Cutting the Tape on Government Regulation

Remarks by

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My object today is to concentrate attention on the problem of over-regulation which threatens to have as serious an effect on our economic well-being as almost any factor I can think of, and to bring you up to date on progress at the Federal Reserve in grappling with this problem in our areas of jurisdiction.

I must stress first that I am not about to encourage a revolt against all regulation. Who in his right mind would oppose a cleaner environment, better working conditions, purer food, safer drugs, nondiscrimination in employment, and a variety of other socially desirable goals? Many improvements have come about from government regulation over the years, and, naturally, I'm for them.

But government regulation has become pervasive and in many cases oppressive to many sectors of our society. Without doubt, the problem of over-regulation demands attention and quickly. Let me give you some idea of the dimensions of the problem:

* Government regulation drastically affects nearly every important sector of the economy--employment, productivity, inflation, profits and capital formation, among others.

* In the end, the public pays the costs, which are often hidden or, at the least, difficult to see;

* Regulation is now and has been for several years one of the most rapidly growing sectors of government;

* Understanding government regulations, always difficult for lawyers, accountants and other professional technicians hired by business, often is virtually impossible for the public.

Excessive government interference in the public sector prevents employers from creating more jobs; hinders economic growth and productivity by forcing business to set aside a rising share of new capital to cover regulatory costs; slows technological innovation; and increases inflation through higher consumer prices. In essence, over-regulation diverts private sector attention from its traditional roles of product development, production and marketing.

As you might expect, the public is the eventual loser in this process because it is the public who must pay. Business attempts to recover higher costs generated by government rules in the traditional way--by passing them on to the customer in higher product prices. Also, the public--taxpayers--must bear the costs of operating the federal regulatory apparatus. Motorists, home buyers, investors and others come in for extra shares of the burden caused by over-regulation.

The emergence of government regulation as a growth industry is easy to document. The Center for the Study of American Business at Washington University has done extensive work in this area. The Center's figures show more government regulatory agencies--20--have been organized during the '70s than in any other decade in American history. In the same period, budgeted expenditures of federal agencies have expanded by a multiple of almost six and now approach the $6 billion level. Staffing of these agencies has nearly tripled in the same span.

Statistics such as these represent only part of the story--the federal portion. Regulation by other governmental units, on the state and local levels, also is burgeoning, although expenditures by these bodies are not readily estimated.

Although no one knows how many regulations are on the books today there are several indirect clues. The Code of Federal Regulations has 38 volumes totaling some 65,000 pages. Placed side by side, the volumes are 15 feet long. The Federal Register, where proposed federal regulatory changes are first published, now prints about 70,000 pages a year, for a cumulative total of over 800,000 pages. Between 1970 and 1975 the annual number of pages in the Register increased about 25 percent a year, some five times the growth rate between 1955 and 1970.

It is important to remember that every regulation has its source in some law passed by a legislative body. Several years ago it was estimated that federal, state and local governments enact 150,000 laws a year. Although each new law does not require a regulation, enough of them do to create a morass of legality and technicality that can give even the most competent legal staffs a massive headache.

Look at one example bankers are familiar with. In 1968 Congress passed a law to protect the rights of borrowers by requiring a declaration of the rate of interest on the borrowing agreement. The Federal Reserve was assigned the task of writing regulations to carry out this Truth in Lending legislation. It is Regulation Z of the Federal Reserve System. But complications written into the law by Congress, some 1,500 Federal Reserve interpretations and many court decisions have enlarged a relatively simple concept into a mass of material nearly two feet high. Even the largest banks in the country, with huge legal staffs, are pressed to keep up with all the pertinent details of Regulation Z. Where does that leave smaller lenders? To give you an idea of the problems we are causing, let me read to you a letter from the president of a small bank in Missouri: "Gentlemen: We are returning your proposed Rule Book to you. We have no comment to make since we couldn't find anyone within 80 miles around here who could understand what in the hell it meant."

Traditionally, economists think of regulations as necessary in the public interest in our complex society in order to smooth imperfections in the private economy and our market system. Generally, regulations are classified in two ways:

1) Economic regulations, which focus on a specific market or perhaps a single industry and prices in that market, and;

2) Social regulations which typically deal with the conditions under which goods and services are produced or the physical characteristics of the goods.

An example of the first, older type, is the Interstate Commerce Commission control over railroads. It is, however, the second, newer social-type regulation which has contributed most to the recent explosion in regulatory activity.

