Briefly Noted

What's Wrong with Europe?

BY PIERRE LEMIEUX

By American political standards, the new president of France elected last May 6 is a far-left politician. The Greek parliamentary election, held that same weekend, raised a challenge for the Greek bailout and budget austerity previously agreed on. These political convulsions are symptoms, but only symptoms, that something is deeply wrong in Europe. What is it?

The welfare state | The first factor, and usual suspect, is the size and cost of the European welfare state, but it must not be exaggerated. As I have argued previously ("A Welfare State by Any Other Name," Spring 2012), both the United States and Europe are blessed with, or cursed by, a large welfare state, and it is only a bit worse and more ingrained on the eastern side of the Atlantic.

Yet, care must be taken not to fall into the opposite error of negating any difference in the relative weight of the welfare state in Europe and America. We must take with a grain of salt the argument, defended by economist Bruce Bartlett in his recent book *The Benefit and the Burden*, that a correct measure of the American welfare state should equate tax preferences (the Earned Income Tax Credit, the income tax deduction of mortgage interest, health insurance, etc.) with the direct transfers or central management preferred by European welfare states.

We can distinguish three ways to run a welfare state (or any interventionist state for that matter):

- The use of taxation to fund command-and-control social programs, as we see, for example, in the national education systems of some countries.
- The use of taxation to fund subsidies for beneficiaries, as we see, for example, in central-government grants to local schools, or school vouchers to parents.
- The use of "tax preferences" to encourage certain types of private spending, such as the American tax break given to employer-provided, or self-employed, health insurance.

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Certainly the second and third alternatives are more efficient than the first because they give more choice to individuals and don't require the central state to act on information that it cannot marshal (i.e., what do individual Americans need to improve their welfare?). Consequently, an American-style welfare state based on tax incentives is more efficient than a centralized welfare state, and the two should not be considered equivalent.

I would further argue—although this may be more controversial and require more discussion—that a tax-preferences system is often better than a taxes-and-subsidies system. Consider first an ethical, or distributive, argument: only if one agrees with Bartlett's suggestion that taxes redistribute "the nation's resources," as opposed to the money of individuals, would one admit that tax preferences correspond to money that belongs to the state but that the latter graciously allows citizens to keep. There is a second, more economic Public Choice argument: if you admit that all "the nation's resources" are for the state to dispose of as it wants, you are in for a lot of redistributive exploitation. In this perspective, even assuming that the deadweight loss of taxes is higher under a tax preferences system than a subsidies system, the former may be preferable. Loopholes may be useful, as Geoffrey Brennan and James Buchanan argued in their 1980 book *The Power to Tax*. This Public Choice approach provides another reason why we cannot give tax preferences the same weight as direct government inter-

ILLUSTRATIONS BY KEVIN TUMA

vention in measuring the welfare state.

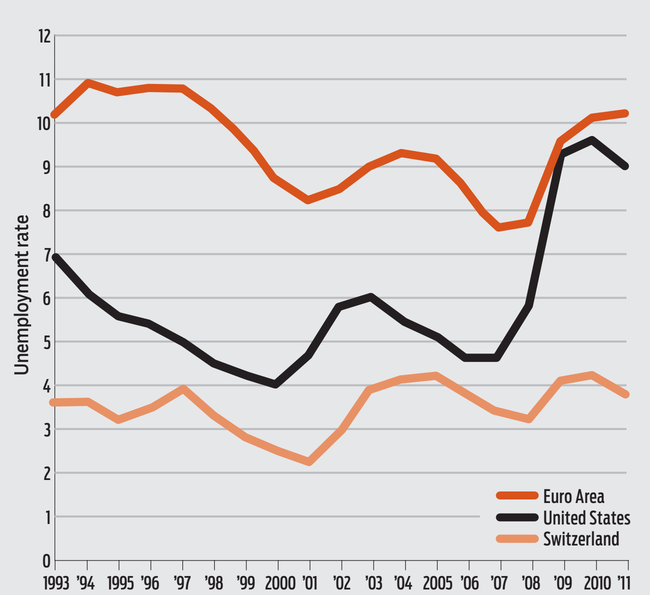
More convincingly, analysts have argued that, on sensible measures, taxes are more progressive in the United States than in many, if not most, European countries. Casey Mulligan, Véronique de Rugy, and (in a way) Bartlett himself are among the latest proponents of this idea, which Maurice Cranston already defended three decades ago. This line of thought further suggests that the welfare state and its redistributive drive do not constitute the main difference between Europe and America.

Regulation | A second, more important factor is regulation. Although regulation and the welfare state naturally come together, the former is arguably more detrimental to liberty and prosperity than the latter. And Europe is very much under the yoke of regulation. Indexes of regulation by the Organization for Economic Cooperation and Development give the European Union a 50 percent higher score than the United States in its measure of economy-wide regulation, a 100 percent higher score in its measure of regulation of professional services, and a 400 percent higher score in the complexity of administrative procedures. The regulatory burden has not improved a great deal since the creation of the EU. National regulations of the labor market still hamper the free movement of labor. Moreover, national regulations have often been replaced by transnational regulation, making regulatory arbitrage more difficult.

