# Perspectives
## on current developments

### Taxis, Jitneys, and Mass Transit

Most urban areas are plagued with transportation problems and, until now, the federal response has emphasized large mass transit systems—bus and especially rail. Little attention has been given to what could be, for many places, a much more efficient mode of urban transportation—taxis and jitneys.

Almost everywhere entry into the taxi business is strictly limited (the major exceptions being Atlanta, Honolulu, and Washington, D.C.). A few cities (including Cleveland, Dallas, Los Angeles, and Philadelphia) franchise just one company. Most license several companies but still limit the number of cabs. Some exercise this control by selling a limited number of new medallions (taxi permits) each year to the highest bidder(s) and allowing these medallions to be resold to other operators. But many of these cities have not issued new medallions since the end of World War II—so that the existing ones often change hands at very high prices, sometimes exceeding $40,000. Other regulations (such as special equipment requirements and rate setting) further limit the taxi business. Consequently, many cities have fewer taxis than they would have if entry were free.

Even tighter restrictions apply to the jitney market. Jitneys are commercial vehicles that follow less regular routes and schedules than buses but that do not provide the on-demand point-to-point service offered by taxis. A jitney operator may collect a number of passengers going in a general direction before making the major portion of the journey and may make up the route as he goes along, depending on where his passengers are going. The result is a trip that usually costs less and takes longer than going by cab, but costs more and takes less time than going by bus.

In most cities jitneys have been outlawed —usually at the insistence of the taxi and bus companies. In others, they have been restricted to certain routes to limit their competition with buses or rails. Those that have survived—in Harlem and in certain parts of Chicago, for example—tend to be part of a "gray market," unlawful but tolerated.

Constraints on taxi and jitney services are not only economically inefficient, but also serve to restrict opportunities for would-be entrepreneurs (especially members of minority groups). They also explain part of the demand for federal aid to mass transit. In other words, if the taxi and jitney markets were made more competitive and efficient, there might be less "need" for federally funded transit projects.

In July 1977 Senator S. I. Hayakawa (Republican, California) introduced an amendment to the National Mass Transportation Assistance Act of 1977, entitled "Minority Employment Opportunities in Transportation" (see *Congressional Record*, June 23, 1977, pp. S 10567-81). Designed to encourage localities to remove restrictive regulations on taxis and jitneys, the amendment would have prevented any locality from receiving federal mass transit funds if its taxi and jitney regulations exceeded certain standards. Specifically, it would have permitted safety standards for operators and vehicles and insurance and licensing requirements for operators, but not the setting of minimum rates and the fixing of routes. According to Senator Hayakawa, the amendment would have created employment and business opportunities for low-skilled individuals with little capital. The technical skills needed to drive a cab or jitney, the capital investment required for a down payment on a vehicle, and the insurance deposit are all relatively small.

Two major objections are typically made to this type of proposal. The first is that if taxis and jitneys become more accessible, mass transit ridership will decline. (This is a form of the argument that says the way to make mass transit systems viable is to force people out of their cars.) Thus, cities that have invested their

own and some federal funds in mass transit systems might face a difficult dilemma: get along without federal assistance or accept it but see mass transit ridership decline. The amendment does not address this issue, though it may be important to bear in mind that the argument makes far more sense where systems are now in place than it does where they are just *planned*; and it makes more sense in the case of rail installations than it does where the mass transit mode is bus and the system can be contracted or redeployed more readily.

The other major objection is that people who have purchased medallions could suffer losses; these losses would be inequitable and those who would suffer them would certainly constitute a major source of opposition. (For an analysis of the value of operating permits in a similarly constrained transportation market, see Milton Kafoglis, "A Paradox of Regulated Trucking," in *Regulation*, September/October issue.) The amendment would have dealt with this problem by providing compensation based on the length of time a medallion has been held—90 percent of the amount invested if the medallion were purchased within the last year, 79 percent if purchased more than one but less than two years ago, and so on down to zero where the purchase was made over seven years ago.

Senator Hayakawa's amendment was not voted on in the Senate. At the request of the chairman and the ranking minority member of the subcommittee with jurisdiction over federal mass transportation programs, it was withdrawn, to be reintroduced as a separate bill and considered in hearings before the subcommittee early next year. The proposal's novelty and potential impact are sure to make it a controversial issue in the next session of Congress.

