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# Saving Lives Through Administrative Law and Economics: A Response

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## RESPONSE

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### SAVING LIVES THROUGH ADMINISTRATIVE LAW AND ECONOMICS: A RESPONSE

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SHI-LING HSU<sup>†</sup>

In response to John D. Graham, *Saving Lives Through Administrative Law and Economics*, 157 U. PA. L. REV. 395 (2008).

John D. Graham, the former director of the Office of Information and Regulatory Affairs (OIRA) and now the Dean at the Indiana University School of Public and Environmental Affairs, has written in *Saving Lives Through Administrative Law and Economics*<sup>1</sup> a valuable twofer: (1) a thorough defense of cost-benefit analysis (CBA) as applied to agency rulemaking and (2) something of a memoir about his tenure at OIRA, from 2001 to 2006. Both are important contributions. We do not hear from agency regulators often enough about how they do their job, and we know too little about how agencies actually carry out their statutory mandates. There are good reasons for this, but, for law professors, this lack of knowledge is unfortunate, because we spend a fair amount of time and energy writing about processes about which I suspect we know less than we think we do. To the extent that Dean Graham sheds light on these processes, we cannot be the worse off for it. And the other goal of the article—a defense of CBA—is achieved by a thorough review of the theory and literature on cost-benefit analysis and a marshalling of all of the arguments for increased agency use of the practice. Along the way, Graham engages with critics of

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<sup>†</sup> Associate Dean for Special Projects, University of British Columbia Faculty of Law. I wish to thank Matthew Adler for some thoughtful remarks on an earlier draft of this Response.

<sup>1</sup> John D. Graham, *Saving Lives Through Administrative Law and Economics*, 157 U. PA. L. REV. 395 (2008).

CBA, some of whom have been quite personal in their attacks,<sup>2</sup> and treats their arguments with seriousness.

However, in marrying these two goals, each goal is slightly compromised. It is not as if Graham's experience at OIRA is irrelevant to an evaluation of CBA, but Graham's defense of CBA inevitably comes around to its use during his tenure at OIRA. I have never gotten the impression that Graham has been particularly interested in vindicating his tenure at OIRA (nor does he have anything to apologize for). But the nature of the attacks on Graham have effectively conflated Graham's name with CBA advocacy (an association from which Graham does not shrink), so that Graham's defense of CBA inevitably comes across as self-defense. For example, Graham describes the OIRA history of the EPA rulemaking over off-road diesel engines.<sup>3</sup> Graham's critics have charged that he stalled this rulemaking by forcing the EPA to redo its CBA with different assumptions.<sup>4</sup> Graham's account is that he used CBA to overcome skeptical politicians and business interests, presenting compelling CBA analysis showing the value of regulation.<sup>5</sup> Graham's account is credible—Senator Christopher Bond of Missouri did indeed undertake extraordinary measures to stall regulation, at one point adding a rider onto a Department of Veterans Affairs and Department of Housing and Urban Development appropriations bill that prohibited California and other states from regulating small off-road diesel engines.<sup>6</sup> It is perfectly understand-

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<sup>2</sup> Lisa Heinzerling and Frank Ackerman have spent the most time and effort criticizing Graham for his advocacy of CBA. Fifteen of Lisa Heinzerling's law review articles mention John Graham, none of them in a positive light. See, e.g., FRANK ACKERMAN & LISA HEINZERLING, PRICELESS: ON KNOWING THE PRICE OF EVERYTHING AND THE VALUE OF NOTHING 195 (2004) ("[Graham at] OMB has lately invented a form of discounting so peculiar, one would think it was a vast typographical error if it hadn't appeared in OMB's handiwork more than once."); Lisa Heinzerling, *Five-Hundred Life-Saving Interventions and Their Misuse in the Debate over Regulatory Reform*, 13 RISK 151, 152-53 (2002) ("Dr. Graham's misuse of his own data in the service of an anti-regulatory agenda warrants assiduous monitoring—by scholars, the public interest community, and the federal agencies themselves—of his activities as head of OIRA."); *id.* at 169 ("Dr. Graham himself has misrepresented his own research."). Ackerman and Heinzerling are also critical of Graham for seeking a \$25,000 contribution from the Philip Morris Companies while he was the head of the Harvard Center for Risk and Regulation. See ACKERMAN & HEINZERLING, *supra*, at 128-29.

<sup>3</sup> See Graham, *supra* note 1, at 466-69.

<sup>4</sup> ACKERMAN & HEINZERLING, *supra* note 2, at 198-201.