Regulations hit labor markets especially hard. The OECD calculates an index of "employment protection" to measure restrictions on freedom of labor contracts and on the capacity to dismiss workers. All EU15 countries (the original members of the European Union) are more restrictive than the United States, and

FIGURE 1

Unemployment Rates: Euro Area, United States, and Switzerland, 1993-2011



Source: Organization for Economic Cooperation and Development.

(with the exception of Ireland and the United Kingdom) more restrictive than Switzerland. Similarly, the most recent *Economic Freedom of the World Index*, produced by the Fraser Institute and the Cato Institute, shows economic freedom in the field of labor to be slightly higher in the United States than in Switzerland, while both countries leave the EU15 far behind.

Switzerland is an interesting case in many respects. It is a European country formally outside the EU, it has a welfare state, and yet its labor market is less regulated than Europe's (it doesn't have an official, centrally determined minimum wage, for example) and, in some ways, America's.

Labor market regulation is widely seen by economists as a major cause of labor market inflexibility and unemployment. The more difficult it is to dismiss employees, the more hesitant employers will be to hire a prospective worker in the first place. Indeed, when we compare unemployment rates with measures of "employment protection" or negative economic freedom in the labor market, the correlation is as expected: the more extensive the labor regulations, the higher the unemployment rate.

Figure 1 lends further support to this conclusion by comparing the evolution of unemployment in Euro-area countries, the United States, and Switzerland. Until the recent recession, the rate of unemployment fluctuated between 8 and 10 percent in the Euro area, which was twice the U.S. rate, while Swiss unemployment was 1 or 2 percentage points below America's. The recession muddled the cards, as the U.S. rate has jumped close to European levels. However, the American economy is recuperating faster than the Euro area, and Switzerland has been barely affected by the surge in unemployment. Not shown on the figure is youth unemployment, now close to 50 percent in Spain and over 20–25 percent in several European countries.

The unemployment picture is not as neat since the recession. Until 2007, the prevalence of long-term unemployment (defined as the proportion of the unemployed without a job for one year or more) was at least four times higher in the EU15 than in the United States, but the gap had dropped to 45 percent by 2010 (the last year of comparative data). It is only in 2010 that the proportion of discouraged unemployed (those who are not seeking employment anymore) in the United States rose a bit over that in the EU15. The recession has been devastating for America, but the devastation had been in preparation for some time as the American economy became much more regulated. Especially notable are the cases of credit markets and general business regulation, where regulation is now often more restrictive in America than in Europe. The Europeanization of America has been advancing.

Bureaucracy | The third factor is the power of Europe's government bureaucracy. European bureaucrats have highly protected jobs, even if that protection has weakened somewhat with the sovereign debt crises. They also form a large part of the population, including the voting population. In the typical core EU country, government employees (all levels, but excluding public corporations) make up 17 percent of the workforce, compared to 15 percent in the United States and 10 percent in

Switzerland. Note again that America is close to, and merely not as bad as, Europe.

Perhaps more important is the day-to-day power of European bureaucrats, called "Eurocrats." Through the non-elected European Commission, they exert much more power on the political structure of the EU than do their counterparts in the United States and Switzerland. The European Commission is the civil service of the EU, but it is also a regulator and it has the exclusive right to propose laws to the European Parliament. Eurocrats form a real aristocracy, insulated from their political masters and from the voters. As *The Economist* writes, "voters cannot throw out the bums in Brussels."

Statism | The fourth factor is the fugacious phenomenon of ideology. Political traditions, the content of public debates, and the composition of political assemblies are less libertarian, more statist, in Europe than in the United States. So when Europeans want to express discontent with the traditional left and right—and they have ample reasons to do so—they have no alternative but voting for more of the same.

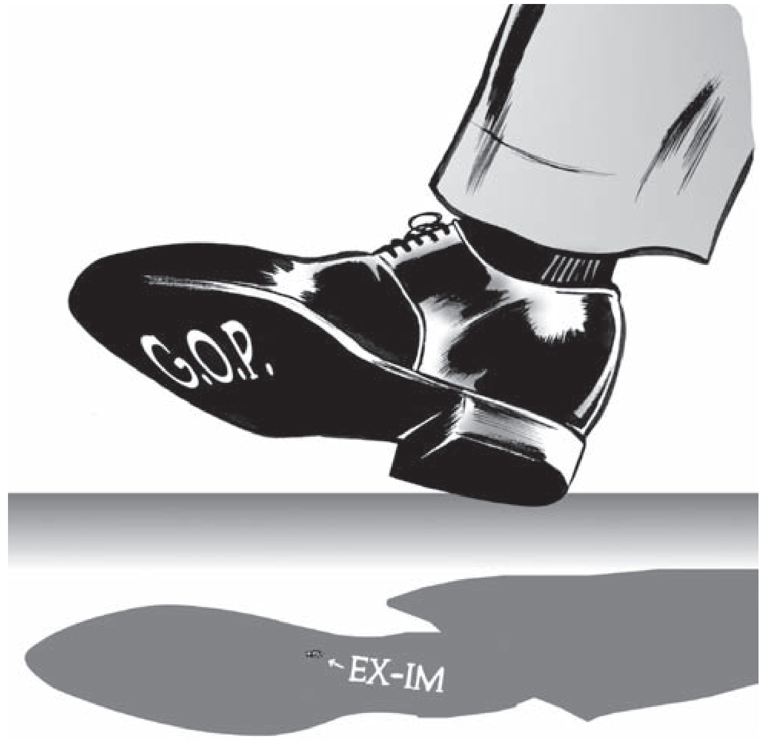
Not everything is wrong in Europe. Mores are more relaxed. The good life is good, if you don't love individual liberty in areas where your government happens to hate it. The Surveillance State is now more constrained than in the United States—who would have imagined that two or three decades ago? Liberticidal laws are not always ferociously enforced. Low-level bureaucrats are less self-righteous and easier to challenge. Yet, by and large, and especially in the narrowly defined economic sphere, the answer to the question "What's wrong with Europe?" is, "Everything that's wrong in America, with a vengeance." R

