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TESTIMONY

DESIGNING A REGULATORY SYSTEM FOR FUTURE GENERATIONS

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Ohio House State and Local Government Committee

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Chairman Wiggam, Vice Chair Ginter, Ranking Member Kelly, and members of the committee:

Thank you for allowing me to speak today with regard to the regulatory environment in Ohio. My name is James Broughel, and I am a senior research fellow at the Mercatus Center at George Mason University and an adjunct professor of economics and law at George Mason University. My research focuses on state regulatory institutions and procedures, the economic analysis of regulations, and economic growth.

The message I want to convey this afternoon is simple: actions policymakers take today have repercussions that will reverberate for years, decades, and even longer. It is all too easy to lose sight of the long run and focus on day-to-day politics and the 24-hour news cycle. We cannot afford to do so, however, if we want future generations to inherit the best possible world. In other words, there are difficult tradeoffs policymakers must consider between the short-run sense of security regulations often provide, and the long-run prosperity and progress humanity relies on to advance well-being and civilization.

Today, I have these broad points to make:

1. First, there is considerable evidence—empirical and theoretical—that regulations slow economic growth.
2. Second, even small reductions in growth rates will have profound negative consequences for the well-being of people in the future. By extension, small sustained improvements in growth rates have profound benefits.
3. Third, placing limits on the accumulation of regulation is a way to boost growth and therefore, well-being for people today and especially in the future.

REGULATIONS SLOW GROWTH

The empirical connection between regulation, economic growth, and the known contributors to economic growth has been made many times in the peer-reviewed academic literature. A 2013 study in the *Journal of Economic Growth* estimates that federal regulation has slowed the growth rate of the US economy by 2 percentage points per year on average since 1949.[1] This estimate suggests that, had

[1] John W. Dawson and John J. Seater, "Federal Regulation and Aggregate Economic Growth," *Journal of Economic Growth* 18, no. 2 (2013): 137–77.

regulation remained at its 1949 level, 2011 GDP would have been about $39 trillion, or 3.5 times higher than it actually was.[2]

A study published by the Mercatus Center estimates that growth has been slowed by 0.8 percentage points per year on average by federal regulations implemented since 1980.[3] That number may sound small, but in fact it suggests that had the federal government imposed a cap on regulation levels in 1980, then by 2012 the economy would have been $4 trillion larger, which amounts to $13,000 per person in the United States.

Notably, the legislation being considered before this committee today, House Bill 115, would place similar limits on the overall amount of regulation issued by Ohio regulatory agencies.

Researchers at the World Bank have estimated that countries with the least burdensome business regulations grow 2.3 percentage points faster annually than countries with the most burdensome regulations.[4]

One study, published in the *Quarterly Journal of Economics*, a top-ranked economics journal, found that countries with heavier regulation of business entry have higher corruption, larger unofficial economies, and less intense competition among firms, all without corresponding improvements in the quality of public or private goods.[5] In the words of the authors of the study,

> We do not find that stricter regulation of entry is associated with higher quality products, better pollution records or health outcomes, or keener competition. But stricter regulation of entry is associated with sharply higher levels of corruption, and a greater relative size of the unofficial economy.[6]

Numerous other academic studies have confirmed the negative effects that product market regulations can have on important contributors to economic growth, including investment rates,[7] innovation and research and development spending efficacy,[8] employment,[9] and productivity growth.[10]

Regulations, by definition, restrict the scope of activities that entrepreneurs can engage in. Restricting access to new technologies can be especially problematic, since technology is known to be a fundamental driver—if not *the* fundamental driver—of economic growth.[11] Regions and industries that are further from the technological frontier (i.e., that are less technologically developed) are likely to enjoy greater benefits from liberalization reforms,[12] such as regulatory reduction efforts. Poorer, less technologically developed