<sup>5</sup> See Graham, *supra* note 1, at 468-69.

<sup>6</sup> See S. 1584, 108th Cong. (2003); see also Press Release, Senator Dianne Feinstein, Senator Feinstein Asks California Congressional Delegation to Help Strip Small Engines Provision from VA/HUD Appropriations Bill (Oct. 23, 2003), *available*

able that Graham wished to show how CBA helped, rather than hindered, regulation, but that story seems more appropriately part of his memoirs.

Despite this slight dilution of purpose, the article does an excellent job of reviewing the technical issues and intellectual background of CBA, tracing its roots to (but ultimately rejecting) the deregulation movement most prominently advocated by the Reagan administration.<sup>7</sup> Graham characterizes CBA advocates (perhaps a little euphemistically) as “regulatory reformers” who mostly reject a rights-based orientation and adopt a welfarist view of regulation.<sup>8</sup> While acknowledging that present analysis of CBA is “not as comprehensive and robust as one would prefer,” he argues that, done properly, CBA is “morally relevant and often helpful (‘determinate’) in distinguishing good rules from bad rules.”<sup>10</sup> In making a case for broader use of CBA, Graham is workmanlike in his thoroughness, sketching out the normative foundations of CBA,<sup>11</sup> the different forms of CBA and alternatives,<sup>12</sup> a review of CBA in federal agency practice,<sup>13</sup> some economic issues surrounding CBA (including the vexing problem of discounting),<sup>14</sup> and finally a menu of suggested reforms.<sup>15</sup> The article provides an admirably comprehensive review; someone with no previous understanding of CBA could bring herself nearly up to speed by reading this carefully.

Graham makes the important and often-overlooked point that CBA is not a single decision-making model but can be used in agency decision making in three ways: (1) as a “hard” rule, in which the benefits must *exceed* the costs of every agency action;<sup>16</sup> (2) as a “soft” rule, in which the benefits must only *justify* the costs, but in which the regulator must explain, if she acts inconsistently with the CBA, why

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at <http://feinstein.senate.gov/03Releases/r-smallenginesdelegation.htm> (criticizing Senator Bond’s proposed rider).

<sup>7</sup> See Graham, *supra* note 1, at 399-400, 404.

<sup>8</sup> *Id.* at 399-401.

<sup>9</sup> *Id.* at 398.

<sup>10</sup> *Id.* at 403.

<sup>11</sup> *Id.* pt. I.

<sup>12</sup> *Id.* pt. II.

<sup>13</sup> *Id.* pt. III.

<sup>14</sup> *Id.* pt. IV.

<sup>15</sup> *Id.* pt. V.

<sup>16</sup> *Id.* at 432-33.

she did so;<sup>17</sup> and (3) as a procedural rule, in which a CBA is required of agency actions but is provided for informational purposes only and not intended to be determinative in any way.<sup>18</sup> Current federal practice is probably best described as a soft rule, as President Bush has altered CBA practices to tighten requirements for regulation but has not abandoned President Clinton's "soft" rule.<sup>19</sup> Graham himself advocates the use of CBA as a "soft" rule, acknowledging that some things worth considering are still impossible or extremely difficult to quantify.<sup>20</sup> For example, Graham is troubled by questions of distribution and first on his to-do list of proposals for improving CBA is to ensure fair treatment for the poor.<sup>21</sup> The soft rule nevertheless places the burden with the regulator to explain why the CBA is not serving as the decision rule.

In my view, the procedural rule is the most sensible way to apply a consistent rule across a wide array of environmental problems, at least within those statutes that allow CBA to be used.<sup>22</sup> A procedural rule has previously been used to great effect in the environmental field: the National Environmental Policy Act (NEPA)<sup>23</sup> requires an environmental assessment in connection with any federal action, and if the federal action will have a significant environmental impact, then a full-blown and extensive environmental impact statement (EIS) is also required.<sup>24</sup> By the terms of the statute and regulations, no substantive outcome is ever required, but the practical effect is that the EIS is very important in federal agency decision making. While federal projects do not necessarily live or die with the findings of an EIS, projects that

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<sup>17</sup> *Id.* at 433-34.

<sup>18</sup> *Id.* at 434-35.

<sup>19</sup> President Clinton's Executive Order 12,866 modified President Reagan's Executive Order 12,291, from a "hard" rule to a "soft" rule. Compare Exec. Order No. 12,866, § 1(b)(6), 3 C.F.R. 638, 639 (1994), reprinted in 5 U.S.C. § 601 (2006) (requiring the benefits of regulation to "justify" its costs), with Exec. Order No. 12,291, § 2(b), 3 C.F.R. 127, 128 (1982), reprinted in 5 U.S.C. § 601 (1988) (requiring the "potential benefits to society" of a regulation to "outweigh" its costs).