## Should Consumers Pay for Lobbying Expenses?

The Civil Aeronautics Board is proposing to require airlines to report the sums they spend on lobbying and related activities and to exclude these sums from the costs on which rates (passenger and cargo) are based. The board's proposed rule came in response to a petition from the Aviation Consumer Action Project, a Nader-affiliated organization formed to represent the interests of airline passengers. The ACAP argued that consumers should not be required to pay for lobbying (the advocacy of corporate interests) or for institutional advertising (that designed merely to enhance the industry's public image). For example, according to the ACAP, the bulk of the $7.47 million in annual dues collected by the major industry group, the Air Transport Association, goes for these two purposes and thus should not be included in the rate base.

In answering ACAP's petition, the CAB tentatively agreed that the costs of advancing corporate interests should be borne by stockholders and not by airline passengers and shippers. In order to find out how much money is being spent on such activities, the board proposed accounting and reporting guidelines and asked for public comment. When the information is in, the board intends to determine whether lobbying and institutional advertising expenses should be excluded and, if so, to what degree.

The position advanced is not new. The Federal Energy Regulatory Commission (formerly the Federal Power Commission) has excluded lobbying expenses from its companies' rate bases for years. But the amounts involved are so small that the FERC computer does not put them in a separate account. Similarly, the Federal Communications Commission now requests certain of the companies it regulates to file quarterly reports listing expenditures meant to influence public opinion on the proposed Consumer Communications Reform Act, commonly known as the "Bell bill." According to FCC staff estimates, the industry has spent over $4 million to support this bill in the last two-and-one-half years. Although the FCC has yet to issue a rule excluding lobbying expenses from rate considerations, the agency is keeping an eye on who is spending how much.

Whatever its justification, the goal of ensuring that consumers do not in some sense pay for lobbying expenses and institutional advertising is difficult to accomplish, especially for the airlines. One reason is that cost disallowances affecting a firm's profitability—either directly on the balance sheet or indirectly through curtailed lobbying and institutional advertising—also affect its cost of raising financial capital. Thus one form of cost—lobbying and institutional advertising—may be re-

duced, but another—interest expense—may rise.

Another reason the goal is not likely to be reached is that the airlines operate in an environment that can be characterized as *regulated competition*, whereas the FCC and FERC, in the two cases mentioned above, are regulating firms that operate as government-sanctioned *monopolies*. The control in these two cases is fairly direct: average cost (excluding the expenses at issue) is added to a pro rata share of the "reasonable" return on investment to come up with the allowable rate. The control over regulated competitive industries is much less direct. Once the rate has been established (based on "appropriate" costs), the firms engage in nonprice competition to determine the precise character (quality) of the service provided. The effect of disallowing certain cost elements in the rate base is to reduce nonprice competition, resulting in a lower quality of service. In that respect, lobbying activities and institutional advertising are still "paid for" by consumers and not by the companies.

With some allowance for oversimplification, rate regulation in the airlines works this way: The CAB determines the per-passenger cost of providing a "standard" service, assuming that 55 percent of the seats are filled, that "standard" seating configurations are used, and so on. To this per-passenger cost is added a pro rata reasonable return element to come up with the approved passenger fare. Now, what happens if some cost elements in the rate base are excluded? From the airlines' point of view the resulting fare is lower than what has been necessary to provide the "standard" service. (Airlines view lobbying and institutional advertising as legitimate business expenses.) Thus, they will decrease their nonprice competition, cut back on scheduling, and raise the percentage of seats filled—in order to lower the average cost per passenger. Therefore, a policy of excluding the expenses at issue from the airlines' rate base would not give consumers the same service at a lower price, but a lower quality of service for the lower price.

Without question, there is considerable appeal to the argument that it is unfair for consumers to pay for industry's efforts to prevent reforms that might result in lower fares and improved service. Yet, one wonders whether it is even possible to impose these costs on stockholders under our current regulatory regime—and the same goes for other regulated competitive industries such as trucking, oil production, and insurance. It will be interesting to see how the CAB's new chairman, Alfred Kahn, and the CAB's newest member, Elizabeth Bailey—both renowned economists—grapple with this one.

## Toxic Substances Control Act: EPA's Initial Effort

From plastics to playgrounds, pesticides to pajamas, chemicals created by industry or extracted from nature abound in our lives—mostly for better, sometimes for worse. Experience has shown that at least some of these chemicals have long-run harmful effects—Tris and benzene, for example. Rather than dealing with such problems on an ad hoc basis, many would prefer that all chemicals be screened for toxicity before they enter the market.

