

As Prepared for Delivery:

Regulation: Looking Backward, Looking Forward

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As you may have noticed, the national debate over regulation has become unusually politicized and polarized. One of our main efforts in the last years has been to go beyond soundbites and slogans and to focus on evidence and data – to ensure that regulation is empirically informed.

The plea for empirical foundations may seem obvious, a little like a plea for sunshine rather snow. But think for a moment about *Moneyball*, the best-selling book and Oscar-nominated film about Billy Beane, who worked with statistician Paul DePodesta to bring the Oakland Athletics into the top-tier of baseball teams, and in a short time transformed baseball itself, by substituting empirical data for longstanding dogmas, intuitions, and anecdote-driven judgments.

Consider this exchange:

“The guy’s an athlete, Bill,” the old scout says. “There’s a lot of upside there.”

“He can’t hit,” says Billy.

“He’s not that bad a hitter,” says the old scout.

“Yeah, what happens when he doesn’t know a fastball is coming?” says Billy,

“He’s a tools guy,” says the old scout . . .

“But can he hit?” asks Billy.

. . .

Paul reads the player's college batting statistics. They contain a conspicuous lack of extra base hits and walks."

"My only question," says Billy, "if he's that good a hitter why doesn't he hit better?" . . .

Over and over the old scouts will say, "The guy has a great body," or "This guy may be the best body in the draft." And every time they do, Billy will say, "We're not selling jeans here," and deposit yet another highly touted player, beloved by the scouts, onto his shit list.

For a long time, those thinking about regulation have been a bit like scouts in the era before Billy Beane. Scouts said that someone is "a tools guy," or that he "has a great body." Those favoring or opposing rules make analogous claims. "It won't cost a penny," or "ten years ago, the following happened," or "the industry will completely shut down." Regulatory systems need their own Billy Beanes and Paul DePodestas, avoiding anecdotes and intuitions, and instead carefully assessing what rules will do before the fact and testing them after the fact.

In these remarks, I will focus on four new directions in the last three years. They are closely related, in the sense that each of them is designed, in an economically difficult period, to ensure that regulation is empirically informed, that it delivers significant economic and other benefits, and that it does not compromise growth and job creation. I might be able to make a few announcements in the process.

- **The regulatory lookback**, designed to catalogue the effects of existing rules, to streamline them, and to eliminate those that are not justified.
- **New requirements for promoting public participation and requiring quantification**, designed to ensure that regulation is empirically justified in advance.
- The increased interest in **eliminating unjustified barriers to trade and exports and using international cooperation to promote economic growth and job creation.**
- The **use of simple, low-cost, noncoercive, empirically informed tools**, especially disclosure requirements

Each of these ideas is a response to a particular problem, associated not only with the current economic situation, but with longstanding difficulties in regulation.

Of course it is true that people's values differ, and in some cases, the relevant values will lead in a certain direction even if the evidence is clear. What I want to emphasize here is the opposite possibility, and the neglected one – that when the evidence is clear, it will often lead in a certain direction even there are differences with respect to underlying values.

If, for example, a regulation would save a lot of lives and cost very little, people are likely to support it regardless of their party identification; and if a regulation would produce little benefit but impose big costs on real people, citizens are unlikely to favor it, regardless of whether they like elephants or donkeys. At least this is so if we engage on the facts.

Now for some details.

For over three decades, the primary role of OIRA with respect to regulation has been twofold:

- To oversee an interagency process, so as to promote coordination and exchange of views. It is important to emphasize that this is an interagency process, which OIRA convenes, with a great deal of input from multiple offices within the government. For example, contributors include the Council of Economic Advisers and the National Economic Council on economic issues; the United States Trade Representative on trade issues; the Office of Science and Technology Policy on scientific issues; White House Counsel and the Department of Justice on legal issues. Legal issues often play a central role in the review.
- To ensure careful analysis of consequences, with cost-benefit analysis. One goal is to ensure that to the extent permitted by law, the benefits justify the costs, in accordance with the principle of “look before you leap.”

These two roles have been in place since the Reagan Administration, and they have become a defining feature of American administrative law. They have bipartisan support. It would be most surprising if a future President were to abandon them.

In this Administration, we have placed a great deal of emphasis on careful analysis of costs and benefits.

Smart regulations save lives. For example, the number of deaths on the highways is now down to its lowest level in sixty years. This is an extraordinary achievement,

produced not only by the commitment and creativity of the private sector but also by educational and regulatory initiatives from local, state, and national governments. In areas that include food and workplace safety, clean air, energy efficiency, and investor protection, well-designed regulations are preventing tens of thousands of premature deaths and hundreds of thousands of illnesses and accidents -- and savings billions of dollars.

Under the President's direction, we have issued rules, in our first three years, with over \$91 billion in net benefits – over 25 times the corresponding figure in the first three years of the Bush Administration, and over six times the corresponding figure in the first three years of the Clinton Administration.