<sup>20</sup> See Graham, *supra* note 1, at 435-38.

<sup>21</sup> *Id.* sec. V.A.

<sup>22</sup> *Whitman v. American Trucking Ass'n*, for example, held that the Clean Air Act, while requiring the EPA Administrator to set ambient air quality standards "requisite to protect the public health," did not permit the Administrator to consider costs in doing so. 531 U.S. 457, 464-71 (2001).

<sup>23</sup> 42 U.S.C. §§ 4321-4370f (2006).

<sup>24</sup> *Id.* § 4332. An "environmental assessment" is required so that an agency can determine whether a more detailed EIS is necessary. See 40 C.F.R. § 1508.9 (2008).

give rise to a significant environmental impact that cannot be mitigated trigger considerable scrutiny.

Perhaps the strongest reason for using CBA as a procedural rule is that it is such a compelling compromise between CBA advocates and detractors. For CBA advocates such as Graham, who argue that CBA presents important and sometimes nonintuitive information, a procedural rule should satisfy their desire for CBA to become a greater part of the public-policy dialogue. As a practical matter, the difference between the soft rule and the procedural rule is not, as Graham acknowledges, necessarily a great one. While the procedural rule may not place any formal restrictions on the agency, it does provide information for other political and legal actors, such as Congress, the courts, and potential litigants.<sup>25</sup> For controversial rules and projects, agency officials ignore a well-done CBA at their peril.

As for CBA detractors, I have trouble understanding how a CBA, if it does nothing more than provide information, can be so threatening to their notions of a healthy administrative state.<sup>26</sup> Acknowledging that there could be some perception of precision in numbers, as detractors have argued, the answer cannot be to dumb down the regulatory process further by stripping it free of numbers for fear of confusing the body politic, as long as the numbers are not systematically or intentionally misleading. Are they systematically or intentionally misleading? The public-choice concern is that regulated industries have a greater and more concentrated incentive to manipulate CBA numbers than public interest groups have to contest them, but the history of administrative regulation in the United States does not suggest that the imbalance of power is limited to the economic arena. On the contrary, it is implausible to think that regulated industries need the cloak of opaque economic analysis to conceal their influence over legislative and administrative bodies.

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<sup>25</sup> See Graham, *supra* note 1, at 453-54.

<sup>26</sup> See, e.g., Lisa Heinzerling, *Regulatory Costs of Mythic Proportions*, 107 YALE L.J. 1981, 2042 (1998) ("Many other scholars have identified situations in which seemingly technocratic decisions mask fundamental choices about values."); Thomas O. McGarity, *Professor Sunstein's Fuzzy Math*, 90 GEO. L.J. 2341, 2366 (2002) (arguing that CBA is "occasionally comprehensible, but frequently preposterous and always manipulable number spinning"); Amy Sinden, *The Economics of Endangered Species: Why Less Is More in the Economic Analysis of Critical Habitat Designations*, 28 HARV. ENVTL. L. REV. 129, 136 (2004) (commenting that President Reagan's executive order requiring agencies to use CBA "was widely viewed as a tool aimed at furthering Reagan's avowed mission of dismantling the regulatory state").

I do have one practical concern about the use of CBA as a procedural rule—just as regulated entities have complained bitterly about the amount of time it takes to prepare an EIS and the delays imposed by NEPA,<sup>27</sup> a lengthy CBA process could be used (and has been used) to delay regulation.<sup>28</sup> To help remedy this, I second a proposal by Daniel Cole. Cole proposes the establishment of a panel of economists, operating under a “quasi-governmental organization, such as the National Academy of Sciences,” to establish a set of best practices for CBAs.<sup>29</sup> Once a set of best practices became standard fare, the quality of a CBA should be considerably easier to ascertain, more so over time as CBAs are defended and debunked.

Concerns over delay aside, then (and the CBA debate does not seem overly focused on delays), why is there no clamor for CBA as a procedural rule? I believe there are two theoretical undercurrents to the CBA debate that have not been fully grappled with and that demand some resolution before any view on the role of CBA becomes settled.