Reforming the Export-Import Bank

BY IKE BRANNON AND ELIZABETH LOWELL

One easy applause line for a politician working a conservative crowd is to bash the Export-Import Bank of the United States. The entity has always been discomfiting for Republicans, many of whom like to paint it as a manifestation of corporate favoritism, wasteful government spending, or managed trade. As Congress lurched toward reauthorizing Ex-Im this spring, criticism of this once-obscure agency intensified as some of the Tea Party members put the agency in their sights.

However, what the Ex-Im Bank actually does is much more complex—and necessary—than what its critics generally assume. As much as conservatives hate to acknowledge it, an entity that helps to finance the purchases of U.S. exports abroad is a necessary



evil in the current environment, where Europe and China's export credit agencies are much more aggressive in the use of export financing than the Ex-Im Bank would ever dare. Eliminating or even scaling back the bank would have been a serious blow to the U.S. manufacturing sector at an extremely unpropitious time and would have saved virtually no taxpayer money.

Tit for tat | It is important to emphasize that what the Ex-Im Bank does is actually a pittance compared to what its counterparts do for their exporters. For example, China's Export-Import Bank provided 17 times more financing as a share of GDP to its exporters than did the U.S. Export-Import Bank in 2008, and all indications are that this figure will only increase. The foreign financing entities of the European Union and Brazil also do more for their exporters than what the Ex-Im Bank does for U.S. companies as a proportion of GDP.

This puts U.S. exports in a bind. When a U.S. company angles for a big sale, the fact that its rivals are able to provide easy financing through their respective nations' export banks is an attractive perk that can (and often does) make closing the deal all the more difficult to accomplish—which is the very reason that our economic rivals are pouring so much into their export banks.

Escalating our own export financing in response to the increasing export financing done by other foreign entities may be far from efficient. But it is different from a tariff war in that it has little negative impact on U.S. consumers, as consumer prices are unaffected.

Reform | While the Ex-Im Bank is a necessity in today's environment, its mission needs to be focused solely on leveling the

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playing field for U.S. exporters. It should be enabled to operate efficiently without targeting specific industries and without suffering from a tangle of conflicting political mandates.

As we argued in our May 2011 paper "Export-Import Bank: Obstacles and Options for Reform," the bank suffers from skewed financing, political interference, and a host of management issues. In 2010 air transportation accounted for almost half of its total exposure, and Boeing's customers received over 60 percent of the Ex-Im Bank's long-term loan guarantees, leading to its nickname of "Boeing's Bank" and a sense of resentment from other industries that have not been as successful at gaining its support.

While a natural response might be for Congress to mandate that it support a more diversified portfolio of loans, the Ex-Im Bank already faces a host of conflicting political directives that complicate its task. For instance, Congress has imposed mandates that it support renewable energy exports, small business exports, and the exports of minority and women-owned businesses—all of which make its task of supporting exports that support American jobs all the more difficult. In addition, Ex-Im must abide by antiquated domestic content requirements and cargo preference requirements when selecting export deals to support. All of these mandates make it difficult to meet other goals, such as the administration's target of doubling total exports in five years.

While the Ex-Im Bank has had more than its share of management issues in the past, such a hodgepodge of restrictions only complicates its task. The bank should be given more flexibility to support deals based on economic sense rather than any narrow political exigencies.

And for those who bemoan its expense as being unaffordable in the era of trillion-dollar deficits, the Ex-Im Bank is currently self-sustaining, covering its operations through fees and interest payments. Of course, it takes only one default to erase that talking point and the bank has taken losses in the past, but budgetary savings that conservatives attribute to the demise of Ex-Im range from the absurd to the ridiculous.

Reauthorization | Killing the Ex-Im Bank would have been a purely pyrrhic victory for conservatives, providing them a scalp while doing not a whit for the economy. Instead, Congress recognized the bank's necessity in the current economic climate. Future congressional action should lift restrictions on who gets loans, require greater transparency, and place a greater emphasis on leveling the field for U.S. exports.