Now let me turn to the new directions.

The Regulatory Lookback

The problem: Rules are placed on the books, often for good reasons. They accumulate. The original reason for some of them vanishes. What made sense once no longer makes sense, maybe because of technological change, maybe because of what has happened elsewhere in the system. Rules may refer to nations that no longer exist and to technologies that are obsolete. They may impose requirements that are now also imposed by the states. They may produce unintended harm. The original analysis of costs and benefits may turn out to be wrong; retrospective analysis may reveal opportunities for streamlining or instead expansion. Redundancies and paperwork burdens mount. A particular problem is the rise of cumulative burdens, stemming from the aggregation of rules that may make sense in individual cases, but that when taken as a whole, are not easy to justify.

Retrospective analysis has long been recommended by those interested in empirical assessment of regulations, including Michael Greenstone, former chief economist at the Council of Economic Advisers: “The single greatest problem with the current system is that most regulations are subject to a cost–benefit analysis only in advance of their implementation. This is the point when the least is known and any analysis must rest on many unverifiable and potentially controversial assumptions.” By contrast, retrospective analysis can help show what works and what does not, and in the process can promote the repeal or streamlining of less effective rules and the strengthening or expansion of those that are working well. Greenstone thus urges a series of reforms designed to “instill a culture of experimentation and evaluation.”

In the past, there have been honorable and occasional, but not systematic, efforts to reassess rules – to analyze their costs and benefits and to streamline or eliminate those that deserve it. Nor has there been an effort to institutionalize “lookback” – to create a regulatory culture of regular evaluation.

The solution: In January 2011, President Obama called for a government-wide review of regulations on the books to reduce costs, to eliminate unnecessary burdens, and to get rid of what the President has called “absurd and unnecessary paperwork requirements that waste time and money.” The lookback process has catalyzed a large and growing number of significant initiatives.

In November, and after careful consideration of public comments, about two dozen agencies produced final plans, spanning over 800 pages and offering more than 500 proposals. A large number of independent agencies followed suit, responding to a historic request from the President to eliminate unjustified costs on their own.

A great deal has happened in a short time. Over 50 lookback rules have already been finalized, and an additional 50 have been publicly proposed.

We are able to announce five final rules today:

- In direct response to public concerns, the Department of Transportation has finalized a rule to extend compliance dates on dozens of new traffic control requirements imposed on states and local government, potentially saving millions of dollars in the process.
- To eliminate unjustified economic burdens on railroads, the Department of Transportation has finalized significant changes in parts of a rule that requires railroads to install safety equipment on trains. DOT expects initial savings of up to \$325 million, with total 20-year savings of up to \$755 million.
- EPA has finalized a rule to eliminate the obligation for some states to require air pollution vapor recovery systems at local gas stations, on the ground that modern vehicles already have effective air pollution control technologies. The anticipated five-year savings are around \$440 million.
- To promote flexibility, the Department of Health and Human Services has finalized two rules to reduce burdensome regulatory requirements now placed on hospitals and doctors. These reforms are expected to save more

than \$5 billion over the next five years.

As the figures above suggest, regulatory reform is already producing big and measurable savings for consumers and businesses. In the next five years, well over \$10 billion in savings are anticipated from just a very small fraction of more than 500 initiatives. In the future, the lookback process is expected to deliver a great deal more. A report from the Council of Economic Advisers, released today, provides the details.

The lookback effort, designed above all to cut through unnecessary red tape, is no one-time endeavor. Just today, the President is issuing a historic Executive Order to institutionalize the process of retrospective review. The order states that “further steps should be taken . . . to promote public participation in retrospective review, to modernize our regulatory system, and to institutionalize regular assessment of significant regulations.”

To promote participation, the Order directs agencies to seek public comments on rules in need to review. To promote priority-setting, the Order directs agencies to emphasize reforms that produce significant quantifiable savings. To promote accountability, the Order requires agencies to provide the public with regular reports on their past efforts and their future plans -- with details and deadlines.

With today’s step, the process of retrospective analysis, no less than prospective analysis, will become a standard part of the assessment of federal regulations. This is a fundamental shift.

New Requirements for the Issuance of Rules

The problem: Notwithstanding impressive efforts by previous Administrations, rulemaking has not always benefited as much as it might from public participation, and it has not always involved state-of-the-art analysis of benefits, costs, and alternatives.

The solution: It is imperative to use new technologies to obtain the best possible information about the likely effects of rules, and to use the best available evidence to increase benefits and to decrease costs.

The January 2011 Executive Order provides a series of new directives to govern future rulemaking. Emphasizing the importance of predictability and certainty, those directives are consistent with, and informed by, what we have learned about regulation in recent years.

Let me emphasize five key points.

