June 11, 2012

Office of Information and Regulatory Affairs
Office of Management and Budget
Attn: Mabel Echols
NEOB, Room 10202
725 17th Street, NW
Washington, DC 20503

Re: Docket ID OMB-2010-0008, Comments of Paul R. Noe in Response to OMB Request for Comment on Whether and How Agencies Should Analyze Employment Impacts of Regulations

To Whom It May Concern:

I want to express my appreciation for the opportunity to provide comments to OMB on whether and how agencies should evaluate employment impacts when analyzing the costs and benefits of regulations, as requested in OMB's Draft 2012 Report to Congress on the Costs and Benefits of Federal Regulations, pp. 79-81. I am submitting these comments solely in my personal capacity as an alumnus of OIRA who is interested in sound and cost-effective regulatory policy and concerned, as we all are, about the state of our economy, the need for a robust U.S. manufacturing base, and the effects of the stubbornly high unemployment rate on our nation, its workers and their families. I would like to submit for OMB's consideration and for inclusion in its record an article on "Analyzing the Destruction of Human Capital by Regulations."[1]

Introduction

In recognition of the economic challenges our country faces, the President has directed agencies to carefully design their regulations with consideration of the effects on jobs. It should be noted that presidents have provided similar direction to agencies for decades. In 1981, when President Reagan formalized the current regulatory review process in Executive Order 12291, it included within the definition of a major rule subject to rigorous benefit-cost analysis "any regulation that is likely to result in . . . [s]ignificant adverse effects on employment." E.O. 12291, Sec. 1(b). It also directed agencies to take into account "the condition of the particular industries affected by regulations, the condition of the national economy, and other regulatory actions contemplated in the future." E.O. 12291, Sec. 2. In 1993, President Clinton reaffirmed this direction in Executive Order 12866, which of course still governs regulatory planning and review today. Like the Reagan Order, E.O. 12866 includes within the definition of an "economically significant rule" subject to benefit-cost analysis a "rule that may . . . adversely affect, in a material way . . . jobs." E.O. 12866, Sec. 3(f)(1). Recently, President Obama has underscored the directive in E.O. 12866 by adding:

[1] Paul Noe, "Analyzing the Destruction of Human Capital By Regulations," 63 Admin. L. Rev. 203 (2011).

> "Our regulatory system must protect public health, welfare, safety, and our environment while promoting economic growth, innovation, competitiveness and job creation. . . . As stated in [Executive Order 12866] and to the extent permitted by law, each agency must . . . tailor its regulations to impose the least burden on society, consistent with obtaining regulatory objectives, taking into account . . . the costs of cumulative regulations.

Executive Order 13563, Sec. 1 (Jan. 18, 2011).

On one hand, the state of the literature and analytic techniques have made analyzing the destruction of human capital and other employment effects of regulation a difficult challenge. On the other hand, the literature has advanced significantly in the last decade, agencies arguably have been out of compliance with longstanding presidential directives to analyze and reduce the costs of job displacement by regulations, the President has been clear, and we must address the worst job market since the Great Depression. Moreover, it bears emphasis that unwarranted job displacement and destruction of human capital by regulation can be reduced through the rigorous and objective application of the efficiency criteria that have been in every Executive order on regulatory analysis and review since OIRA was created. More effort could be focused there. Finally, one response to the need for jobs and economic growth is that "government should regulate less during periods of high unemployment than during periods of low unemployment."[2]

There are several options OMB could pursue in response to the current presidential directives to minimize the job displacement costs of regulation. First, OMB could, with the help of the agencies, quantify and monetize the costs of job displacement (including lost productivity during the period of unemployment and adverse health impacts) and incorporate them into benefit-cost analyses, as well as analyze and describe the distributional effects in the regulatory impact analysis, and all of this information could be considered by the ultimate decision makers. Second, the President or OMB could issue a directive to the agencies to minimize the adverse impacts of regulations on disproportionately affected industries and their workers. Just as regulatory agencies often protect consumers who are highly sensitive or highly exposed, agencies could identify workers whose skills are industry-specific or are in areas where regulation could cause the supply of workers to exceed the near-term demand. Third, OMB could more rigorously apply the efficiency criteria of E.O. 12866 and E.O. 13563. Fourth, OMB could, more or less, continue the status quo in which agencies sometimes create questionable employment impact statements and apply them in an ad hoc and non-transparent manner.

I submit that, in light of the President's direction and the state of our economy, the fourth option is unacceptable, the third option is imperative, and careful consideration should be given to the first and second options. Because the President has been abundantly clear on the third option, and there also is broad consensus among economists and regulatory policy experts on how the rigorous and objective application of efficiency criteria would

[2] Jonathan S. Masur and Eric A. Posner, "Regulation, Unemployment, and Cost-Benefit Analysis," 98 U.Va. L. Rev. 579, 625 (2012).

help promote economic growth, I will focus in these comments on the first and second options to respond to OMB's request.

