Perspectives
on current developments

Sugar Quotas: A Guide for the Economically Perplexed

As George Stigler wrote in these pages two months ago ("Economists and Public Policy," May/June 1982), there is no validity to the economists' standard complaint that the political world disregards the teachings of their science. To the contrary, he asserted, "if we look at any important economic policy of the state, we shall find that it takes account of whatever established knowledge economists possess, and perhaps of some that we do not possess." If economists do not like the results, it is usually not because the results were ignorantly produced, but because political actors are motivated by goals other than an abstract desire for efficiency, chiefly the goal of subsidizing some groups at the expense of others.

Stigler's point is well illustrated by the recent flap over the sugar import quotas imposed by President Reagan on May 5. If there is any government policy calculated to make economists feel slighted and put upon, it is the import quota. "Not year after year but generation after generation," to quote Stigler, economists have argued that import restrictions, as a means of helping domestic producers, are inferior to taxing a portion of the income obtained with free trade and using it to pay off the domestic producers directly. He might have added that given a choice between tariffs and quotas, economists will usually say that quotas are the less efficient alternative. Yet the Reagan administration has just embraced this worst of all protectionist schemes. Are the economists being ignored?

Probably not. Given the goal of subsidizing domestic producers—and given a few auxiliary goals of other sorts—the sugar import quotas may well have been the most direct and certain means available. Critics of the sugar quota decision may well dispute the administration's goals, but probably should not claim that it chose an inefficient way of achieving them.

Take, for instance, the possibility of raising the existing tariff on sugar. Since 1974, when the quota system in the old Sugar Act of 1934 expired, the United States has used variable tariffs to keep the price of imported sugar at or above a "market-stabilization price." The current stabilization price of 19.88 cents is derived under a complex formula from the support price of domestic sugar of 16.5 cents, which was written into Title IX of the Agriculture and Food Act of 1981.

However, there is a statutory limit on how high the variable sugar tariff can go. Under the current law, it must equal the sum of two components: (1) a flat per-pound duty that under the Trade Expansion Act of 1962 cannot exceed 2.8125 cents, and (2) a sliding fee that under section 22 of the Agricultural Adjustment Act of 1933 cannot exceed 50 percent ad valorem. Because of the effect on the second factor in this formula of the precipitous 1982 decline in world sugar prices, the variable tariff cannot now be raised enough to keep the market price above the market-stabilization price. Raising the tariff further would thus have required an appeal to Congress to change the laws, with the outcome uncertain at best.

The long-term welfare costs of tariffs on the economy are significant, but not very large compared with the total sums changing hands. In a 1980 Federal Trade Commission staff report, Morris Morkre and David Tarr estimated that the efficiency cost of the sugar tariffs would amount to $155 million over four years (in 1977 dollars). Since Morkre and Tarr assumed that a cost of $45 million would be incurred in shifting labor to other lines of work if the tariff were eliminated, they concluded that the net cost of the tariff to the economy was $110 million, or an average of $27 million per year.

For this relatively small sum in inefficiency loss, sugar tariffs allow the government to achieve a large amount of wealth redistribution from consumers to producers—as do quotas (though with a somewhat greater inefficiency loss). The reason is that sugar is quite price-inelastic: a large increase in price causes a small curtailment of demand. Assume, for example, that tariffs or quotas succeed in raising sugar prices here to the current market-stabilization price of 19.88 cents a pound and that the world price stays at 7.4 cents a pound, the average level recorded since the quota was announced. (In fact, the quotas have for the moment produced an even bigger spread between U.S. and world prices; as of July 9, the New York price was 21.8 cents and the world price 7.7 cents.) Then, assuming shipping costs of 1.5 cents per pound, the implicit subsidy to domestic producers would be just under 11 cents per pound, or more than $1.3 billion in all for the 11.6 billion pounds of sugar now produced domestically. (The difference would not be quite so large in practice, because world prices would rise if the United States reentered the market.)

This explains why a tax-and-subsidy program is unlikely to be taken seriously as an alternative to the tariffs and quotas. Aside from the political impossibility of openly proposing to give sugar growers $1.3 billion from the Treasury and then getting Congress to pass such a scheme, it is not even clear that the costs of running such a program would be cheaper than the $27 million dead-weight cost of tariffs or the doubtless higher cost of the current amalgam of quotas and tariffs.

Economists often declare that quotas are inferior to tariffs for two major reasons. First, not all quotas will be assigned to the lowest-cost foreign producers, leading to some inefficiency, and foreign countries will expend valuable resources jockeying in Washington for advantage. These costs are borne by foreign producers, however, and the latter may actually be of some benefit to this country, or at least to Washington officials and restauranteurs. Second, although fewer foreign producers will get to sell sugar to us, those who do will get a higher price than before, so that in effect a windfall value will be attached to their quota right. Since the quotas will be granted without charge to foreign countries, each of which will allocate them among its producers, the value of the quotas will represent a transfer from U.S. consumers to foreign producers. Some such countries will ship less than half as much sugar to the United States under the quotas, but will get half again as high a price for it—which, given that they can still sell the rest of their sugar on the world market, will make quotas more lucrative for them than free trade.

While it is too early to know for sure just how much the new quotas will be worth to those foreign countries, a likely minimum is $80 million in the second half of 1982. As before, we assume that sugar will sell for 19.88 cents a pound here and 7.4 cents a pound elsewhere. We also assume that tariff and ocean freight charges remain at the current level of 7.7 cents a pound and that the fourth quarter quota will be set at the same rate as that announced for the third quarter (840 million pounds). Under these assumptions the value captured by quota recipients will amount to 4.7 cents a pound, which, multiplied by 1,680 million pounds, will equal $80 million over six months or $160 million at an annual rate.