1. **Public participation.** The President has made an unprecedented commitment to promoting public participation in the rulemaking process – with a central goal of ensuring that rules will be informed, and improved, by the dispersed knowledge of the public. Agencies are not merely required to provide the public with an opportunity to comment on their rules; they must also provide timely online access to relevant scientific and technical findings, thus allowing them to be scrutinized.
2. **Advance consultation.** The Order directs agencies to act, even in advance of rulemaking, to seek the views of those who are likely to be affected. This group explicitly includes “those who are likely to benefit from and those who are potentially subject to such rulemaking.” Among other things, this emphasis on early involvement is an effort to acquire relevant information and to avoid unintended harmful consequences.
3. **Simplification and harmonization.** The new Executive Order specifically directs agencies to take steps to harmonize, simplify, and coordinate rules. It emphasizes that some sectors and industries face redundant, inconsistent, or overlapping requirements. In order to reduce costs and to promote simplicity, it requires greater coordination. The order also explicitly connects the goal of harmonization with the interest in innovation, directing agencies to achieve regulatory goals in ways that promote that interest.
4. **Quantification.** The Executive Order firmly stresses the importance of quantification. It directs agencies “to use the best available techniques to quantify anticipated present and future benefits as accurately as possible” – and to the extent permitted by law, to proceed only on the basis of a reasoned determination that the benefits justify the costs.
5. **Flexibility.** The Executive Order directs agencies to identify and to consider flexible approaches that reduce burdens and maintain freedom of choice for the public. Such approaches may include, for example, public warnings, appropriate default rules, or provision of information “in a form that is clear and intelligible.” We know that simplification of existing requirements can often promote compliance and participation, and that complexity can have serious unintended consequences. We also know that flexible performance objectives are often better than rigid design standards, because performance

objectives allow the private sector to use its own creativity to identify the best means of achieving social goals. To promote flexibility, we have recently several calls to all agencies to reduce reporting burdens on small business and to eliminate unjustified complexity. We have received many important initiatives in response.

Promoting Trade and Exports through International Cooperation

The problem: Companies often face disparate requirements across borders. These disparate requirements may not reflect differences in values or facts, but a simple failure to discuss and to coordinate. The result can be conflicting or redundant requirements – and thus higher costs for companies and consumers, and adverse effects on growth and job creation and also on trade and exports.

The solution: As the President’s Jobs Council has suggested, it is important to work with other nations to eliminate unjustified disparities that impose unjustified costs and red tape.

Of course any work in this domain must respect the primacy of domestic law and national priorities. While showing that respect, we can do a great deal to eliminate unnecessary burdens.

In line with the general effort to achieve that goal, President Obama issued, just last week, a new Executive Order, “Promoting International Regulatory Cooperation,” that is designed to spur efforts to align regulatory requirements so that companies do not face unnecessarily divergent rules when they do business across national boundaries. The Executive Order offers a series of specific directions for promoting that goal. For example, initiatives for revisiting existing rules, to foster harmonization, must be considered for inclusion in the process of retrospective review.

Today's action builds on many other administration efforts to eliminate unjustified regulatory costs and to reduce burdens by promoting international regulatory cooperation.

One example: The U.S. has long required employers to use warning symbols to inform employees of potential safety hazards. Other nations require warnings, too, but in many cases they mandate the use of different symbols. The result of the disparate requirements is to impose pointless costs on those who do business in

more than one nation. Why should chemical manufacturers have to create multiple labels for the same product in different countries?

To address this problem, the Department of Labor recently harmonized its labeling requirements with those of many nations around the world, a reform that is projected to save American businesses more than \$475 million each year.

More generally, President Obama has worked closely with his Canadian and Mexican counterparts to create High-Level Regulatory Cooperation Councils with both countries.

The councils are developing and implementing plans to eliminate or prevent the creation of unnecessary burdens on cross-border trade, streamline regulatory requirements, and promote greater certainty for the general public and for businesses in multiple areas.

The U.S. and Canada have already agreed to harmonize their rules with respect to fuel economy, building on a long history of collaboration on national emission standards for new vehicles. This step will avoid divergent requirements and unnecessary costs on both automobile companies and consumers.

The U.S. is also working closely with the European Union to eliminate unnecessary differences in U.S.-European regulatory requirements. Last February, the Obama administration announced an agreement with the EU under which organic products certified as such in Europe or in the U.S. may be sold as "organic" in either jurisdiction. This is not just a victory for those who grow and eat organic broccoli. The trans-Atlantic partnership, involving the two largest organic food producers in the world, will help reduce costs and support jobs in the years to come.

Whether the issue involves chemicals or vegetables, nations can do a far better job of harmonizing regulatory requirements to make it easier for companies to do business, and without sacrificing public health, safety and the environment. Last week's executive order provides a new model for eliminating red tape and promoting trade and job creation.