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[2] Patrick A. McLaughlin, Nita Ghei, and Michael Wilt, "Regulatory Accumulation and Its Costs: An Overview" (Mercatus Policy Brief, Mercatus Center at George Mason University, Arlington, VA, 2018).
[3] Bentley Coffey, Patrick A. McLaughlin, and Pietro Peretto, "The Cumulative Cost of Regulations" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, 2016).
[4] Simeon Djankov, Caralee McLiesh, and Rita Maria Ramalho, "Regulation and Growth," *Economic Letters* 92, no. 3 (2006): 395–401.
[5] Simeon Djankov et al., "The Regulation of Entry," *Quarterly Journal of Economics* 117, no. 1 (2002): 1–37.
[6] Djankov et al., "The Regulation of Entry."
[7] Alberto Alesina et al., "Regulation and Investment," *Journal of the European Economic Association* 3, no. 4 (2005): 791–825.
[8] Chiara Franco, Fabio Pieri, and Francesco Venturini, "Product Market Regulation and Innovation Efficiency," *Journal of Productivity Analysis* 45, no. 3 (2016): 299–315.
[9] Giuseppe Nicoletti et al., "European Integration, Liberalization, and Labor-Market Performance," in *Welfare and Employment in United Europe*, ed. Giuseppe Bertola, Tito Boeri, and Giuseppe Nicoletti (Cambridge, MA: MIT Press, 2001).
[10] Renaud Bourlès et al., "Do Product Market Regulations in Upstream Sectors Curb Productivity Growth? Panel Data Evidence for OECD Countries," *Review of Economics and Statistics* 95, no. 5 (2013): 1750–68.
[11] James Broughel and Adam Thierer, "Technological Innovation and Economic Growth: A Brief Report on the Evidence" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, 2019).
[12] Giuseppe Nicoletti and Stefano Scarpetta, "Regulation, Productivity, and Growth: OECD Evidence," *Economic Policy* 18, no. 36 (2003), 11–72.

US states may be disproportionately burdened by regulation for this reason; and manufacturing may be particularly burdened, relative to services industries, by excessive regulation.[13]

Outside this robust empirical literature, economic theory also supports the notion that regulations hinder growth. Leading growth economists readily admit their preference that policy aim for a rate of growth below the economy's maximum sustainable rate of growth.[14] Why? Because many economists find it optimal to transfer consumption from the future to the present (i.e., for present citizens to consume at the expense of future citizens). These economists believe this would bring about a more equitable distribution of wealth across generations. Unfortunately, these economists conceal value judgments about their preferences for intergenerational equality in arcane technical aspects of policy analysis.[15] For example, although cost-benefit analysis (CBA) is sometimes undertaken before regulations go into effect, CBA also allows policies that provide short-term, temporary benefits while slowing long-run economic growth to pass a cost-benefit test in many instances.[16]

Economists, like policymakers, too often focus on the short run, but both groups should not lose sight of the long run.

SLOW GROWTH HAS DIRE CONSEQUENCES FOR HUMAN WELL-BEING, ESPECIALLY IN THE FUTURE

The empirical academic literature suggests regulations could slow annual economic growth by a percentage point or more. To put this in context, in 2017 Ohio real GDP grew 1.6 percent, and the 2007–2017 compound annual growth rate for Ohio real GDP was 0.9 percent,[17] so adding a percentage point or two to annual economic growth could double or even triple Ohio's current growth rate. A difference of one or two percentage points in lost growth may not sound like much, but small reductions in growth rates have enormous consequences for living standards over long periods.

Growth of 1 percent a year means it takes 70 years to double real GDP, just nine years shy of the life expectancy of an American born in the year 2014.[18] When the economy grows at 2 percent annually, the time to double GDP falls to 35 years—roughly half a lifetime. An economy growing at 3 percent will double GDP in 24 years, roughly the time it takes to graduate college. These small differences in growth rates mean the difference between an economy doubling one, two, or three times in a lifetime.

It is difficult to even conceive of what the US economy would be like were it two to three times as large as it is today. The benefits in terms of technology, wealth, and opportunity stretch the bounds of the imagination. The miracle of compound growth becomes more evident when considering longer time horizons, as demonstrated in table 1 below. Table 1 presents how a theoretical $100 investment would grow over time at various annual rates of return.