Accordingly, Congress enacted the Toxic Substances Control Act of 1976. Its major objectives are to provide the public with better information on the risks of chemicals, to provide for routine screening of all new chemicals introduced into the environment, and to regulate (and in some cases prohibit) the manufacture and sale of especially dangerous toxic substances. Specifically, the Environmental Protection Agency must compile an initial inventory of all chemicals manufactured or processed commercially during the three years prior to January 1, 1978—no small task, given the estimated 30,000 chemicals on the domestic market. After EPA completes its inventory, manufacturers intending to produce chemicals not appearing on the list (or to produce listed chemicals for "significant new uses") must notify EPA ninety days before beginning commercial production. If the available information on the chemical is not adequate to enable EPA to evaluate its health and environmental effects, or if the chemical is suspected of posing an unreasonable risk, EPA may require the manufacturer to develop test data before the chemical is approved for manufacture or distribution. In addition, EPA is directed to review certain existing chemicals—some that it will choose and others that will be recommended by an

eight-member committee drawn from various health, safety, and science agencies of the federal government. If EPA finds that any of these chemicals pose an unreasonable risk, it may regulate its manufacture and sale.

On March 9, 1977, taking its first step to implement the act, EPA issued a draft proposal outlining the procedures manufacturers should follow in reporting the chemicals they have produced or processed during the past three years. A revised proposal of August 2, 1977, limited the reporting requirement to roughly 20,000 basic chemical and petroleum refining producers but added the requirement that manufacturers (except for very small businesses) list not only chemical substances, but where they were produced and in what quantities. EPA's tentative position is that this additional information is necessary if the agency is to identify the sources of toxic chemicals (say, in an emergency) and to rank potentially hazardous chemicals by volume for further investigation.

Responses to EPA's revised proposal, most of them from industry, reveal four main areas of contention.

*The "small business" exemption.* While all manufacturers must disclose basic information such as business addresses and chemicals produced, the request for site and quantity information is waived for firms with only one manufacturing site and either total sales of less than $100,000 in the most recent fiscal year or not more than 2,000 pounds annual production of each manufactured chemical. Critics claim the definition is so restrictive that few chemical manufacturers would be exempt and many small businesses would suffer undue hardships.

*Classification by site.* Many manufacturers agree that total production volume is a legitimate concern, but maintain that classification by site is unnecessary. Production by site can change frequently, making the data obsolete. Most important, the collection of such detailed information would greatly increase costs, while providing benefits only in cases of extreme emergency. A more realistic approach, it is argued, would be to require the total volume of each producer's chemicals and the location of each plant. If an emergency should occur, the manufacturer could then determine which site was producing the toxic chemical, thereby isolating the problem.

*Definition of "intermediate" chemicals.* The production of most chemicals involves a substantial number of chemical reactions. The byproducts created along the way, or the intermediate states of the chemical as it progresses towards final form, are usually referred to as "intermediates." Because EPA fears that an inadequate definition of these intermediate chemicals might exclude some substances from the notification requirement, it defines the term to mean any chemical that "could be isolated." The problem is that a large number of intermediates *could* be isolated in a chemical reaction, although only a few actually are. The critics say that this could lead to a flood of costly and useless information.

*Protection for confidential information.* Manufacturers are concerned about this because disclosure of information on intermediates and on production volume by site might reveal to competitors the raw materials and technology used. This act puts EPA squarely in the midst of a dilemma. For example, if the chemical name of a substance (which EPA, by law, must publish in its inventory list) is claimed as a trade secret and if EPA or the courts agree that this confidentiality should be protected, EPA could not divulge that information publicly. This could be a problem for the courts or perhaps Congress to resolve.

EPA tentatively decided that the proposal discussed here does not require an Economic Impact Statement since, in its judgment, the annual costs would not exceed $100 million. (For an assessment of President Carter's proposal to modify the Economic Impact Statement program, see page 12, this issue.) Even so, EPA might find it useful to prepare an appraisal of its overall approach in order to ensure that the goals of the toxic substances act are achieved at lowest cost.