Flexible, low-cost regulatory tools, including disclosure

The problem: Disclosure has become a central part of modern regulation, but often disclosure has not been helpful. One reason is that disclosure has not always

been attuned to how real people actually process information. Sometimes people get too much information, and the information they get complicates rather than simplifies their decision-making.

The solution: Where appropriate, agencies should reduce complexity and promote clear, simple disclosure.

An orienting idea is the *need for a clear path, or (in a catchphrase) **Plate, not Pyramid*** (more on that shortly). When people are informed of the benefits or risks of engaging in certain actions, they are far more likely to act in response to that information if they are simultaneously provided with a clear, explicit path about how to respond. For example, those who are informed of the benefits of a vaccine are more likely to become vaccinated if they are also given specific plans and maps describing where to go. Similarly, behavior has been shown to be significantly affected if people are informed, not abstractly of the value of “healthy eating,” but specifically of the advantages of buying 1 percent milk as opposed to whole milk.

In many domains, the identification of a specific, clear, unambiguous path or plan has an important effect on social outcomes. Complexity or vagueness can ensure inaction, even when people are informed about risks and potential improvements. What appears to be skepticism or recalcitrance may actually be a product of paralysis and uncertainty about what to do.

Here are some examples:

- *Food plate replacing food pyramid:* The much-viewed Food Pyramid has long been criticized as insufficiently informative. It did not provide people with any kind of clear “path” with respect to healthy diet. In response to these objections, and after an extended period of deliberation, the United States Department of Agriculture replaced the Pyramid with a new, simpler icon, consisting of a plate with clear markings for fruit, vegetable, grains, and protein. The new icon has been widely praised.
- *Fuel economy label:* Automobile manufacturers are currently required by statute to disclose the fuel economy of new vehicles as measured by miles per gallon (MPG). This disclosure is useful for consumers and helps to promote informed choice. As the Environmental Protection Agency (EPA) has emphasized, however, MPG is a nonlinear measure of fuel consumption. For a fixed travel distance, a change from twenty to twenty-five MPG produces a larger reduction in fuel costs than does a change from thirty to thirty-five MPG, or even from

thirty to thirty-eight MPG (because less efficient cars will turn over their fuel supply more frequently). To see the point more dramatically, consider the fact that an increase from ten to twenty MPG produces more savings than an increase from twenty to forty MPG, and an increase from ten to eleven MPG produces savings almost as high as an increase from thirty-four to fifty MPG. Recognizing the imperfections and the potentially misleading nature of the MPG measure, the Department of Transportation and EPA adopted an approach that calls for disclosure of relevant, meaningful factual material, including a prominent statement of annual fuel costs. The new label must also provide a clear statement about anticipated fuel savings (or costs) over a five-year period. The information about annual fuel costs and five-year fuel savings (or costs) should simultaneously help counteract the potential difficulties with the MPG measure and not leave it to consumers to do the arithmetic needed to figure out the net economic effects of fuel economy standards on their budgets and lives.

- *Health insurance information.* Implementing a provision of the Affordable Care Act, the Department of Health and Human Services has finalized a rule to require insurance companies to provide clear, plain language summaries of relevant information to prospective customers. The rule calls for disclosure of basic information, such as the annual deductible, a statement of services that are not covered, and a statement of costs for going to an out-of-network provider. This disclosure requirement has been described as a kind of “nutrition facts” for health insurance.

These are simply a few examples of a number disclosure requirements that are meant to promote informed choices. We continue to seek ways to ensure that disclosure requirements will prove helpful rather than confusing. In this respect, the effort to promote clear, meaningful disclosure belongs in the same family as other efforts to promote empirical testing of rules, perhaps above all through the regulatory lookback.

One of our hopes is that the recent efforts to rethink the regulatory system might inaugurate a broader and more empirical conversation about how we might promote economic growth and job creation while protecting the health and safety of the American people.

Over two centuries ago, Alexander Hamilton helped inaugurate another and even larger conversation, when the nation was in the midst of an even more passionate and polarized debate. Hamilton’s own work can be found, in part, in a series of essays that came to be known as *The Federalist Papers*. Attempting at once to

lower the volume of the discussion and to raise its level, he wrote quietly but firmly, and at the very start of The Federalist No. 1:

“It has been frequently remarked that it seems to have been reserved to the people of this country, by their conduct and example, to decide the important question, whether societies of men are really capable or not of establishing good government from reflection and choice, or whether they are forever destined to depend for their political constitutions on accident and force.”

Of course the current process of regulatory reform does not have anything like the momentousness of the decisions made by We the People in the late 1700s.

But the process is also in its way an effort not to depend on accident and force, but to promote good government by reflection and choice. In that sense, it might be seen as an effort, in one domain, to honor our founders' extraordinary achievement.

Thank you.