a new pickup truck, and they realize that they're paycheck went up 2½ percent. Their taxes went up 3 percent, and the price of that pickup truck went up 6 percent.

They've got a youngster getting ready to go to college, and all of a sudden they have real sticker shock and they realize how much it costs to send a kid to college nowadays.

So there is a genuine American anxiety out there. They haven't quite made the connection yet. Folks like you and folks like us I think can help them at least get the facts.

So my concluding admonition or request to you is that you will continue to provide this subcommittee and this Congress and more importantly this member with the facts, because facts are stubborn things.

In this debate, as I said, it's not so much right versus left. It is right versus wrong, and frankly, we've been on the wrong track for a long time as it relates to how we deal especially with small businesses.

We're doing our best to turn that around, but we're finding that Washington resists change even more than we thought. Thank you so much for coming.

Mr. SHADEGG. Gentlemen, I just want to conclude by also thanking you for coming. You are all admired on this committee at least by members on our side of the row.

I think that when you mentioned how difficult it is to get this point across even to 18- and 19-year-old and 20-year-old students in your classes, it is a mystery to me that there is so little understanding of economics and so little appreciation for what we are doing to this country.

I commented earlier we formed this country to get away from an all-powerful central government, a king, and now we're right back at that same situation.

I have faith in the American people. I think we are slowly getting the message out. I do think this coming election will be a referendum on that.

And I appreciate the facts that you bring forth because my opinion is my opinion. A minority member's opinion is his opinion or her opinion, but with the information you bring forward, we can, hopefully, get the message out.

I do want to comment that we held up this rather large stack of materials which are all the forms that have to be filed.

I don't think it's clear in the record, but I want to make it clear in the record this stack, which is about three-quarters of an inch thick, consists of the Federal forms that are required to be filed to start a business in any State in the United States if you have just one employee.

So you decide to form business. You're only going to have one employee. You're going to live up to all of the State requirements and regulations.

There are this stack of Federal forms to start that business, and there are 39 separate Federal forms if you have one employee.

Is it any wonder that we have a country that has grown to have a growth rate of 2 percent, and we think that's marvelous.

I thank you for coming and for your testimony, and with that, I declare this meeting concluded.

[Whereupon, at 1:20 p.m., the subcommittee was adjourned.]

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