The 1970s have seen the establishment of such regulatory commissions as the Environmental Protection Agency (EPA), OSHA, the Office of Consumer Affairs and Regulatory Functions and the Consumer Product Safety Commission. Each agency is concerned with some facet of job safety, environmental purity, safe products and overall consumer protection.

Earlier this year the Center for the Study of American Business, headed by Professor Murray Weidenbaum, released figures covering the budgeted expenditures of 56 federal agencies with major regulatory functions. They showed the most rapid expansion in the "newer product lines." A growth of almost 1,200 percent in 10 years for government regulatory expenditures in the environmental and energy areas; nearly 600 percent growth for regulating job safety and other working conditions, and a 300 percent growth for consumer safety and health regulatory budgets.

Meanwhile, the 10-year increases in the older areas of regulation--such as finance and banking, specific industries (including the ICC, CAB and FCC) and general business (including the SEC and FTC)--was a combined 166 percent. Budgets of the newer social regulatory agencies accounted for over four-fifths of the regulatory expenditures estimated for fiscal 1980. Still that does not lessen the Federal Reserve's responsibility for ameliorating the regulatory burden on the financial world.

Recognizing the spreading disease, President Carter issued an executive order On Improving Government Regulation, accompanied by establishment of an inter-agency Regulatory Analysis Review Group and Regulatory Council. The Review Group was directed to evaluate regulatory analyses of 10 to 20 major regulations a year. The Council was directed to coordinate activities of agencies to avoid overlapping and duplication in regulation and is to publish a unified calendar of planned major regulations stating goals, benefits, expected timetables and estimates of economic impact.

Congress has also reflected the concerns of constituencies about government over-regulation. Various committees, including the Subcommittee on Economic Growth and Stabilization of the Joint Economic Committee, have conducted extensive hearings on the costs of government regulation. And numerous regulatory reform measures are pending in the current Congress.

The tremendous costs of government regulation, as hard as they may be to determine accurately, have inspired these actions. Based upon what he describes as a conservative estimating procedure, Professor Weidenbaum uses a multiplier of 20 times the budgeted expenditures of the regulatory agencies to determine the costs of the private sector in complying with federal rules. In the year ending September 30, 1979, he estimates the direct costs of running the federal regulatory machine at over \$5-3/4 billion. Using the multiplier of 20 produces a total estimated cost of federal regulation, including the costs of compliance, of above \$120 billion, or over $600 for each man, woman and child in the United States. These figures are just about double the 1976 estimates!

Measuring costs of regulation, even direct expenditures only, is no easy job. The costs of secondary effects of complying with regulations are even more difficult to ascertain. Most of us in business know firsthand about the paperwork necessary to comply with government rules. But there are many other diversions of time and manpower in meeting regulatory requirements that are not as easily recognized. Hiring of professional help to comply, maintaining files to be able to comply the next time, meeting with regulatory officials, and monitoring new and revised regulations. I have already mentioned some of the other hidden and visible costs involved.

This, then, is the ever-spreading malady, born in the public interest, but now costing society more than its benefits in many cases. It demands quick-acting medicine.

We have reached the point today when a magazine of mass appeal reprints an article headlined "Time to Control Runaway Regulation;" when a major daily newspaper runs an editorial entitled "Costly Regulation;" and when the nation's premier business journal concludes an editorial about "regulatory-born virus" with the suggestion--only partly tongue in cheek--that: "Undoubtedly the answer lies in the creation of a new superagency for the protection of people from government regulations."

With this somewhat pessimistic background, let me now turn to the regulatory problem at the Federal Reserve. Make no mistake about it, the Federal Reserve is one of the principal agencies issuing consumer regulations these days. As I mentioned already, the Board administers the Truth in Lending Act and Regulation Z. But, in addition, its regulations deal with many other consumer subjects including (1) the nondiscriminatory granting of credit, (2) the resolution of computer billing errors, (3) the privacy of credit files, (4) the disclosures required on consumer leases, and so on.

Just as consumer statutes prompt the issuance of regulations, the Board's consumer regulations, as I pointed out earlier, prompt the issuance of complex and formal Board interpretations, staff interpretations, examiner guidelines and other regulatory material. In the past ten years, the small staff of five initially assembled to administer Regulation Z has grown to a full Board division with a current total staff of 43, and the efforts of this division are supplemented by additional staff at the Reserve Banks.