## Laetrile: A "Forbidden Fruit"

It is reported that roughly 50,000 cancer patients take Laetrile in the hope that it will cure, arrest, or at least mitigate the symptoms of their disease. They persist in taking the drug, an extract of apricot pits, despite the Food and Drug Administration's ban on its manufacture and distribution and the medical profession's

repeated warnings that it has no therapeutic value. Such open defiance is causing political shockwaves that are undermining one of the pillars of current FDA regulation: the requirement that new drugs be proven effective as well as safe before they are marketed.

The effectiveness requirement was enacted in 1962. Many argue that, without it, unscrupulous pharmaceutical manufacturers would turn quick profits by producing and selling useless drugs to an unsuspecting public. Patients buying those drugs would not only be wasting their money but could also be harming themselves by foregoing effective (or partly effective) conventional treatment. Doctors could provide a measure of protection for their patients by not prescribing drugs they had found to be ineffective. But without systematically testing each drug they prescribed or keeping up to date on tests by others, they might not be able to screen out ineffective drugs. In other words, supporters of the effectiveness requirement believe that relying on individual doctor and patient decisions to weed out ineffective drugs is too risky.

But can all drugs be readily divided into those that are effective and those that are not? Critics of the requirement contend (1) that the concept of effectiveness is better represented by a continuum on which the FDA draws an arbitrary line and (2) that the reasons given for deciding where the line should be drawn are often not sufficient to justify a legally binding distinction between effective and ineffective drugs.

There is little disagreement in the scientific community about Laetrile's lack of effectiveness. To most researchers, Laetrile is a "cruel hoax" for which there is "not a shred of evidence" of therapeutic value. The case histories of patients allegedly helped by the drug are dismissed as anecdotal evidence at best and frauds at worst. Indeed, Laetrile has never been subjected to a well-controlled clinical test in humans because scientists have found animal studies too unpromising to warrant such efforts.

Even in the face of such evidence, some maintain that patients should be permitted to use Laetrile, or any other drug of questionable therapeutic value, so long as it is safe. The proposed Medical Freedom of Choice Act (H.R. 54), introduced by Congressman Steven D. Symms (Republican, Idaho), would eliminate the effectiveness criterion from FDA drug regulation. Congressman Symms contends that laws prohibiting fraud provide adequate protection against unethical manufacturers. Although Symms's bill has 100 cosponsors, there is little chance that it will be voted on by the full House of Representatives since the committee to which it has been assigned is overwhelmingly opposed.

Seven states (Arizona, Delaware, Indiana, Louisiana, Nevada, Oregon, and Texas) have legalized the manufacture and distribution of Laetrile within their borders. Because the FDA's jurisdiction is limited to drugs "introduced into interstate commerce," the agency has no authority to interfere with purely intrastate activity. The agency has warned, however, that it will attempt to prevent producers operating under permissive state laws from importing any of Laetrile's ingredients across state lines. The scope of the FDA's authority to prevent interstate commerce in goods other than drugs in marketable form will probably have to be settled by the courts. The rulings on the FDA's power to restrict imports of apricots, apricot pits, and extracts of apricot pits will be particularly important; at least some of the states that have legalized the production of Laetrile do not have adequate supplies of the drug's active ingredients to support substantial Laetrile production.

Other legal challenges to the FDA's ban on Laetrile are also pending. Three theories are currently being advanced: (1) that Laetrile is not a drug, but a vitamin ($B_{17}$), and therefore is not subject to the effectiveness requirement; (2) that Laetrile is exempt from the FDA's effectiveness requirement under a "grandfather" clause exempting drugs "generally recognized" by experts as safe and in use prior to 1962; and (3) that a law denying cancer patients the freedom to choose nontoxic treatments not sanctioned by the government intrudes on the constitutionally protected right to privacy. Relying on the second and third arguments, a federal district court judge in Oklahoma recently enjoined the FDA from interfering with the distribution of Laetrile in interstate commerce, with the use of Laetrile by a cancer patient, and with the administration of Laetrile by a licensed doctor. The FDA will almost certainly appeal the decision.

Meanwhile, the agency will probably try to establish that the premise of the judge's decision—that uncontaminated Laetrile is at least safe—is incorrect. The Department of Health, Education, and Welfare has already cautioned the public that the Laetrile now in distribution may not be as harmless as earlier supposed. Dr. Julius Richmond, assistant secretary for health at HEW, reported on August 10, 1977, that various types of impurities, including bacterial contamination and potentially harmful solvents, had been found in test samples. According to Richmond, at least thirty-seven cases of poisoning and seventeen deaths have been linked to the use of the drug, and two medical schools believe Laetrile is responsible for a wide variety of conditions ranging from skin rashes to muscle weakness. Ironically, Richmond asserted that at least part of the danger comes about because Laetrile is available only on a black market not subject to the FDA's quality standards.