One undercurrent, pursued by Matthew Adler and Eric Posner, is the debate over CBA and *welfarism*.<sup>30</sup> For Graham and CBA advocates, a procedural rule would represent a retreat from current federal practice of CBA as a soft rule, but more fundamentally, the procedural rule would return administrative decision making to the political realm, which has exhibited poor priority-setting in the past. For CBA advocates, the future of administrative lawmaking lies in a welfarist framework. For CBA critics, welfarism is inherently indeterminate and detracts from the important debate that we should be having over values, not numbers.<sup>31</sup>

Superficially, CBA critics would seem to have the intellectual upper hand in this debate. The difficulty of constructing a social welfare

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<sup>27</sup> A historical list of complaints is long, but Bradley C. Karkkainen provides a short description. See Bradley C. Karkkainen, *Toward a Smarter NEPA: Monitoring and Managing Government's Environmental Performance*, 102 COLUM. L. REV. 903, 909-37 (2002).

<sup>28</sup> President Clinton's Executive Order 12,866, however, requires the OIRA analysis to be done in no more than ninety days. Exec. Order No. 12,866 § 6(b)(2)(B)-(C), 3 C.F.R. 638, 646-47 (1994), *reprinted in* 5 U.S.C. § 601 (2006).

<sup>29</sup> See Daniel H. Cole, 'Best Practice' Standards for Regulatory Benefit-Cost Analysis, 23 RES. L. & ECON. 1, 22-23 (2007).

<sup>30</sup> See, e.g., MATTHEW D. ADLER & ERIC A. POSNER, NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS 25-26 (2006) (declaring CBA to be a “welfarist decision procedure” and promoting a form of “weak welfarism”).

<sup>31</sup> See, e.g., Heinzerling, *supra* note 26, at 2064.

function has haunted CBA advocates. Without a way of weighting individual preferences, there is no single correct way of adding up these preferences to obtain a unique measure of social welfare. On this, Graham does not help us, but nor should we expect him to, given the extensive debate that has preceded his work without resolution.

We could, however, be more creative in the way that we attempt to address the indeterminacy problem, attempting to refine CBA so that benefits and costs more accurately reflect some fundamental notions of social welfare. One currently fashionable way to pursue this accuracy is in the area of happiness research.<sup>32</sup> Here, Graham gives unfortunately short shrift to this promising area of research, noting only that “[t]his line of research . . . raises as many questions as answers.”<sup>33</sup> If there is a fun way to prolong the debate between strong welfarists and categorical antiwelfarists, pursuing happiness research is the way to do it. Happiness research may yield a set of preference weightings that are exogenous to any specific environmental-policy problem and provide at least some keys to a way to construct a social welfare function of all of the pertinent stakeholders. This may seem like a pipe dream at this early stage, but such is the nature of research.

Happiness research, mostly empirical at this point, explores the mental states of individuals under different circumstances and in a universe of circumstances that range well beyond the monetary states with which economists usually work. But, whereas most economists would posit that most nonmonetary circumstances can be reduced to monetary value, happiness research explores errors that people systematically make in forecasting their own welfare, casting doubt on the ability of economists to monetize the value of different circumstances, since ultimately economists return to individual choices as their gold standard of preference revelation. If those choices are systematically flawed, then economists’ gold begins to look more like some less valuable metal.

However, as Adler and Posner have pointed out, happiness research does not undermine CBA.<sup>34</sup> In fact, if economists are as imperialistic towards happiness research as they were in annexing that field of psychological research pioneered by Herbert Simon, Daniel Kah-

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<sup>32</sup> See Graham, *supra* note 1, at 407.

<sup>33</sup> *Id.*

<sup>34</sup> Matthew D. Adler & Eric A. Posner, *Happiness Research and Cost-Benefit Analysis* 13-18 (Inst. for Law & Econ., Univ. of Pa. Law Sch., Research Paper No. 07-15, 2007), available at <http://ssrn.com/abstract=999928>.



neman, Amos Tversky, and Jack Knetsch as “behavioral economics,” then economics will have enriched itself yet again. And by opening up its methodological framework to new areas of empirical research, it will be refining itself and possibly setting the stage for a much broader public acceptance.