Background

The Status Quo: Current Agency Practices

Current practices analyzing and actually considering the employment impacts of regulation need significant improvement if they are to be seriously considered. As Masur and Posner have observed, "agencies' existing approaches for addressing the unemployment effects of proposed regulations are ad hoc and incoherent."[3]

Some of the key problems with current agency approaches include:

- The agency typically does not incorporate the costs of job displacement into the benefit-cost analysis (BCA) where they might make a difference in the outcome of the BCA. Instead, typically agencies only include direct compliance costs in the BCA, and they assume the economy is at full employment, and any employment effect is a rounding error. Any worker displaced from his or her job today is assumed to find a replacement job tomorrow. Of course, such an assumption is particularly dubious in today's economy.

- Agencies often do not include a robust distributional analysis in the regulatory impact analysis that describes the workers who likely will be displaced from their jobs and the effects.

- If employment effects are assessed, the agency may include the assessment in its feasibility analysis or do a job-loss analysis, and in neither case are the results incorporated into the BCA.[4] The agency may perform the analysis with little clarity or rigor to how it is applied. For example, typically there is no uniform definition of what is "feasible," so there may be a lack of consistency in a given analysis and certainly across feasibility analyses within a given agency and across multiple agencies.[5]

- Agencies often fail to consider data specific to a given industry, and they often lump disparate industries together, which can produce estimates with little or no relevance for a given industry. Instead, "when agencies estimate the effects of regulations on employment, they should take into account the *actual industry affected by the regulations*" and not rely on studies that do not apply to the industry at issue.[6]

[3] Id. at 633; see also, id. at 585-603.

[4] Id. at 585.

[5] Id. at 585-603.

[6] Id. at 633 (Emphasis added).

- Agencies also often use outdated data, and even if the data related directly or indirectly to the industry at issue, it may not longer be applicable. For example, the elasticity of demand curves may have changed significantly due to foreign competition, technological changes, structural changes in the economy, etc.

- Agencies may rely on models that are not transparent, use data not accessible to the public, and that may be outdated because they use old data sources and make no adjustment for the depressed condition of the U.S. economy.

- Agencies may only focus on net job effects, not gross job effects, under the assumption that "a job is a job." This assumption is questionable, and in the process of making it, agencies may neglect search costs and displacement costs to workers, their families and their communities.

- Job displacement costs to workers that agencies could monetize and incorporate into BCAs, but do not, include lost earnings potential from the destruction of human capital, relocation costs, the cost of new job training, etc. Agencies also do not, but could, include the health effects of job displacement, including illness, mental suffering, and longevity impacts.[7]

The Impacts of Job Displacement

Over 12 millions Americans currently are unemployed, and the U.S. unemployment rate has been over 8% for an extended time period. Other estimates that include discouraged workers are far higher. In either case, Americans are facing the worst job market since the Great Depression.

Job losses result in a host of costs to workers, their families, their communities, and society. For individual workers and their families, these costs include lost earnings potential from the destruction of human capital, the deterioration of jobs skills, relocation expenses, the costs of job retraining, etc., as well as the adverse impacts of job displacement on health and well-being.

Recent research indicates that the economic impacts of job losses are much larger than previously thought. For example, Davis and von Wachter found that the present value of future earnings is reduced by an average of 11% for men with three or more years on the job who are terminated as part of a mass layoff.[8] If the layoff occurs during a recession,

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[7] Noe, supra note 1, at 206 & n.4; Masur and Posner, supra note 2, at 605-606 & n.111; 615-618 & nn.132-146. See also, Randal Lutter and John F. Morrall III, "Health-Health Analysis: A New Way to Evaluate Health and Safety Regulation," Journal of Risk and Uncertainty 1 (8) (1994), pp. 43-66; F. Kuchler, J.L. Teague, R.A. Williams & D.W. Anderson, "Health Transfers: An Application of Health-Health Analysis to Assess Food Safety Regulations," *Risk: Health, Safety & Environment, 10,* 315-332 (1999).

[8] "Recessions and the Costs of Job Loss," Steven J. Davis, Chicago Booth School of Business; Till von Watchter, Columbia University, September 12, 2011 (paper prepared for the Brookings Papers on Economic Activity).

future earnings are reduced by a daunting 19%, or about three years of earnings at the pre-layoff level.