Whatever the ultimate resolution of the Laetrile controversy, one cannot deny the truth of an observation by Dr. Franz Ingelfinger, former editor of the *New England Journal of Medicine:* "Forbidden fruits are mighty tasty, and especially to those who hope that a bite will be lifegiving."

## EFT, the Fed, and Your Right to Privacy

Ever since its creation in 1913, the Federal Reserve System has provided a mechanism for clearing checks for member and nonmember banks. Last year the Supreme Court ruled in *U.S.* v. *Miller* that individuals have no legal right to confidentiality in the information carried on their checks (addresses, telephone numbers, amounts paid, drivers license numbers, and so on). About the same time the Federal Reserve System (Fed) began linking together various regions of the country for the *electronic* interchange of debits and credits. Indeed, according to many experts, within a few years most check-clearing will be done through the aid of electronic funds transfer (EFT) mechanisms. These two developments have raised serious concerns about the Fed's role in EFT.

The issue was recently given national prominence by the Privacy Protection Study Commission. In its final report, *Personal Privacy in an Information Society* (June 1977), the commission stated that the provision of EFT services by the federal government would constitute "an unparalleled threat to privacy" because of the potential it offered for the surveillance of individuals engaged in financial transactions. Accordingly, the privacy commission recommended that the Fed and other government agencies be barred from managing, operating, or otherwise directly controlling EFT systems.

The technology making EFT possible is part of the problem. It sharply reduces the cost of recording and "accessing" the relevant information. Moreover, it may provide greater economies of centralization than does the existing system (the physical clearing of the checks). The latter consideration might suggest the desirability of having a single provider of EFT services, whether public or private. (This arrangement would not appear to be inevitable, however, as banks in New York and Chicago have already begun to develop electronic payments mechanisms in competition with those of the Fed.)

Whether EFT services are eventually provided publicly, privately, or both, the privacy problem will remain. Conceiving of a set of safeguards to impose on the system(s) is difficult enough, but, according to the privacy commission, the problems associated with government access to sensitive information would be compounded if the agency charged with supervision of the EFT system (say, the Fed) were allowed to participate in it. In this event the agency expected to be a watchman of other providers and users of EFT services would in essence be assigned to watch itself.

The commission also noted that the Fed is politically autonomous. Though this autonomy is arguably justified for reasons of insulating monetary policy from short-term political interests, the commission concluded that insulation from oversight by the President and Congress would be unwise for "activities which may impinge on personal privacy." (On the other hand, some observers have suggested that, even in this context, political autonomy for the Fed is an asset rather than a liability; a politically autonomous institution like the Fed

might have fewer reasons of its own for using EFT data for political purposes than an agency subject to direct presidential or congressional control.)

Throughout the debate, there is one question that transcends the issue at hand: How does one join regulatory and operational responsibilities within any single agency and ensure adequate safeguards? It was partly this problem that caused the Atomic Energy Commission to be split, part of it becoming the Nuclear Regulatory Commission and part going to the Energy Research and Development Administration. Until the problem is solved we are confronted with the perplexing question: Who will watch the watchers?

## After Economic Impact Statements—What?

The "problem of regulation" has many facets and it would seem logical to use a "mix" of approaches. One technique has been the Economic Impact Statement (EIS) Program initiated by former President Ford. (See article by James Miller in *Regulation*, July/August.) This program requires that before promulgating a major regulation, an executive-branch agency must prepare an *economic impact statement* analyzing the costs and benefits of its proposal and of alternative ways for securing the same objectives. Costs and benefits must be quantified to the extent feasible.

In recent months, the Carter administration has closely scrutinized the EIS program as part of its overall effort to improve the performance of regulatory agencies. Two extremes were considered. The first was to require that before a truly major regulation was formally proposed, the draft regulation, plus an analysis of its economic impact, be submitted to a review committee reporting to the White House Economic Policy Group. If the analysis were found to be lacking (or the proposal's substance questionable), the matter then would be put before the Economic Policy Group and other officials for resolution. The other extreme was to end the program or at least make it voluntary. Especially, critics urged, the requirement for quantifying benefits wherever feasible should be removed as unworkable.