What's being overlooked in the fight to end this entity is that a successful Ex-Im leads to the creation of precisely the sort of high-paying manufacturing jobs that the American economy has been hemorrhaging over the last few years. In a climate where states cough up billions of dollars to entice employers to locate (or merely remain) in their state, investing in an entity that can potentially increase U.S. manufacturing exports by hundreds of billions of dollars at virtually no cost to the taxpayer is not a bad investment. It beats any alternative proposals that would inevitably fill the political need that the Ex-Im Bank's absence would create. R

Ex-Im Is Beyond Reform

BY SALLIE JAMES

In the previous article, American Action Forum scholars Ike Brannon and Elizabeth Lowell argue that free-market advocates are much too critical of the Export-Import Bank of the United States. They claim that it fills an important role in counterbalancing the trade subsidies that many other nations give to their exporting industries. I disagree. Ex-Im exposes American taxpayers to billions of dollars of risk, introduces distortions to the economy, and inserts politics into what should be commercial decisions. The federal government should divest itself of this risky and distorting attempt at managed trade.

The fact that China and Europe extend subsidized credit to their exporters is irrelevant at best, and a counterexample at worst, for economic policy decisions in the United States. Reforming Ex-Im by changing some of its mandates or lending practices would not address the fundamental problem with the bank: that as a government entity it is inherently driven by political considerations. The best solution is to close it down altogether and leave export financing decisions to private actors putting their own money at risk.

Path to statism | Brannon and Lowell point to the relatively small share of Ex-Im financing as a proportion of U.S. GDP compared to other countries' efforts as a reason to ratchet up U.S. export finance. It should not be a surprise that China—which, despite great strides, remains to a large extent a state-controlled economy—provides 17 times more financing as a share of GDP to its exporters. But following China's lead by "escalating our own export financing in response" would indeed be very costly.

And how far should we go in response? What if China decides to finance every export? Does that mean the United States should do the same? Far from being a "necessary evil," it would be nonsense for the United States to respond to distorting and economy-weakening policies abroad by imposing the same policies on our own economy. Doing so may well be different from a tariff war, but it is still very damaging.

The 'costless' myth | Brannon and Lowell assert that closing the Ex-Im Bank would "save virtually no taxpayer money." The fact that the bank is "self-sustaining" and, since 2005, has returned $3.4 billion to the U.S. Treasury are common talking points of bank supporters such as the U.S. Chamber of Commerce.

Suggesting that the bank is costless ignores the very real distortions introduced into the economy whenever the government intervenes. In this way the bank is analogous to regulations,

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which impose costs on businesses and consumers even if they do not show up as a line item in the federal budget. So we should first acknowledge that a lack of fiscal outlay does not mean a policy decision or government action is "free." Official export credit and other subsidies promote exports only by removing resources from the productive, more efficient sectors of the economy, thereby distorting and weakening them. Efficient economic activities that have met market tests will contract so that resources can be moved to less efficient politically directed activities.

A recent analysis by Jason Delisle and Christopher Papagianis, researchers at the economic policy group e21, exposes claims about the bank's financial position as "almost surely an accounting illusion" based on official federal government accounting rules that discount or exclude altogether the cost of market risk. (See "Critics of the Export-Import Bank Have a New Weapon at Their Disposal: Fair-Value Accounting," *economics21.com*, March 29, 2012.) They estimate that if fair-value accounting rules are applied to Ex-Im Bank figures, then the bank's long-term loan guarantee program is operating at a loss, not a profit. The subsidy to borrowers, according to Delisle and Papagianis, amounts to about 1 percent of the amount borrowed, which translates to a loss for taxpayers of about $200 million in 2012. If you include the losses on smaller Ex-Im loan programs, which even government accounting rules show are subsidized, then the subsidies provided by the bank are even higher.

There are also the potential losses should Ex-Im loans fail. If we have learned one thing from the enormous losses and subsequent bailouts of Fannie Mae, Freddie Mac, and other government-backed entities, it is that claims to be "self-financing" or even "profit-making" are to be treated with a great deal of suspicion.

Misguided notions of trade | Brannon and Lowell acknowledge that the bank's activities are hindered by "skewed financing, political interference, and a host of management issues." As a government entity, all of those bugs should be expected and will not be fixed by tinkering with the bank's mandates as Brannon and Lowell propose.

Moreover, the authors display an apparent, unjustifiable bias by placing emphasis on the bank's ability to support manufacturing jobs. There is nothing special about a dollar earned in manufacturing compared to a dollar earned in, say, services. Even the Obama administration's former economic adviser, Christina Romer, says that politicians' manufacturing fetish is largely baseless. The first step in preventing the sorts of proposals to "fill the political need" to promote manufacturing exports that Brannon and Lowell suggest will inevitably arise is surely to refrain from perpetuating myths about manufacturing's supposed superiority.