Recent research on the adverse health impacts associated with unemployment also reach striking conclusions. For example, a paper in the *Journal of Social Science & Medicine* found that the risk of death for unemployed people was 63% higher than for employed persons.[9] Other research has concluded that symptoms of depression and anxiety were significantly greater in the unemployed than the employed. Moreover, unemployed men took more medications and visited physicians significantly more often than their employed counterparts did.[10] Adverse vascular changes also have been documented in individuals who lose their jobs late in their careers but prior to voluntary retirement.[11]

Masur and Posner estimate that *the costs of unemployment for an average worker could be as high as $260,000,* and they arrive at two key insights:

> "First, unemployment costs for workers are *far from trivial*. A *conservative estimate* is that an average worker who loses his job in a mass layoff will suffer *earnings losses of more than $100,000 over the rest of his life*, *plus a host of nonpecuniary costs including increased mortality and unhappiness, which could be valued at another $160,000*. Second, unemployment costs for workers vary with the characteristics of workers, such as age and experience and the industry in which they are employed." (Emphasis added).[12]

Masur and Posner also provide specific examples to illustrate how accounting for the costs of job displacement by regulation could change the outcome of benefit-cost analyses, such as EPA regulation of the pulp and paper industry.[13] In theory, if the analysis were taken seriously, it could alter the decision of whether and how to regulate, particularly for the most adversely affected industries.

Recommendations:

Our goal should be sustainable regulation – regulation that addresses environmental concerns, economic needs and social expectations. There is no better place for a robust manufacturing sector than the United States, which has been blessed with highly productive workers who only ask for the right to compete, creative entrepreneurs and

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[9] See David J. Roelfs, et al., *Social Science & Medicine,* Volume 72, Issue 6, March 2011.

[10] "Effects of Unemployment on Mental and Physical Health," Margaret W. Linn, et al., *American Journal of Public Health* (1985).

[11] W.T. Gallo et al., "*The Impact of Late Career Job Loss on Myocardial lnfarction and Stroke: A 10 Year Follow Up Using the Health and Retirement Survey,"* 63 Occupational & Envtl. Med. 683 (2006).

[12] Masur and Posner, supra note 2, at 618.

[13] Id. at 626-633.

innovators, abundant resources, a strong Democratic legal system, and regulatory agencies capable of leading the world on sustainable regulation.

Accordingly, the following recommendations are offered for your consideration:

Recommendations Related to Option One (Incorporate Costs of Job Displacement into BCAs)

- For economically significant rules, agencies should analyze the unemployment effects, monetize those impacts to the extent feasible, and incorporate them into the benefit-cost analysis.[14]

- The distributional impacts of job displacement by regulations, while outside the traditional benefit-cost framework, should be identified and described in the regulatory impact analysis and considered by the relevant policy-making officials.[15] Distributional impacts that agencies could describe in the RIA include whether there are particularly vulnerable subpopulations who could be harmed by job displacement and the impact.[16]

- An independent entity should perform analyses of the employment displacement effects of regulation. One possibility is the Office of Manufacturing Services in the Department of Commerce. The Office already has taken significant strides to assemble excellent staff, but it should be provided additional resources as needed. Having an independent entity conduct the analysis would foster greater objectivity and promote the development of expertise in state-or-the-art methodologies for conducting the analyses. The independent entity also could build a database and models that are publicly accessible and will facilitate employment impact analyses and promote transparency.

- Employment displacement analyses should account for the difference between short-term and longer-term employment impacts. For example, the use of job-years should be considered.

- OMB should prepare, and take public comment on, best practices for conducting employment displacement analyses for regulations. As an alternative to the government producing the information, OMB should allow affected industries to supply their own data and analyses for the government to use.

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[14] Noe, supra note 1, at 204 (noting that the longstanding guidance for regulatory analysis, OMB Circular A-4, does not specifically ask agencies to examine job destruction caused by regulatory policies, despite the language in E.O. 12866); Masur and Posner, supra note 2, at 633.

[15] Noe, supra note 1, at 204.

[16] Id.

- When the potential job displacement for an industry is calculated, it is critical that the analysis be done using data relevant to *that particular industry*, not an aggregation of data from disparate industries that bears little or no relevance to the industry at issue.[17]

Recommendation Related to Option 2 (Decisional Rule to Minimize Adverse Impacts)

- In the tradition of the Regulatory Flexibility Act, which is intended to minimize the adverse impacts of regulation on small entities, the President or OMB could direct the agencies to minimize the adverse impacts of regulations on disproportionately affected industries and their workers.[18] This would focus the regulatory agency, OMB and other participants in the regulatory review process on regulatory options that could minimize unnecessary regulatory costs. Such a decisional rule, if implemented rigorously, also would create a market for the production of high quality information about regulatory impacts. In fact, this exercise could reveal regulatory options that could significantly reduce unwarranted regulatory burdens, save workers' jobs, free up additional investment and job creation, and not sacrifice important regulatory benefits.

Thank you again for providing an opportunity to comment on whether and how agencies should consider the employment effects of regulation, and for taking the time to consider these personal thoughts. If you have any questions, please feel free to contact me at paul.noe1@verizon.net

Best regards

Paul R. Noe

Attachment

[17] See, e.g., Masur and Posner, supra note 2, at 633.

[18] See Noe, supra note 1, at 210.