President Carter appears to be coming down between the two extremes, though his program has aspects of both. In early October 1977, a task force headed by Stanley Morris of the Office of Management and Budget completed a draft executive order revising the EIS program. On November 18, President Carter published a proposal entitled "Improving Government Regulations" in the *Federal Register* and solicited public comment. (This is the first time a draft executive order has been released for public comment.)

Briefly summarized, the major features of the administration's proposal are:

- There is a general policy admonition that regulations should be set forth clearly and simply, should be effective and efficient, and should not impose unnecessary burdens.
- The order applies to all "significant" regulations issued by executive-branch *and independent agencies* (subjective criteria are provided for determining which regulations are significant).
- The existing process by which regulations are developed within agencies is modified to require that each agency publish a semi-annual agenda of the regulations it is considering, that its staff provide agency heads with a clear and detailed work plan for each proposed regulation, that agencies solicit more effective public participation in the regulation development process, and that agency heads or other statutory officials approve all significant regulatory proposals.
- Agencies must prepare a *regulatory analysis* of regulations that might have "major consequences" for the general economy (subjective criteria are provided for determining which regulations have major consequences). This analysis must contain a succinct statement of the problem requiring action and of the major alternatives for dealing with it, must analyze the economic consequences of the proposal and the alternatives, and must explain why one approach was chosen over the others.
- Agencies must review important regulations already on the books to see that they are clear, effective, and not unnecessarily burdensome.
- All regulatory proposals underway on the date the executive order becomes effective are exempt from the new standards. Failure to comply with the requirements of the order does

not constitute grounds for judicial review of agency action. The order expires on June 15, 1980 (unless extended).

According to reports, the program outlined in the executive order is to be supplemented by a Regulatory Analysis Review Group (chaired by the Council of Economic Advisers and including representatives from the major economic and regulatory agencies). If significant questions are raised about the quality of the analysis, the review group may ask the Council on Wage and Price Stability to prepare an in-depth evaluation. Then, if the views cannot be reconciled, the CEA chairman can recommend that economic questions on the proposal's consequences be discussed by more senior officials.

The proposal differs from the present EIS program in four principal ways. The first is the emphasis it puts on forcing agencies to use economic analysis in the development of their regulations. A major criticism of the present program is that many agencies view the required economic impact statement as merely a necessary hurdle to be cleared and use it mostly to justify the particular approach they have chosen. Whether the new procedures will succeed in getting agencies to incorporate economic analysis into their decision-making process at an early stage remains to be seen. It would appear that an agency bent on proposing an inefficient or burdensome regulation—to please a constituent, for example—could still do so without much trouble. Perhaps a strong policing mechanism—backed by veto power—will be necessary.

The second difference is that the proposed program applies to both *old* regulations and new. Granted, the agencies would have discretion in deciding which regulations should come up for periodic review. But forcing reassessment of existing regulations by means of executive order (supplemented by the Regulatory Analysis Review Group) is likely to have better results than relying solely on in-house evaluation by the agencies.

The third difference is that the proposal applies to independent agencies (the Interstate Commerce Commission, the Consumer Product Safety Commission, and so on) as well as to executive-branch regulatory agencies (such as the Environmental Protection Agency and the Food and Drug Administration). This feature may well be tested in the courts inasmuch as lawyers involved in putting together the old EIS program were convinced the President did not have the authority to extend it to independent agencies.

The final difference is that the existing requirement for a quantitative assessment of benefits and costs is deleted. Instead, agencies would be required only to analyze the "economic consequences" of their proposals and alternatives. Without question, it is sometimes difficult to put numbers on costs and—especially—on benefits. But the old requirement has imposed greater discipline on the proposal development process. Also, even if we accept the argument that it is impossible to put a dollar value on certain benefits (for example, lives saved or illnesses prevented), this does not mean that estimating the *number* of lives saved, illnesses prevented, et cetera, is not useful. Such information can often indicate ways for altering a regulation so that it yields greater benefits for the same expenditure of resources (public or private).

## Steel Imports—"Reference Prices" and a Precedent

Responding to pressure from Congress, the Carter administration is taking action to protect the U.S. steel industry from foreign competition.