The actual figure will probably be higher than this for two reasons. First, the quotas may push the domestic price of sugar above the intended market-stabilization price. One reason to suspect that it may is that the 840-million-pound quota level announced for the third quarter of 1982 is far below the projected 1982 gap between domestic consumption and production of 7.6 billion pounds a year or 1.9 billion pounds a quarter (as taken from a June 1982 International Trade Commission report). Second, under the present legal formula, one component of the sugar tariff must drop when the market price rises above the stabilization price, reducing that item of expense to foreign producers.

Two American Enterprise Institute studies give some indication of how much sugar quotas were worth to foreign producers under the old Sugar Act. Ilse Mintz (1973) estimated the value at $398 million, and D. Gale Johnson (1974) estimated it at $326 million (both in 1977 dollars). The old quotas, however, may have been more stringent, and thus more expensive, than the present quota.

The question thus arises why the administration did not simply auction off the quotas, as it is permitted to do under the Trade Agreement Act of 1979. An auction would have been quite similar to a higher tariff in its effects, and the $160 million annual value of the quota would have enriched the Treasury instead of foreign producers.

The answer may lie in geopolitics. Specifically, the $160 million subsidy to foreign producers may be functioning in part as a substitute for the Caribbean Basin Initiative proposed by President Reagan in February. That initiative had hardly started, so to speak, when on May 19 the Senate Foreign Relations Committee voted 9-to-8 to transform it into a multilateral aid program run by the World Bank, a move that would afford the United States little control over the eventual disbursal of the funds. The sugar quotas may be an alternative, unilateral form of foreign aid: over a third of their value would now go to small countries in the Caribbean, Central America, and the West Indies, and they can be adjusted in the future to tilt even further toward these countries.

The Reagan administration could probably have achieved the same two objectives, subsidizing domestic producers and assisting friendly foreign countries, more efficiently if it could have imposed a higher tariff and used the proceeds for foreign aid. But that would have meant getting Congress to pass *two* new laws.

To be sure, it is a mystery to many why anyone except sugar farmers themselves would take such an interest in their welfare, since they do not seem so much more deserving than the much larger bloc of sugar consumers. But that is a reason to bring the goal itself into question, as distinct from the means of achieving it—which seem to have been selected in this case with all too much efficiency.

A Charter for Bus Reform

Earlier this year, Texas International Airlines began to advertise what it called "bus fares." A flight from Baltimore to Houston, for example, cost $20 less than taking the bus. Not surprisingly, Greyhound found it had to lower its interstate fares to meet TI's, so it applied for permission to the Interstate Commerce Commission—which took only a week. Then it applied to the Texas Railroad Commission for permission to lower its *intrastate* fares—and that took two more months.

For all the problems the airlines are having, the bus industry is eager to join them in deregulation. Bus companies have improved their ridership and financial health slightly in the past two years, but they are still worse off than in 1970. New entry into the industry has been liberalized somewhat by the ICC. The difficulty of entry and the burden of subsequent regulation remain substantial enough, however, that illegal operations—what might be called "gypsy buses," mass-carriage equivalents of New York's "gypsy cabs"—now carry a significant percentage of all traffic.

The Bus Regulatory Reform Act of 1982 is intended to remedy matters. The bill passed the House last November as H.R. 3663, and a more liberal version, approved by the Senate Commerce Committee this May, passed the full Senate June 30 by a vote of 85 to 10. Observers are predicting that the House will go along with most of the Senate's changes. Although both houses have thus far resisted some strong deregulatory proposals put forth by the Department of Transportation and the Federal Trade Commission, the bill does make some notable changes.

• *Entry*. Several of the landmark decisions by which the ICC under Darius Gaskins eased entry into the trucking business also applied to buses. Licensing procedures, however, can still be a major barrier. For example, back in November 1979 when Greyhound challenged an application by Trailways Tamiami to operate between Atlanta and Orlando, Tamiami obtained 423 witnesses in favor of the new service and Greyhound lined up 390 witnesses against. After a nineteen-day hearing at which 327 witnesses testified, an ICC panel granted the application. Another year was taken up by Greyhound's unsuccessful appeal to the full commission (after which Tamiami was allowed to begin service) and yet another by its appeal to federal court, which failed in October 1981.

Under the Senate bill, carriers applying for new routes would still have to show that they met federal safety and insurance standards. For special and charter service and for scheduled service to unserved communities, such "fitness" is all they would have to show. (DOT wanted to leave it at that for all new entry.) Most carriers applying for scheduled routes, however, could be challenged by competitors, and would then face an added inquiry into whether granting their request is "consistent with"—instead of "required by," as existing law

In Brief–

Public Confusion. A nationwide Gallup poll conducted for the League of Women Voters and the Bendix Corporation suggests that the American public isn't very well informed about federal regulation. The poll found:

- Half of those interviewed could not name even one federal regulation that affected them or their family.
- Only 17 percent knew that the executive branch is responsible for making federal regulations; 47 percent thought Congress was.
- Opinion was split evenly on whether federal laws or federal regulations dealing with an issue are usually made first.
- More than half either could not name any difference between federal laws and federal regulations or else believed there was little or no difference between the two.
- Of those who did name a difference, the most popular response was that laws were mandatory, while regulations were optional.

There is not much sign that the regulators who have been fostering greater "public participation" in the rulemaking process have reached the real public.

Carcinogen of the Month. In the ever-growing list of substances, processes, and conditions linked to cancer, the newest culprit is stress—otherwise known as anxiety, nervous tension, jitters, and the heebie-jeebies. Dr. Vernon T. Riley, chairman of the Department of Microbiology at Pacific Northwest Research Foundation, says that recent experiments reveal that stress may at least promote, if not directly cause, the onset and spread of cancer in mice and other laboratory animals.