The arguments advanced by Brannon and Lowell in support of their proposals for Ex-Im are unconvincing. Rhetorically opening the door to matching the Chinese (or any other) government policy-for-policy in a misguided attempt to level the trade playing field is a recipe for disaster. R

Driver Distractions and Regulatory Dystopia

BY THOMAS A. HEMPHILL

In December 2011 the National Transportation Safety Board (NTSB), the federal agency responsible for traffic safety and investigating traffic-related accidents, recommended that all states ban drivers from using portable electronic devices (PEDs) while operating a motor vehicle. The board's recommended prohibition would cover hands-free as well as handheld devices.

According to March 2012 data collected by the Insurance Institute for Highway Safety (IIHS), an Arlington, Va.–based nonprofit research group funded by the vehicle insurance industry, 35 states and the District of Columbia presently ban text messaging for all drivers; seven additional states ban novice drivers from texting; and three of those seven states also ban school bus drivers from texting while operating their vehicles. In addition, 10 states and the District of Columbia presently ban handheld cell phone use by drivers; 30 states and the District of Columbia ban all cell phone use for novice drivers; and 19 states and the District of Columbia prohibit cell phone use by drivers when operating a school bus. Also, many localities have enacted their own bans on cell phone usage or texting while driving. Interestingly, no state or the District of Columbia presently bans the use of hands-free telecommunication devices for the general populace.

Accident reduction? | Despite the NTSB's recommendation, recent research studies suggest that PED bans may have little effect on traffic safety. In a December 2009 study by the Highway Data Loss Institute, an organization affiliated with the IIHS, researchers concluded that, while handheld cell phone usage generally declined following implementation of a ban in the three states surveyed [California (inconclusive data), Connecticut (76 percent), and New York (47 percent)] and the District of Columbia (76 percent), insurance collision loss experience data analysis did not indicate a decrease in crash risk. Similarly, a September 2010 study released by the Highway Data Loss Institute found no reductions in motor vehicle crashes after text messaging bans went into effect in four states (California, Louisiana, Minnesota, and Washington). In fact, in this study, the enactment of such legislation was found to be associated with a slight, statistically significant increase (a range of 1–9 percent) in the frequency of insurance claims filed under collision coverage for damages after vehicular crashes in

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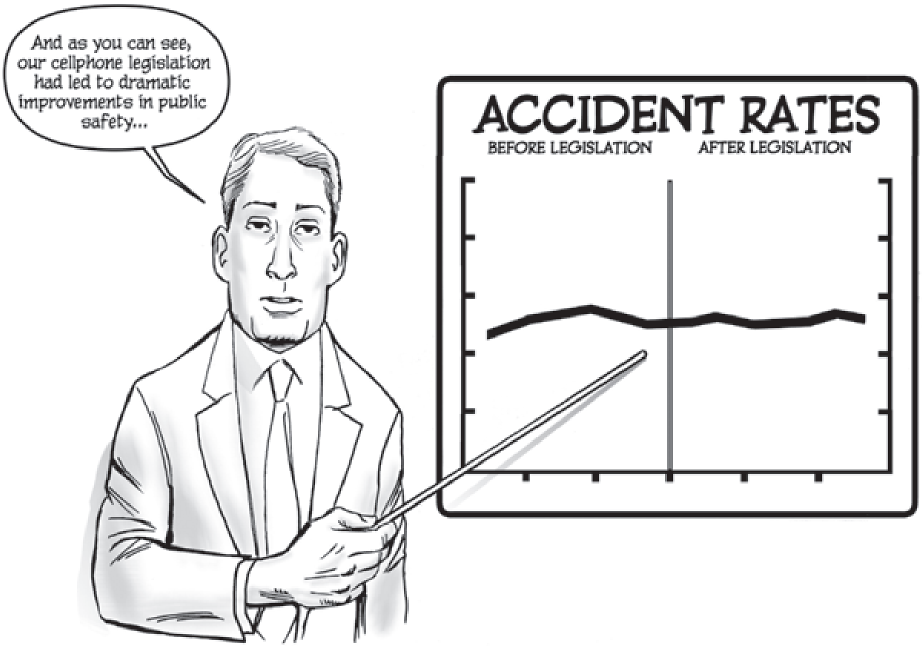
three (California, Louisiana, and Minnesota) of the four states studied (Washington having a statistically insignificant 1 percent increase).

Results of a July 2009 study by the Virginia Tech Transportation Institute (VTTI) found that texting drivers increased their probability of crashing 23.2 times, but dialing a cell phone only increased the risk of accident by 2.8 times, and talking or listening to a cell phone conversation increased the risk 1.3 times. In comparison, reaching for an object while driving an automobile increases the risk of an accident by 1.4 times. According to the VTTI, the major factor whether or not a traffic accident occurs is having the driver keep his eyes on the road, as the odds of a crash or near-crash more than doubled when a driver's eyes were off the road ahead for more than two seconds.