But that is not all. The Board's regulatory responsibilities concerning bank holding company activities have grown rapidly since the passage of new legislation in 1970. And the Board's responsibilities have grown even further with the passage of The Financial Institutions Regulatory and Interest Rate Control Act late last year. This legislation requires, among many other things, stringent regulation of bank loans to insiders, close monitoring of changes in bank control, and detailed regulation of electronic funds transfers.

All of these were added on to the existing core of the Board's regulatory activities relating to monetary policy, bank supervision, and securities credit.

Given the System's deep involvement in the regulatory process, what can and should be done to minimize the regulatory burden?

I am pleased to report that the Board last year inaugurated a Systemwide program to review and simplify all Federal Reserve regulations. A small group of professionals has been assembled to work full time on the project. In addition, heavy reliance is placed on Federal Reserve Bank staff. Under this program, a zero-based review of each Federal Reserve regulation is being conducted to determine (1) its fundamental objectives and the extent to which it is currently meeting them, (2) the costs and benefits of the regulation, (3) any unnecessary burdens that can be eliminated, (4) the clarity and readability of the regulation, and (5) nonregulatory alternatives that would accomplish the same objectives.

To date, the Board has taken final action on eight regulations. Four of these have been completely overhauled, and three have been rescinded. In addition to reviewing existing regulations, this regulatory review group has put a good deal of effort into ensuring that the Board's newest regulations--those implementing the International Banking Act and the Financial Institutions Regulatory and Interest Rate Control Act (FIRA)--were written as simply and clearly as possible.

A significant part of the Federal regulatory burden is related to reporting requirements. The Federal Reserve has both wide-ranging supervisory responsibilities and substantial economic data needs. Both of these, unfortunately, involve heavy reporting demands. The Board has instituted a program to establish better control over the entire reporting process. It has established stringent guidelines for the evaluation and clearance of proposed new reports. Several groups subject any report proposal to critical examination before it is adopted. Moreover, each report now has a short life: each is subject to a "sunset" date after which it must be reviewed and reauthorized by the Board. Using a simple calculation of burden (the number of items of information required, times the frequency of the report, times the number of respondents) a gross measure of overall reporting burden has been developed. Through the program, a significant reduction in reporting burden has been accomplished.

The Board has also adopted new regulation-writing procedures directed toward improving both the substance and readability of its regulations. Elements of the program include early involvement of the public in the rulemaking process by such means as advance notice of proposed rules; a special effort to identify areas in which the Board would particularly like comments; informal public hearings; and the direct solicitation of the views of interested persons or groups. A particularly important part of this program is the presentation of a "regulatory analysis" with each major new proposal. This analysis focuses on possible regulatory and nonregulatory alternatives, and includes an estimate of the possible economic impact of the regulation, as well as the burdens of compliance.

As part of this program the Board has recently begun publishing a "regulatory agenda" listing all of the regulatory actions likely to be considered in the next six months. The agenda even tries to introduce a human element into the regulating process by giving the name and telephone number of the staff member working on the project.

Other efforts are underway. A new regulatory service will provide a single convenient source to all Board regulations, published and previously unpublished Board interpretations, staff opinions, and policy statements. It is our hope that this publication, assembling all regulatory materials, will ease the task of understanding and complying with Board rules.

However, the success of all of these efforts aimed at significantly reducing the regulatory burden will depend upon our overall concept of the proper role of Federal regulation.

It is my deeply held view that the nation simply cannot afford to orchestrate a Federal regulatory response to every problem of the marketplace. Certainly our experience of the last few years should make us acutely aware of the tremendous costs associated with Federal regulation. In each instance of proposed regulation we must be sure that whatever problems are identified are of such magnitude that they warrant the often massive allocation of resources and the disruptions that Federal regulations necessarily entail.

It should be clearly understood, however, that from a policy-maker's point of view it is sometimes far easier to regulate than not to. The issuance of regulations serves to quiet the sometimes shrill Congressional voices calling attention to cases of individual abuse. It is far easier to acknowledge the occurrence of such problems and write new rules than to suggest that a new Federal regulatory scheme may not be the appropriate response.

In order for the regulatory agencies to be successful in arguing against more regulation, in the face of admitted instances of overreaching, we must have the support of the affected industry in providing nonregulatory solutions to these problems. Strong industry efforts are needed, for example, to limit questionable bank advertising, unreasonably delayed availability of funds, and other potential areas of abuse if we are to be successful in holding the line on new regulation. With the commitment of the System, and the help of industry, I feel confident we can begin to find a solution to this serious national problem and hopefully resist, in the future, the tendency to overregulate. But it is unquestionably an uphill battle for which I solicit your support.