"Two groups of mice carrying a breast cancer tumor virus were subjected to different environmental conditions," according to an account in the *Baltimore Sun*. "After thirteen months, tumors had appeared in 60 percent of those mice placed in a noisy environment on rolling, open racks." Of the mice who enjoyed a calm, serene environment, only 7 percent developed tumors.

The discovery of this whole new category of carcinogens opens up exciting prospects for the regulation of stress. There could be national standards for the ambient level of frustration in factories, offices, even homes; state implementation plans for the reduction of nameless dread; and distinctions between naturally present stress and artificially added stress.

Keep Those Complaints Rolling. The Federal Trade Commission's antitrust arm wants to do something fast about a problem that becomes more pressing every day: the complaint shortage. "FTC: Bureau of Competition Begins Intensive Effort to Generate Complaints" was the way the Bureau of National Affairs headlined a recent story. According to a 57-page progress report, the commission "has recently undertaken an intensive experiment of short duration specifically directed toward testing case-generation strategies." The commission's Bureau of Consumer Protection is also faced with a steadily shrinking backlog of cases.

To stave off the ultimate fear of any bureaucracy—a lack of problems to solve—lawyers from each of the commission's bureau sections and regional offices are being assigned to the quest for new complaints. One must hope that the Defense Department does not have similar plans for generating its own business.

Burned by the Freeze. A General Accounting Office report released in March confirms what armchair government-watchers have long suspected: across-the-board federal hiring freezes haven't worked. Investigators found that the four government-wide freezes imposed since March 1977, three by President Carter and one by President Reagan, have hampered agency operations in various ways without making a significant dent in federal employment levels.

Agencies evaded the freezes by resorting to such time-honored techniques as hiring part-time and temporary employees and increasing their use of overtime and outside contractors. Others, according to GAO, adopted the less imaginative tactic of simply ignoring the orders. Of course, the Office of Personnel Management exaggerated the success of the operation: while it claimed that the first Carter freeze had cut permanent full-time employment by 16,800 between March and June 1977, GAO found that 7,099 of that reduction was due to the routine summer furlough of Defense Department teachers.

Not surprisingly, GAO also found evidence that hiring freezes disrupted agency operations. The resulting costs to the government included such items as lost tax revenues and uncollected debts.

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has it—the "public interest." The burden of proof would be transferred to the protester, and the legislative history indicates that "public interest" is to be defined more broadly than the traditional test of "public convenience and necessity." Still, Congress is really just replacing one ambiguous standard with another and hoping for the best.

More troublesome yet is language in the Senate-passed bill that would instruct the commission to consider such factors as whether the granting of an application "would impair the ability of [the incumbent carrier] to provide a substantial portion of the regular-route passenger service which such carrier provides." The committee reports express a pious hope that the parade of passenger witnesses at hearings will come to an end with the abolition of the "public convenience and necessity" standard. But surely there remain at issue under the proposed new standard questions such as whether the new carrier would divert existing riders from the incumbent's lines, thus possibly harming other small towns served by the incumbent—which is a call for the same old parade. Like the trucking reform act passed in 1980, the bill contains a cryptic provision that the mere diversion of business will not, "in and of itself," be grounds for denial. That, as well as everything else, suggests that how much deregulation comes about will depend on how the ICC chooses to apply the law.

• *Ratemaking.* The Senate bill would deregulate rates for special and charter operations and establish a zone of rate freedom for scheduled operations. (DOT wanted to abolish rate regulation entirely after three years.) It would also end antitrust immunity for collective setting of "single-line" rates (those which a company offers over routes in its own system) and some "jointline" or "interline" rates involving two or more companies. Collective ratemaking would still be allowed for across-the-board general rate increases, the industry's preferred method of fare-setting. (DOT wanted to phase out this type of antitrust immunity too.)

• *Federal preemption.* The Senate bill would permit, though not mandate, federal preemption of state control over the intrastate portions of interstate routes. As it stands now, if a bus route runs from Buffalo through Cleveland and Toledo to Chicago, the Ohio Public Utilities Commission can (1) prevent it from carrying local Cleveland-Toledo traffic; (2) allow it to carry such traffic, but at a lower fare than it charges for comparable route segments elsewhere; and (3) refuse to let the carrier abandon the local route even if it drops the rest of the interstate route. Under the bill, state control over pricing and exit on the local segments of interstate traffic would continue, but after unsuccessfully exhausting state appeals, bus companies could apply to the ICC for relief. The commission could grant the relief if the state's action posed an "unreasonable burden on interstate commerce." This compromise may have succeeded in making preemption more politically palatable to the states, but it means that regulatory relief would be available only after cumbersome procedures. (DOT wanted to preempt state regulation entirely.)

Considering Greyhound's current dominance of the market, it is noteworthy how little fear has been expressed that that company will monopolize the industry under deregulation. This may reflect a belief that smaller companies are fully competitive on thin, rural routes; or it may be a judgment based on the airline experience, where smaller carriers have done better than large ones under deregulation; or it may be just a shrewd calculation that Greyhound will not tempt antitrust enforcers by growing much larger. Whatever its basis, the confidence on this point seems well justified. In Florida, which abolished all intrastate transportation regulation two years ago, there has been no trend toward monopoly, and smaller bus carriers have prospered. (See Robert Mabley and Walter Strack, "Deregulation: A Green Light for Trucking Efficiency," p. 36.)