Recent data on nationwide automobile fatalities shed additional light on the driver distraction controversy. For 2010, the National Highway Traffic Safety Administration (NHTSA) reported that 32,788 people died as result of motor vehicle accidents on American roadways. That is the lowest level of fatalities since 1949, when there were 30,246 fatalities recorded. Also for 2010, the fatality rate per 100 million vehicle miles driven fell to an historic low of 1.09. According to NHTSA, the 3,092 distraction-related reported fatalities in 2010 (down 43.5 percent from 5,474 fatalities in 2009) are attributed to a variety of driver distractions, including cell phone use and texting, eating, drinking, conversing with passengers, interacting with in-vehicle technologies and PEDs, daydreaming, and dealing with intense emotions.

Voluntary guidelines | The NTSB's call for an all-out ban on PED usage by drivers resulted in strong criticism from the automobile industry and consumers alike, as such an outright prohibition would be virtually impossible to enforce actively. More significantly, the ban may be unnecessary because there may be a better way to improve traffic safety.

NHTSA and the Alliance of Automobile Manufacturers, a trade association of 12 car and light truck manufacturers, are now engaged in developing a set of "NHTSA Visual-Manual Driver Distraction Guidelines." For over a decade, Alliance members have been applying their own guidelines in vehicle integrated design connectivity technologies that strive to make those technologies no more distracting than common manual radio controls. Unlike PEDS, automobile-integrated technology features are designed in a way that helps drivers keep their eyes on the road and hands on the steering wheel by allowing a driver to operate the system through verbal commands. The Alliance guidelines, an industry self-regulatory approach, are in their third iteration, and NHTSA will use the Alliance guidelines as a point of departure for developing its draft guidelines.

The Alliance argues that implementation of NHTSA guidelines over direct command-and-control regulation is an appropriate approach (given the scope of the guidelines, i.e., light-duty vehicles) to addressing this driver distraction safety problem, given how rapidly technology is evolving, the evolving state of knowledge about drivers' behavior behind the wheel, and the agency's lack of regulatory authority over PEDs. Furthermore, the Alliance believes that it is appropriate to limit or prohibit certain automotive functions or features that are determined through testing pursuant to the performance-based metrics in the NHTSA guidelines to be incompatible with safe driving, including completely disabling such intense visual-manual activities as texting and entering phone numbers or addresses.

A recent study conducted by Bryan Reimer, Bruce Mehler, Ying Wang, and Joseph F. Coughlin of the Massachusetts Institute of Technology's Age Lab and the New England University Transportation Center may, however, limit the impact of the hands-free, voice-activated technology solution to addressing the driver-distraction issue. This study of 108 actual drivers, balanced by gender and across three age groups—20–29, 40–49, and 60–69—utilized a test car that was fitted with sophisticated sensor technology that made it possible for the researchers to analyze a test subject's cognitive load. The researchers found that an increase in the driver's "cognitive load"—that is, an increase in the complexity level of the conversation or voice commands—can lead to "tunnel vision," or gaze concentration distraction, that drivers may be unaware of when their hands are not holding a cell phone or turning a dial in the vehicle. Therefore drivers are not aware of their own cognitive limits, and those limits can rapidly change as the cognitive load increases and decreases while operating a vehicle. This research finding challenges the hands-free technology solution as a panacea to the driver distraction problem. More likely, it will help establish clear opportunities and limits on technology as a complement to other responsible driver practices and regulatory responses.

Conclusion | The existing state of knowledge regarding driver distraction and public policy intervention leads to some tentative conclusions.

First, while enacting a state law banning high-risk driver text messaging may be reasonable public policy, research results show that this blunt regulatory approach, along with bans on handheld cell phones, has no discernible impact on reducing automotive accidents. A caveat to this conclusion, however, is that recent NHTSA statistics for 2010 show a marked decline in distraction-related accidents over the previous year. It is too soon, however, to discern whether this decline is significantly related to whether American drivers are finally conforming to the proliferation (and active enforcement) of PED bans or other mitigating factors are responsible for this outcome.

Second, while automobile manufacturers are cooperatively engaging with the federal government to reduce vehicle functions and features that may increase visual distractions in a vehicle, this solution does not adequately address PED usage or a myriad of other potential distractions that take place in a moving vehicle. Further research into what levels of distraction are inappropriate while driving need to be investigated.

Third, with these new scientific insights into a driver's cognitive load limit, policymakers will be better equipped to decide on the appropriate (and effective) level of command-and-control regulation. This public policy will likely be complemented by industry self-regulation regimes, driver education and public relations campaigns to reinforce safe driving practices focused on in-vehicle driver distraction reduction, and manufacturers focusing their innovation efforts on technology solutions such as vehicle artificial intelligence sensors capable of recognizing driver signals indicating an unsafe cognitive load, thus disconnecting voice-activated features in the vehicle.