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[13] Giuseppe and Scarpetta, "Regulation, Productivity, and Growth."
[14] See, for example, Kenneth Arrow, "The Trade-Off between Growth and Equity," in *Theory for Economic Efficiency*, ed. Greenfeld, et al. (Cambridge, MA: MIT Press, 1979); F. P. Ramsey, "A Mathematical Theory of Saving," *Economic Journal* 38, no. 152 (1928): 543–59; Tjallin C. Koopmans, "On the Concept of Optimal Economic Growth" (Cowles Foundation Discussion Paper No. 163, Cowles Foundation for Research in Economics at Yale University, New Haven, CT, December 6, 1963).
[15] One example of such arcane technical aspects is the discount rate. See James Broughel, "Equity or Efficiency? The Battle for the Soul of Benefit-Cost Analysis" (Mercatus Policy Brief, Mercatus Center at George Mason University, Arlington, VA, March 2019).
[16] This can occur because distant future outcomes receive very little weight in analysis as a result of the practice of discounting.
[17] Bureau of Economic Analysis, "BEARFACTS (Ohio)," March 26, 2019, https://apps.bea.gov/regional/bearfacts/action.cfm.
[18] Centers for Disease Control and Prevention, *Table 15. Life Expectancy at Birth, at Age 65, and at Age 75, by Sex, Race, and Hispanic Origin: United States, Selected Years 1900–2016*, 2017, https://www.cdc.gov/nchs/data/hus/2017/015.pdf.

TABLE 1. COMPOUNDING AT DIFFERENT GROWTH RATES

	Annual Growth Rates			
Year	1%	3%	7%	10%
0	$100	$100	$100	$100
1	$101	$103	$107	$110
5	$105	$116	$140	$161
10	$110	$134	$197	$259
25	$128	$209	$543	$1,083
50	$164	$438	$2,946	$11,739
75	$211	$918	$15,988	$127,190
100	$270	$1,922	$86,772	$1,378,061

Source: James Broughel, *Regulation and Economic Growth: Applying Economic Theory to Public Policy* (Arlington, VA: Mercatus Center at George Mason University, 2017), 7.

As should be clear, the difference between 1 percent annual growth and 10 percent annual growth is beyond night and day. And while national or state economic growth on the order of 7 to 10 percent annually is probably unrealistic, growth in the range of 3 to 4 percent is not. Some states' economies are growing north of 3 percent annually right now.[19] And while GDP does not measure all aspects of human well-being, the income generated by a vibrant and growing economy can improve living standards in countless ways. With more wealth, Ohioans would have far greater opportunity to increase investments in health and education, pass along bequests to their children, and pursue the kind of life they and their offspring think is best.

At some point, an economy that grows more quickly than another economy is so much richer, in terms of wealth, technology, and opportunity that one can say that it is objectively better off in terms of human well-being.[20] Every state in the country should be concerned about growth, especially Ohio, with growth rates below the national rate and regulatory restrictions far above the state average.[21]

THE MORAL CASE FOR CONTROLLING REGULATION

Regulation affects nearly every aspect of modern human life.[22] Toothbrushes are treated as medical devices and are regulated by the FDA. The amount of water toilets use when they flush is regulated by the Department of Energy. The EPA regulates shower heads. And the Consumer Product Safety Commission even regulates matchbooks. States impose countless additional restrictions on top of these federal mandates.

While many of these rules have benefits associated with them, the accumulation of regulations also slows economic growth. It would be one thing if the burdens of reduced growth fell primarily on current citizens—they would bear the consequences for any mistakes made by the leaders they elected. But in fact, the burdens of the current generation's mistakes fall primarily on others—people in the future—when regulations slow economic growth.

[19] For example, in 2017, Oregon real GDP grew 3.6 percent.
[20] Bureau of Economic Analysis, "BEARFACTS (Ohio)."
[21] A recent estimate is that Ohio has more than 100,000 restrictions in its regulatory code than the average state. See James Broughel, "Achieving a Modern Regulatory System in Ohio" (Testimony before the Ohio Senate Government Oversight and Reform Committee, Mercatus Center at George Mason University, Arlington, VA, February 26, 2019).
[22] Susan E. Dudley, "A Regulated Day in the Life," *Regulation*, Summer 2004.

Regulatory cleanup is therefore more than a matter of simple good housekeeping. Managing regulatory burdens is necessary if the current generation is to be a good steward of civilization and leave behind the best possible world for future generations.