While the deregulatory features of the bus regulatory reform bill are limited, experience in other industries indicates that the camel's nose or domino principle has strong application to regulatory reform; after the first reform bill is enacted, pressures mount for further liberalization. Four years after Congress passed the Railroad Revitalization Act of 1976, it came back to pass the more liberal Staggers Rail Act. Since enacting reforms in airlines and trucking, Congress has debated, though not yet passed, an early sunset of the CAB, and it is expected to consider truck reforms next year, including a possible sunset of the ICC. The Bus Regulatory Reform Act should thus be seen as the first step in a process: while not as sweeping as the Airline Deregulation Act, it may contain the seeds of greater change yet to come.

Antitrust and Travel Agents: Immunity with Reservations?

In many regulated industries—from shipping to public utilities—one of the benefits that it is within the power of the federal regulating agency to confer is immunity from the antitrust laws. Under some statutes, such as the Shipping Act, the agency's power to confer that immunity is explicit; under others it derives from the so-called doctrine of primary jurisdiction, which gives the agencies the first and often final say over the extent to which their substantive statutes implicitly modify the normal "rule of reason" standards of the antitrust laws.

When regulation is eliminated through repeal of the substantive statute, the antitrust immunity of course terminates as well. But in the current era of deregulation through agency refusal to use continuing statutory authority, there is a possibility that the previously regulated industry may, so to speak, keep the *quid* even though it has gotten back the *quo*. That is to say, an agency may eliminate most or all of the constraints that it had previously imposed, but still continue the antitrust immunity. On June 1, a CAB administrative law judge recommended precisely this course with respect to the airlines in their relations with travel agents; the CAB will review that decision later this summer.

Three years ago the CAB initiated an investigation of the Air Traffic Conference (ATC)/ International Air Transport Association (IATA) "conference" system of accrediting travel agents. Under that system, airlines collectively set and enforce accreditation standards for the nation's 18,000 travel agents. Some of these standards are of the sort frequently encountered among professional groups: agents must meet financial requirements, have a certain number of years of experience, and maintain certain facilities. Airlines, for their part, agree not to pay commissions to unaccredited agents. (While the international agreements do not contain such a provision, there is enough overlap between the two conferences that the effects have been similar.)

In the conferences' scheme of things, the role of the travel agents is to "promote and sell" air transportation, with the emphasis on "promote." The agreements are therefore intended, as James C. Miller III testified in the proceeding (before he joined the Reagan administration), to "reserve to air carriers 'easy' sales and to confine to travel agents only 'difficult' sales." For instance, a large chunk of sales for which customers already know where and when they want to travel is reserved for the airlines by an IATA rule that prevents agents from locating in or near airports. Similarly, business travel departments, which plan flight schedules and write tickets in virtually the same way as travel agents, cannot be accredited as agents (and thus cannot receive commissions) because of a rule forbidding agents from doing more than 20 percent of their business with a company under the same ownership. Deregulation may have weakened the effectiveness of this rule, since the business travel departments may now bargain for special discounts, although they cannot share in the bargaining power of the agents.

That this system successfully divides "easy" from "hard" sales is evidenced by the fact that the cost to airlines of selling tickets directly is only 3 to 5 percent of the purchase price, while the commission they pay to agents is on the order of 10 percent. Customers, of course, pay the same rates whether or not they require help from travel agents—so that those who do need such help are in effect subsidized by the "easy" customers who do not.

Naturally this redistributive effect is accompanied by some dead-weight loss: the ATC/ IATA agreements prevent airlines from exploring promising new ways of marketing tickets. World Airways, a major carrier that does not belong to ATC, has sold tickets through Ticketron outlets since 1978. Such "no-frills" retailing, reflected in lower fares (as it is in World Airways' case), can offer significant savings to passengers who already know where and when they want to go, just as discount stockbrokers with no research departments have saved "do-it-yourself" investors millions in recent years.

The airlines and agents argue that antitrust immunity is all that stands between the travel business and utter chaos. British Airways, for instance, stated that "the very existence of [British Airways] in [the United States] in anything like its present form is dependent upon the sales representation we receive under the IATA program." The relationship between airlines and agents, they argue, rests on the trust engendered by the common accreditation system. Agents are entrusted with blank ticket stock, accepted by all member airlines, that could easily inflict large costs on airlines if misused. Moreover, if individual airlines had to accredit their own agents, airline travelers would ultimately be burdened with the higher costs, and in addition would have no assurance that a ticket written on one carrier could be used ("interlined") on another.

Administrative Law Judge Ronnie A. Yoder's decision reflects these concerns. Subjecting the system to the antitrust laws, he argues,

> would undermine intercarrier confidence in the travel agent network and in the reliability of interlining . . . threaten the com-

> petence and professionalism of the travel agent industry as a whole [and] reduce the availability of travel agents.

After listing a series of "what ifs" concerning the possible misdeeds of "irresponsible, incompetent or careless" travel agents, Yoder concludes:

> Certainly nothing in this record would justify risking the current air transportation marketing system in reliance on assertions that the Board should disapprove the agreements and trust other market forces to solve the resulting problems "in the long run."

References to things like "intercarrier confidence" are reminiscent of the CAB of many years ago.

Yoder's 200-page decision notes that under the agreements airlines are allowed to sell tickets to resellers (who, unlike agents, assume the risk of unsold inventory) and recommends disapproving the IATA curb on agents' locating near airports, as well as some other clearly anticompetitive conference standards. But it is ambiguous on the issue of retailing innovations. The most troubling passage, to deregulators, is one that discusses the role of Ticketron and notes that "the distinction between agent and non-agent status may be difficult to resolve in any given case." Relying on Ticketron's own assertion that it would be "economic insanity" for anyone to try to compete with it for the no-frills market, the decision recommends that "the Ticketron ticketing operations . . . be incorporated as a *sui generis* exception" to the rule that airlines may sell tickets only through agents. Thus a regulatory agency that many people thought dead is to consider *creating* a national monopoly in a potentially important market: no-frills airline ticket sales.