To effectively manage this complex safety problem will undoubtedly require an evolving strategy of complementary business, consumer, and public policies and approaches in an increasingly "distracting" American society. R

READINGS

- "A Field Study on the Impact of Variations in Short-Term Memory Demands on Drivers' Visual Attention and Driving Performance across Three Age Groups," by Bryan Reimer, Bruce Mehler, Ying Wang, and Joseph F. Coughlin. *Human Factors: The Journal of the Human Factors and Ergonomics Society*, forthcoming.
- "Hand Held Cellphone Laws and Collision Claim Frequencies," published by the Insurance Institute for Highway Safety, Arlington, Va. *Highway Loss Data Institute Bulletin*, Vol. 26, No. 17 (December 2009).
- "Texting Laws and Collision Claim Frequencies," published by the Insurance Institute for Highway Safety, Arlington, Va. *Highway Loss Data Institute Bulletin*, Vol. 27, No. 11 (September 2010).

Preventing the PBGC from Becoming the Next Government Bailout

BY THOMAS J. HEALEY

If there were ever any doubts about the need for a hard-nosed solution to the chronic financial woes of the Pension Benefit Guaranty Corporation (PBGC), American Airlines has put them decisively to rest. The beleaguered airline, following its bankruptcy filing last November, is looking to shift billions in unfunded pension benefits covering four retirement plans and 130,000 participants to the PBGC. Not only would this move trigger a $9 billion loss for the government-charted agency, it would also push it a giant step closer to a massive public bailout. The fact that American Airlines has subsequently pulled back does not diminish the precarious state of the PBGC.

The agency's latest annual report drives that point home. For fiscal year 2011, the agency saw its deficit soar to the highest level in its 37-year history, to $26 billion from $23 billion the prior year. That, however, could be just the tip of the iceberg. The PBGC reported that its potential exposure to future pension losses from financially weak companies increased by $57 billion from a year ago to a staggering $227 billion.

PBGC director Joshua Gotbaum has pushed back against any attempt by American Airlines to terminate its pension plans, claiming it would saddle his agency with $17 billion in benefit obligations. Before killing its pension program, Gotbaum has said the airline must prove "there is no better alternative."

This fierce argument underscores the vital role the PBGC plays for workers enrolled in more than 27,000 private-sector defined benefit pension programs. If an employer fails and is no longer able to meet its pension obligations, the agency steps in as trustee and assumes monthly payments to retirees. The agency is funded by investment returns as well as premiums.

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Battered by a weakened economy, the PBGC found itself responsible for 152 new private-sector pension plans for the fiscal year ended Sept. 30. In addition to the new obligations, the agency was financially weakened by record-low interest rates, which actuarially magnify the present value of future benefit obligations.

Roadblocks to reform | The plight of the PBGC has hardly gone unnoticed in Washington. There have been calls for meaningful changes in recent years, but they have all foundered on the shoals of politics, expediency, and self-interest. Companies have steadfastly resisted reforms, particularly increases in the premiums they pay, for obvious reasons; unions have resisted on grounds that any change will serve to accelerate the already rapid decline of defined benefit pension plans; and Congress has failed to act because of the pressure that's been applied by companies and unions—coupled with the fact that, like the federal budget deficit, it's much easier for lawmakers to kick the PBGC can down the road.

That dereliction of duty is only making a bad situation worse. To be sure, there is no shortage of intelligent and far-sighted ways to make the PBGC a self-sustaining and actuarially sound entity with the ability to weather economic storms as well as repeated business and industry failures.

One of the most obvious ways—as unpalatable as it may be to certain sectors—is to raise premiums. It's axiomatic that no insurance plan can hope to survive if it can't charge adequately for the coverage it provides. The PBGC needs to be given the authority—which it currently lacks—to increase premiums (around $35 per participant) to a level that will prevent the need for a government-financed rescue. President Obama has proposed the PBGC be granted such powers.

More than just a higher flat-rate premium spread across all participants, however, the PBGC should have the authority to weigh the risk of a pension plan in its premium calculations. This would be based on such factors as the performance of its investment portfolio, its pension funding percentage, and the overall health of its corporate sponsor. Another change that deserves strong consideration is capping the maximum PBGC benefit (currently $54,000 a year per participant), at least until the agency has regained its financial footing.

How to finesse the gridlock in Washington? One way is to replicate the successful model put in place by Congress in 1988 to deal with the highly sensitive issue of military base closings. Using that process, the president would appoint an independent panel to hold hearings, conduct research, and make concrete proposals to strengthen the PBGC. Those proposals would be submitted to the president who, if he approves, would send them to Congress. If legislators fail to act on them within 45 days, they would automatically become law.

In the end, the issue is this: Does the government have the foresight, courage, and good sense to address the metastasizing PBGC problem now, or will we continue to dither until the only option left is a taxpayer bailout rivaling that of AIG, Fannie Mae, Freddie Mac, and other institutions deemed "too big to fail"? R

What Does an Hour of Regulatory Compliance Cost?

BY SAM BATKINS

U.S. businesses spend billions of hours each year in an effort to comply with the reams of regulations issued by government. The "billions" figure is not guesswork: federal regulatory agencies are required to produce a good-faith estimate of the amount of time a newly issued regulation will require us to spend doing paperwork in order to comply with the law. The Office of Information and Regulatory Affairs (OIRA) calculates that the federal government currently imposes more than 10.3 billion hours of paperwork compliance annually. To put that number in perspective, New York could build more than 1,400 Empire State Buildings in the equivalent amount of time.