For example, happiness research has thus far shown that the relationship between money, wealth, and happiness (or “subjective well-being,” in the main line of happiness research) is much more complicated than a simple marginal-utility-of-money model could simulate. However, the relationship is generally positive, even if there are a number of factors that affect the magnitude of the relationship, and the now-growing body of literature reveals a number of findings that would support some preference weightings that could be incorporated in a CBA.<sup>35</sup> One important finding is that the correlation between income and happiness is weaker in wealthy nations,<sup>36</sup> suggesting that wealthy nations have something that moderates differences in income, such as education, literacy, longevity, or, quite possibly, political conditions such as human rights or equality. Another important finding is that increases in income in wealthy societies tend to increase happiness less than expected.<sup>37</sup> While this area requires more research, it has real implications for CBA. If it is true that equality and human rights moderate differences in income changes, then that might suggest some dramatic and concrete changes to the way we would estimate compensating variations in CBA. I can readily foresee providing an actual number as a weight for the income of poorer populations in evaluating potential rulemakings, directly addressing number one on Graham’s CBA research to-do list: ensure the poor are treated fairly.

There is another undercurrent to the CBA debate, one that has heretofore been neglected: the matter of language, power, and discourse. Here we could learn something from our postmodernist colleagues, who might have some insights about why CBA critics have fought so bitterly to keep the environmental debate out of the economic realm. It could be that these CBA critics suspect that shifting

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<sup>35</sup> For a review of this literature, see Ed Diener & Robert Biswas-Diener, *Will Money Increase Subjective Well-Being?*, 57 SOC. INDICATORS RES. 119 (2002).

<sup>36</sup> See Ed Diener & Carol Diener, *The Wealth of Nations Revisited: Income and the Quality of Life*, 36 SOC. INDICATORS RES. 275, 284 (1995).

<sup>37</sup> See Ed Diener & Shigehiro Oishi, *Money and Happiness: Income and Subjective Well-Being Across Nations*, in CULTURE AND SUBJECTIVE WELL-BEING 185 (Ed Diener & Eunkook M. Suh eds., 2000).

discourse into an economic realm is giving in to the structuralization of power and language in a way that is friendly to economic (read: industrial) development and hostile to environmental protection. In fact, many critiques of CBA have a decidedly postmodern flavor, evincing deep suspicion of an attempt to make environmental decision making more "objective," as the patina of objectivity is, in the postmodernists' account, an instrument of power.<sup>38</sup> It could be indeed, that the language of economics is such that it unconsciously places an onus of proof on less measurable values, such as environmental protection and human health. This would also explain why CBA critics have been so virulently critical of economists' attempts to address the incommensurability problem, such as by developing the contingent valuation methodology.<sup>39</sup> Although none of the CBA critics that I know of have come out as postmodernists, their categorical rejections of CBA are consistent with a postmodernist suspicion of objectivity and the formalization of power structures.

Although I continue to personally struggle with postmodernism, there is no doubt in my mind that the most satisfying response to postmodernist critiques is genuine curiosity about the alternative realities that may lie outside of one's own consciousness, personal experience, and intellectual training. Economists have not always been very good at this. Graham must surely admire Richard Posner, a kindred spirit when it comes to CBA, who has at least tried to place his own thinking in a broader spectrum of intellectual traditions, including pragmatism and postmodernism.<sup>40</sup> For his own part, John Graham has been better than most, and this article, with its serious treatment of criticism and its list of potential CBA reforms, is a strong step in the right direction. Fortunately for John Graham and environmental economists, the economic paradigm is not as far removed from the concepts of environmental protection and human health as, say, the concepts of law and justice have sometimes been to persons of color or to women in a male-dominated legal society. Environmental eco-

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<sup>38</sup> Ackerman and Heinzerling, for example, attempt to link fascism with economics by noting that Italian dictator Benito Mussolini's favorite teacher was the Italian economist Vilfredo Pareto. ACKERMAN & HEINZERLING, *supra* note 2, at 32-33.

<sup>39</sup> See, e.g., *id.* at 176 ("If whales were consumers, swimming up to the market with cash held in their fins, economists could interview them about their willingness to pay for not being harpooned. Instead, we are left with contingent valuation of the existence of whales as our only option for assigning a number to their lives.").

<sup>40</sup> See RICHARD A. POSNER, THE PROBLEMATICS OF MORAL AND LEGAL THEORY ch. 4 (1999).

nomics is not as fertile a breeding ground for postmodernist dissent as other areas of law and policy have been.

In this Response, I have suggested how Dean Graham's article might have been more focused, and I have explored some areas in which I believe his treatment to be incomplete, but only because this would seem to be the most useful way to interpret and build on Graham's work, not to reflect a negative review of this excellent article. As someone with administrative responsibilities myself, I am particularly impressed that someone who has been a dean for the past several years could have composed this article, which has become the latest word on CBA in many respects. Graham's calls for further research to refine CBA should be taken up in earnest by the economics-and-public-policy profession, and those calls should be received with more openness by the legal academy.

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