Permitting all airlines to sell through other Ticketron-type outlets, by itself, may not lead to much innovation. For one thing, the antitrust immunity would still permit the ATC to exclude such outlets from the clearinghouse that settles carrier/agent accounts, thus forcing those outlets to adopt costly special arrangements for payment. Even ending antitrust immunity completely might not change matters drastically. Indeed, stripped of the more restrictive provisions—those that the courts would interpret as a collective refusal to deal—the agreements could probably continue in much their present form. Critics of the conference system also allege that the agents can enforce their will informally: any airline that tried to sell tickets through other outlets might experience a sudden drop-off in its sales through agents. Since agents account for well over half of total airline sales, such a threat might suffice to prod a straying airline back to the fold.

The apparent power of agents to discipline airlines—even though it is the latter who write the rules for the system—illustrates the difficulty of determining just which side, in a bilateral monopoly like ATC/IATA, has the real market power. Under regulation, the airlines used the ATC/IATA conference system to set commissions collectively. Since commissions were allowed to float in 1978 (for international routes) and 1980 (for domestic routes), they have risen rapidly, from around 7–8 percent to about 10 percent today. At the same time, there is evidence that travel agent costs have not risen dramatically—which may indicate that the old system was protecting the airlines from the market power of the agents, rather than vice versa.

Active Judges and Passive Restraints

The June 1, 1982, decision of the U.S. Court of Appeals for the District of Columbia Circuit in the so-called airbag case, *State Farm Mutual Automobile Insurance Company* v. *Department of Transportation*, is certain to be one of this year's most significant judicial pronouncements in the regulatory field. The court's specific holding—invalidating NHTSA's repeal of the automobile "passive restraint" requirements promulgated by the Carter administration—is of immediate importance to auto manufacturers, insurers, and buyers. But of even broader concern is the basis of the holding, a theory of judicial review and of required administrative process that may impede all deregulatory initiatives by agencies.

The controversy underlying the case is so old that it no longer excites. Department of Transportation Standard 208 was issued in 1967, requiring seat belts in all cars. Finding that people did not use the darned things, the department began a new rulemaking in 1969 to consider whether to require "passive restraint systems," defined as protective systems that require "no action by vehicle occupants." That standard was issued in 1970. It was successively modified many times thereafter, the effective date being pushed back with each modification so that a passive restraint requirement never did enter into force. (What did enter into force, in Ralph Nader's finest hour, was the interim requirement—until manufacturers could tool up for passive restraints—of an "ignition interlock" device making it impossible to start the vehicle unless seat belts were engaged. That much-hated feature, and its cousin the continuous buzzer, were banned by Congress in 1974.) Shortly before the 1976 effective date, Ford administration Transportation Secretary William Coleman began a new rulemaking to reconsider the issue, and ultimately suspended the requirements in favor of a proposed "demonstration project" involving up to 500,000 cars. Four months later Coleman's successor, Brock Adams of the Carter administration, reopened the rulemaking, and subsequently issued a new mandatory passive restraint rule with an effective date beginning (for large cars) in the 1982 model year. Once again, however, the promised day never came. Adams's successor, Drew Lewis of the Reagan administration, reopened the rulemaking once again in February 1981; two months later NHTSA ordered a one-year delay in the application of the standard to large cars; and in October 1981 it promulgated a new standard eliminating the passive restraint requirement altogether. That action was the subject of the present case. Four aspects of the court's lengthy opinion merit comment:

The Variable Standard of Review. The Administrative Procedure Act (APA) sets forth only one standard for judicial review of ordinary agency rulemaking. Agency action may be set aside if it is "arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law." Where Congress wants stricter review, as it does under a number of regulatory programs, it specifically provides that the rules must be supported by "substantial evidence." (Never mind that it is hard to see why a rule would not automatically be "arbitrary" if there were no substantial evidence to support it; it is absolutely clear that Congress *intends* the "substantial evidence" test to be stricter.)

In the air-bag case, however, the D.C. circuit follows several recent appellate decisions in asserting that the "arbitrary and capricious" test itself is not one but many. (As the court's opinion puts it, "the same verbal standard of review should be given different scope in different contexts.") This principle may not be as transcendent as the Trinity, but it is at least as mysterious; it defies not merely language, logic, and legislative history, but even a Supreme Court opinion that rejected a similar attempt to give variable content to the "substantial evidence" test.

The only thing that can be said in favor of the D.C. circuit's position on this point is that it is true. There is not the slightest doubt that the "arbitrary and capricious" test, like the "substantial evidence" test, the "preponderance of the evidence" test, the "reasonable man" standard, the "probable cause" requirement, or any other decisional criterion that the mind of man or lawyer has been able to devise, is *in fact* stretched to varying degrees, in one direction or another, as the needs of reality and the equities of "hard cases" seem to require. That is, some would say, part of the play in the joints that any legal system must possess. But courts normally have the good sense and decency to lie about it, recognizing that in this context, as in many, hypocrisy is the beginning of virtue. With formal acknowledgment of a multiplicity of standards, occasional stretching of the law is replaced by regular eccentricity and, ultimately, complete disregard of the legislative command. We doubt that the Supreme Court will support this explicit rewriting of the APA.