Steel imports are blamed for massive layoffs of steelworkers and for contributing to the nation's rising trade deficit. Spokesmen for industry and labor have charged that foreign producers engage in unfair pricing practices and that foreign governments subsidize their steel exports, in effect "dumping" steel on U.S. markets. They have urged restrictions on steel imports, either as a long-term measure to protect American firms and workers against foreign beggar-thy-neighbor policies or as a short-term expedient to give American industry time to modernize and improve its competitive position.

But others have maintained that the rising tide of steel imports is a reflection of lethargic U.S. management and exorbitant U.S. wage settlements. Thus import restrictions would merely reward inefficiency and lead to higher prices for consumers.

Whatever the merits of the argument, it has been obvious for several months that some form of protection would be given the U.S. steel industry. Basically, there are two, interrelated approaches to protecting a domestic industry from foreign competition. The first, on which we have relied principally in the past, is to limit imports directly. For example, during the period 1969 to 1974 the federal government negotiated and maintained "voluntary restraint agreements" with the Japanese and European steel exporters. More recently, at the urging of the International Trade Commission, the government imposed a specific quota on imports of specialty steel.

The less direct approach is to put foreign producers at a price disadvantage, either by imposing tariffs or by establishing minimum prices below which foreign producers may not sell. The approach announced by President Carter on December 6 is of this type and uses the discretion afforded the Treasury Department under our "anti-dumping" statutes, in effect, to set a price floor under foreign sales. This initiative has significance far beyond the steel industry since it establishes a precedent for aiding other industries that may experience strong foreign competition.

Several months ago the steel industry gave halfhearted support to the idea of new voluntary restraint agreements, and major foreign producers seemed to favor such a measure as the least onerous approach to the problem. But the Carter administration, fearing this might lead to a gradual dismantling of the established trade order, declined to take this path. Instead, it first suggested that U.S. firms file anti-dumping petitions with the U.S. Treasury under the new and largely untested provisions of the 1974 Trade Act. But this suggestion did not satisfy critics on either side. Free traders argued it would disturb relations with our major trade partners, and some in the industry said it would not afford sufficient protection. Thus, the administration found itself on the horns of a dilemma: strong decisions in favor of U.S. producers would be likely to provoke retaliation against U.S. exporters, but denial of the petitions or weak decisions would likely lead to congressional action on behalf of the industry, with equally disturbing consequences.

So the administration turned to a somewhat different approach, one produced by a task force headed by Treasury Under Secretary Anthony M. Solomon. Under it, a system of "reference prices" is being established for major categories of steel products. These will reflect the "landed value" (production and transport costs plus a provision for profits) of the most efficient foreign exporters (at this time, the Japanese). In order to provide a margin for error, the reference prices will be set some 5 percent below the computed landed value. Proof that imported steel was being sold below the reference price would trigger a Treasury Department investigation, leading to fines or other penalties against the foreign producer if dumping were found to have occurred.

From the viewpoint of U.S. producers of steel, the new system has the advantage of speed and comprehensiveness. (The alternative route of filing anti-dumping petitions—and waiting for Treasury to decide if an investigation was warranted—would have yielded results only after more than a year's investigation, would have to have been repeated against a large number of foreign companies from many countries, and would have been ineffective against sporadic—hit-and-run—dumping.) However, from the viewpoint of U.S. consumers of steel, the large discounts that many foreign steel sellers have customarily conceded will no longer be available. Thus complaints and perhaps antitrust actions to test the new approach in the courts might occur.

Under the new program, decisions on *adjusting* the reference prices to allow for cost increases are likely to be just as important and as controversial as the decisions establishing their initial levels. This will become a particularly sensitive issue because U.S. steel firms realize that their pricing freedom will be intimately linked with the reference prices set. Unless the industry is given a voice in the process, it may find itself the subject of government price controls through the back door. Foreign exporters, who also have a great stake in the matter, have urged that they be consulted before reference prices are set or changed.

Many difficulties will have to be resolved if the new system is to work smoothly. Not only will prices have to be established for many kinds of steel, but provision will have to be made for extras (special sizes, treatments, or services), seconds (substandard grades),

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and fabricated products. Also, one might expect foreign competition to intensify in markets for "indirect steel exports," including ships and automobiles. But the greatest problem will probably be disagreements among domestic steel producers, foreign exporters, and U.S. government officials on the overall level and structure of the reference prices. ■