Calculating the monetized cost for those hours of paperwork is a bit dicey, however. OIRA estimates that the associated cost of compliance for those 10.3 billion hours comes to $77.2 billion, which means that the government believes an individual's time is worth $7.45 per hour. That is less than the minimum wage in Washington, D.C.

This raises the question of how exactly the federal government quantifies its paperwork burden on businesses. The answer usually depends on the particular agency involved and whether it wants to monetize paperwork costs or conveniently ignore them. Typically, agencies would rather skip the exercise altogether if possible or, failing that, find the lowest wage rate it can justify and use that to low-ball the true compliance cost.

One place an agency could find data on the cost of a compliance hour would be in the Bureau of Labor Statistics' (BLS) Occupational Employment Statistics. It specifies a wage rate for a general compliance officer (who can "examine, evaluate, and investigate eligibility for or conformity with laws and regulations") of $30.66 an hour. If this rate were applied to the nation's cumulative compliance burden, the associated costs of doing the required

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paperwork necessary to comply with federal regulations would tally $317.4 billion, more than four times the cost that OIRA lists. However, a cursory examination reveals few agencies bother to use this $30.66 figure.

Dodd-Frank burdens vary | The most egregious contributor to the unrelenting rise in the number of hours spent complying with federal paperwork has been the mountain of new regulations resulting from the 2010 Dodd-Frank legislation. While various financial regulatory agencies are far from done generating all the regulations that the law requires, the total time needed to comply with the regulations already issued eclipses 50 million hours, much of which the government has not bothered to monetize.

One of these agencies, the Consumer Financial Protection Bureau, is guilty of one of the more egregious failures to estimate a regulatory compliance cost: it omitted important data from its remittance transfer rule (Regulation E). This rule imposes a compliance burden that the agency estimates will take private businesses more than 7.6 million hours to satisfy. If we value each hour spent complying with paperwork at the hourly wage of a compliance officer, the total compliance cost for this one regulation alone is roughly $225 million. However, if we use the median hourly wage rate for Dodd-Frank compliance (roughly $100), compliance costs climb to $760 million.

Given the breadth of Dodd-Frank regulations and the plethora of regulated entities issuing them, it is no real surprise that there is no set hourly wage used for estimating the law's compliance costs. For instance, the Federal Reserve has listed an hourly rate as low as $42.95 for some of its regulations, while the Commodity Futures Trading Commission routinely uses $100 per hour. The Securities and Exchange Commission once estimated a compliance hour to be worth as much as $400, while acknowledging that regulating large financial institutions likely means that the employees in charge of ensuring compliance may be paid somewhat over the mean hourly wage rate. Most of the other agencies continue to low-ball hourly wages whenever possible.

ACA estimates | Just as with the implementation of the Dodd-Frank legislation, the cost estimates for the time spent complying with regulations issued under the Affordable Care Act (ACA) also vary, but agencies have been far more transparent at monetizing hourly rates for compliance personnel. For example, the Centers for Medicare and Medicaid Services (CMS) routinely cite BLS data to monetize paperwork impacts. In one rule implementing sections of the ACA, the CMS estimated hourly compliance would cost $59.27, "the mean hourly rate for computer and information systems managers based on the 2010 [BLS]."

However, in a recent rule designed to prevent Medicare and Medicaid fraud ("Changes in Provider and Supplier Enrollment"), the CMS demonstrated the arbitrary nature of some hourly estimates, projecting an hourly rate for compliance at just $14.51, two-thirds of the average U.S. hourly wage of $21.74. The CMS did note that a "medical technician" complying with the regulation receives a higher wage, which the agency estimated at $17.27 per hour. If the administration had used this hourly estimate, the rule's cost would have increased by $5.7 million over the $30.3 million CMS listed in paperwork costs.

An hourly wage? | Federal agencies either underreport or simply fail to monetize paperwork requirements on a regular basis. This is just one tactic agencies can use to tip the scales of benefit-cost analyses of proposed regulations. Most businesses would likely report that their time is worth more than the $7.45 hourly wage that OIRA lists, especially since many cannot legally pay an employee that little. The federal government certainly pays better than that.

In a May 1, 2012 *Wall Street Journal* op-ed, OIRA administrator Cass Sunstein wrote that the Obama administration's Executive Order 13609 on regulatory reform would be "a new model for eliminating red tape and promoting trade and job creation. Let's get to work." With 10.3 billion hours of compliance and countless agencies that omit relevant cost data, Administrator Sunstein has plenty of work on his plate.

TABLE 1

Examples of the Cost of Compliance

Information collection	Cumulative compliance hours	Government estimate of hourly compliance cost
IRS Form 1040	2.7 billion	$13
SEC Form 10-k	21.4 million	$133
IRS Form W-2	253 million	N/A
IRS Form 1099-MISC	24.6 million	N/A
SEC Form S-3	244,399	$1,200