Deregulation Subject to Strict Review. Still, what threat could such a principle possibly pose to deregulation? Even if the "arbitrary and capricious" test turns out to be a sliding scale rather than a standard, surely an agency's elimination of burdens upon private parties—like an agency's failure to impose burdens in the first place—must fall within that portion of the scale giving the administrator broadest leeway, and the courts the narrowest scope of review.

Not so. The key to the scale, it turns out, is the existence of "danger signals"—alarum bells audible to the trained judicial ear—which convey the message that strict court scrutiny is needed. One of these klaxons is "sudden and profound alterations in an agency's policy." The court acknowledges that it makes more sense for this particular bell to ring in the case of adjudication than rulemaking, since general adherence to precedent is the essence of a fair and responsible case-law system. But even in rulemaking, the court asserts, sudden and abrupt change is a danger signal because it suggests "that the will of Congress is being ignored." This reasoning is not explained, which is unfortunate since it is counterintuitive. The institutional inertia of administrative agencies being a well recognized and thoroughly documented phenomenon, one would expect that, *au contraire*, a sudden and abrupt change of policy is more likely an indication that Congress *is* being listened to!

The court's opinion seems to indicate that the mere occurrence of an abrupt change in policy is itself enough to create a suspicion that Congress is being ignored, which suspicion is itself enough to trigger strict scrutiny. The opinion goes on, however, to a particularized examination of the "will of Congress" with regard to passive restraints—a will that the court discerns not in the language or legislative history of the statutory text under which NHTSA was acting, but in Congress's failure to overturn the passive restraint rule by legislation or legislative veto, and in the legislative history (or, more precisely, nonlegislative history) of proposals *almost* enacted which would have mandated passive restraints. "Reading this legislative history as a whole," the court concludes, "suggests a congressional commitment to the concept of automatic crash protection devices . . . that we may not take lightly. . . . [W]e conclude that rescission of the standard must be subject to 'thorough, probing, in-depth review' lest the congressional will be ignored."

One is tempted to criticize this portion of the opinion merely on the ground that it is invalid to rely on scattered statements in the course of legislative nonaction as an indication of legislative intent. Or on the ground that, to the extent congressional intent never embodied in a law has any relevance (which perhaps should be not at all), then surely it is only *present* congressional intent, which in the case at hand is most clearly indicated by the failure of either house to take any action opposing the highly publicized and controversial repeal of the passive restraint requirements. But let all that go. The *real* novelty in the concept of violation of congressional intent as a "danger signal" is the consequence that the court attaches to it. If there really was, in any valid and operative sense, a "congressional commitment to the concept of automatic crash protection devices," then surely the consequence should be not an increase in the D.C. circuit's ability to scrutinize the reasonableness of NHTSA's repudiation of that concept, but rather—quite simply—invalidation of NHTSA's action, reasonable or not. But of course the court does not assert the existence of any such operative congressional action—merely that "the [passive restraint] standard has come as close as an agency-made regulation can come to being affirmatively endorsed by Congress, without Congress actually having done so." Only a sound sense for the hackneyed prevents one from mentioning pregnancy. This notion of an ineffable, "almost," congressional will, not strong or clear or legitimate enough to bind an agency outright but somehow effective to make an agency's action smell bad and thereby expand the scope of judicial review, is extraordinary.

Shifting the Burden of Proof. It is not clear whether the last two novelties of the air-bag opinion result from the application of a heightened standard of review on the basis of the theory just expounded, or rather are totally independent principles that would be applied to any rescission of a rule, even when "thorough, probing, in-depth review" was not indulged in. The first of these is the principle that a rescission is arbitrary unless the agency establishes that the preexisting rule will not be desirable. It is not enough, according to the D.C circuit, merely to establish that there is no reason to believe that the preexisting rule *will* be desirable.

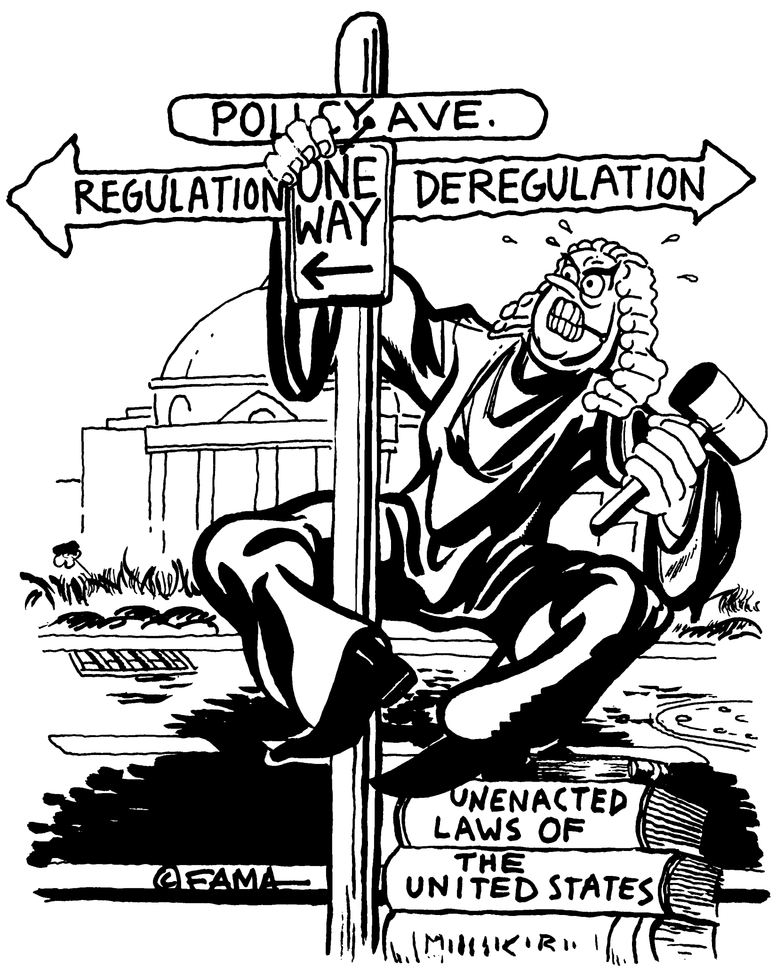
In the air-bag case, this principle is applied to the crucial question of whether the passive restraint standard would result in increased use of seat belts. Although automakers could have met that standard by equipping cars with either automatically engaging ("passive") seat belts or air bags, NHTSA concluded (and the court did not dispute) that the overwhelming majority of new cars would be equipped with the former. It also concluded (and the court did not dispute) that the standard would be worthwhile only if the passive belts (which under the standard could be detachable) would increase nationwide seat-belt use by at least 13 percentage points, from 11 percent to 24 percent. Data on the use of passive seat belts in VW Rabbits and GM Chevettes showed an increase of more than this amount, but NHTSA found it impossible to generalize from those data for a number of reasons: (1) the data pertained to subcompact cars, where belt usage is always higher, (2) Rabbit owners are typically better educated and more affluent than the population at large, (3) some of the models had certain coercive use features not required by the standard, and most important, (4) the owners voluntarily paid for the passive belts and so would be less likely to detach them.

The D.C. circuit did not contest the unreliability of the data on increased use, but that was still, it said, no justification for abandoning the passive restraint rule, because "*the question is not whether evidence shows that usage rates will increase by the necessary amount, but whether there is evidence showing they will not*" (emphasis added). Without such evidence, the rule might be temporarily suspended or amended, but "the regulatory program [could not] be abandoned altogether."

This part of the court's opinion is lent some credibility by what might be called the procedural inertia of our laws, which favors the regulatory status quo, with no bias toward either the regulated or the unregulated state. That is to say, neither may an unregulated field be regulated, nor a regulated field be decontrolled, without conducting a rulemaking proceeding. As far as the Administrative Procedure Act is concerned, the promulgation of a rule and the repeal of that rule are equivalent.

But parity of process does not necessarily entail parity of substance. Granted that a rulemaking proceeding must be conducted to impose regulation and to eliminate regulation alike, it does not necessarily follow that in both types of proceeding the burden of justification rests on the proponent of change. As far as the *substantive* inertia of our laws is concerned, that favors not the status quo but private autonomy, whether or not that is what the status quo prescribes. That is to say, private freedom can neither be constrained *nor continue to be constrained* without good reason. The D.C. circuit acknowledges this. "Implicitly," it says, "the perpetuation of a regulation involves a decision that its continuation is worthwhile, and reasonable decisionmaking requires that this too be supported by reasons."

If, then, all of the evidence in a proceeding to consider the revocation of a rule fails to establish the utility of the rule, why must the agency continue to search further, for evidence that positively *proves* the rule to be ineffective? There might be reason for such a requirement if the evidence to be considered were within the exclusive control of the agency—so that a malevolent agency bent on scuttling a desirable



rule could do so by simply failing to introduce into the proceeding any demonstration of the rule's beneficial effect. But that is not the case under the APA. NHTSA could not have prevented *any* person from introducing proof that detachable passive-restraint belts would increase seat-belt usage the necessary 13 percentage points; it found (and, in the court's judgment, reasonably found) that no one had done so. Given this protection against malevolence, and if it is indeed unreasonable to continue a regulation that is not affirmatively found to be useful, how can it possibly be considered "arbitrary" to revoke a regulation that the agency properly finds no evidence to support? Either the court's concession of the presumption in favor of private autonomy or the court's requirement of proof of nonutility must be wrong.

Mandatory Consideration of Other Regulatory Alternatives. Even if an agency can sustain the burden of proving that a regulation will not do any good, it is still not yet out of the woods. According to the D.C. circuit's opinion in the air-bag case, it cannot then simply walk away and leave the area (shudder) unregulated. Just as President Reagan's Executive Order 12291 requires agencies to regulate only incrementally, choosing in each case the "least onerous alternative" that will produce the desired result, the D.C. circuit opinion creates a rule of incremental *de*regulation—allowing an agency to revert to the unholy state of utter deregulation only when all more onerous alternatives have been exhausted.

Thus, said the D.C. circuit, even if NHTSA *had* proven that the existing rule would *not* increase seat-belt use by 13 percentage points, it would not have been justified in repealing the rule, but would have had to consider other options, such as (1) requiring the seat belts to be nondetachable, and (2) eliminating the seat-belt option entirely, and requiring air bags for all cars.

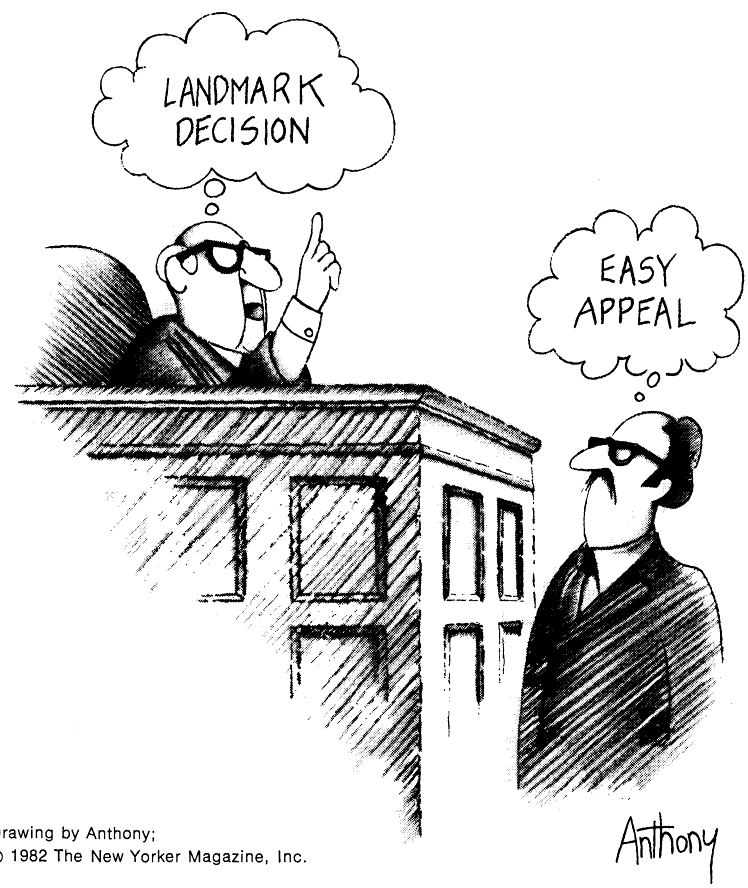
This portion of the court's opinion has intuitive appeal. When regulation of a certain type or at a certain level is seen to be unjustified, surely a rational decision maker will not immediately abandon regulation entirely, but will first search for other alternatives to achieve the same result. And failing to do so can properly be called "arbitrary."

This assumes, however, that the decision maker *wants* to achieve the goal which the regulation sought to achieve, or that he has some obligation to continue the pursuit of that goal. And that is the crux of the matter. The keystone of this portion of the opinion is the court's assertion that "if NHTSA did not believe the standard as written would fulfill the standard's goals, its foremost obligation was to consider whether an amended standard could." If this refers just to the statutorily prescribed goal of highway safety, it would of course be correct. But it does not. It refers to one particular means of achieving that more general goal—namely, the prescription of effective passive restraints. At that level, it is not self-evident why the goal pursued by an earlier administration must be pursued by its successors.

Generally speaking, regulators have no obligation to implement particular modes of regulation or to focus on particular segments of commerce within their statutory jurisdiction. If, for example, the Federal Trade Commission chose never to devote its attention to used car dealers, it is most unlikely that any court would say it had to do so—even if a plaintiff was prepared to prove that this area contained more abuses and was more in need of regulation than other fields the commission had already entered. Similarly, it is unlikely that any court would have forced NHTSA to consider imposing passive restraints if NHTSA had never done so. In other words, the establishment of intermediate regulatory objectives and targets leading to the prescribed statutory goal is largely (in the nonpartisan sense) a political judgment. What the air-bag decision asserts is that the *dis*establishment is not. To personify the matter: we can decide to pursue a "passive restraint" approach to automotive safety by electing Jimmy Carter, but cannot abandon it by electing Ronald Reagan.

It is difficult to understand why the court felt constrained to create this asymmetry. At most, the APA requires that the particular rule be determined to be not demonstrably effective before it can be revoked; nothing requires that a rulemaking then be conducted to fill the resultant void. At that point the choice between passive restraints and other approaches could have been recommitted to the political process.

Perhaps the court's position on this point is not quite as sweeping as has just been suggested, because it is all bound up with the notion of Congress's "almost" legislation—so that the court speaks at times as if it is not the more general objective of automotive safety but the specific program of passive restraints that Congress itself has prescribed. That is why the last two sentences of the opinion make so little sense: "If NHTSA finds nonarbitrary reasons for rescinding the standard, of course, its action will be affirmed. Absent such reasons, or intervening action by Congress, NHTSA may not arbitrarily veer from the course the Congress has set." One would have thought that NHTSA cannot even *non*arbitrarily veer from a course that Congress has set. But of course earlier jurisprudence provides no examples of "almost" legislation.



Drawing by Anthony;

In the world of action, as opposed to ideas, the air-bag opinion may be inconsequential. Courts are superb obstacles, but most ineffective spurs—a quality that may have something to do with the fact that they were never intended to be the executive branch. In the present case, the court could hardly mandate the continuation of the current passive restraint rule, given the fact that there was no evidence it would be effective. Instead, it gave the agency thirty days "in which to submit a schedule for resolving the questions raised in this opinion, leading either to the rescission or suspension of the standard or to a judicially approved schedule for the effective implementation of that standard or an amended standard." In other words, the court did not mandate anything but the spinning of more wheels.

Really nice questions, adumbrated in the present opinion, lie ahead: When the agency rejects nondetachable passive-restraint seat belts on the ground that the intrusion on personal freedom (in the most literal sense) is too high a cost to pay, can that justification be sustained? When it rejects air bags on the ground that even at the lowest estimated cost—and even if that cost will be more than recovered over the vehicle's life in lower insurance premiums—the government has no business requiring such substantial mandatory expenditures for a product that could be made available (at a higher price) voluntarily, will that justification be sustained? Or what if the agency simply says: "We regard our proper governmental function to be to make sure that no defective or ill-designed features of cars *cause* accidents, and to make sure that all self-protective features are available on the open market; all the rest is nannyism"? There is language in the opinion which suggests that none of these justifications will satisfy the D.C. circuit—but that language ultimately hinges on a ghostly legislative intent that the Supreme Court may not believe in. The D.C. circuit's last major attempt to mandate a regulatory program, which involved Federal Communications Commission supervision of radio format content, came to a bad end (see "Reversing the D.C. Circuit at the FCC," Perspectives, *Regulation,* May/June 1981); this one is likely to be buried alongside it.