CONCLUSION

Regulatory reform is atop many states' agendas, including Ohio's. Numerous states have engaged in red-tape-cutting reforms in recent years.[23] Virginia is one notable state with a bipartisan regulatory reduction effort underway.[24] Even Idaho, one of the least regulated states (according to Mercatus Center data), is engaged in comprehensive regulatory reforms.[25] Some of these efforts have been ongoing for years with no detrimental effect on public health, safety, or the environment observed.

With House Bill 115, Ohio may be poised to be the next leader among the US states when it comes to meaningful regulatory reforms. This bodes well for the well-being of state residents now and in the future.

Thank you for granting me the opportunity to speak today. I'm happy to answer any questions you may have.

ATTACHMENTS (2)

James Broughel and Jonathan Nelson, "A Snapshot of Ohio Regulation in 2018" (Mercatus Policy Brief)
James Broughel, "Ohio, A Leader in Cutting Red Tape, Can Do More," *Columbus Dispatch*, April 19, 2018

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[23] One recent estimate is that 20 states have engaged in red tape cutting reforms since 2010. See Justin Smith, "No MO Red Tape: Cutting Burdensome Rules in Missouri" (presentation, University of Missouri Law School, Columbia, MO, February 8, 2019); Exec. Order No. 2016-03, 22 Arizona Administrative Register 900 (December 31, 2016); Exec. Order No. 2017-02, 23 Arizona Administrative Register 540 (March 3, 2017); Maryland Exec. Order No. 01.01.2015.20 (July 9, 2015); Colorado Exec. Order No. D2012-002 (January 19, 2012); Massachusetts Exec. Order No. 562 (March 31, 2015); Illinois Exec. Order No. 2016-13 (October 17, 2016); Nebraska Exec. Order No. 17-04 (July 6, 2017); Missouri Exec. Order No. 17-03 (January 10, 2017); Missouri Exec. Order No. 17-11 (April 11, 2017).

[24] James Broughel, "A Reform That Offers Hope for Centrists," *Washington Post*, March 14, 2018.

[25] Idaho Executive Order 2019-02 (January 21, 2019); James Broughel, "Idaho's New 'Budget' for Red Tape," *Coeur d'Alene Press*, April 1, 2019.

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POLICY BRIEF

A Snapshot of Ohio Regulation in 2018

246,852 Restrictions, 15.2 Million Words, and 21 Weeks to Read

by James Broughel and Jonathan Nelson

February 2018

It would take an ordinary person more than two and a half years to read the entire US *Code of Federal Regulations* (CFR), which contained more than 104 million words in 2016.[1] The sheer size of the CFR poses a problem not just for the individuals and businesses that want to stay in compliance with the law but also for anyone interested in understanding the consequences of this massive system of rules. States also have sizable regulatory codes, which add an additional layer to the large body of federal regulation. A prime example is the online version of the 2018 *Ohio Administrative Code* (OAC).[2]

Researchers at the Mercatus Center at George Mason University developed State RegData,[3] a platform for analyzing and quantifying state regulatory text. State RegData captures information in minutes that would take an ordinary person hours, weeks, or even years to obtain. For example, the tool allows researchers to identify the industries that state regulation targets most by connecting text relevant to those industries with restrictive word counts. Known as regulatory restrictions, the words and phrases *shall*, *must*, *may not*, *prohibited*, and *required* can signify legal constraints and obligations.[4] As shown in figure 1, the three industries with the highest estimates of industry-relevant restrictions in the 2018 OAC are chemical manufacturing, food manufacturing, and animal production and aquaculture.

1. This assumes that a person reads 300 words per minute for 40 hours per week with two weeks of vacation per year. See "RegData 3.0," QuantGov; Patrick A. McLaughlin, Oliver Sherouse, Daniel Francis, Michael Gasvoda, Jonathan Nelson, Stephen Strosko, and Tyler Richards, "RegData 3.0 User's Guide," accessed February 2, 2018, https://quantgov.org/regdata/users-guide/.
2. Ohio Laws and Rules, *Ohio Administrative Code*, accessed January 3, 2018.
3. State RegData is part of a broader project called QuantGov, which seeks to quantify legal text. See Patrick A. McLaughlin and Oliver Sherouse, "QuantGov—A Policy Analytics Platform," QuantGov, December 20, 2017.
4. Restrictions can also occur in legal text for other purposes, such as for definitional purposes. At times, restrictions may relate to government employees rather than the private sector.

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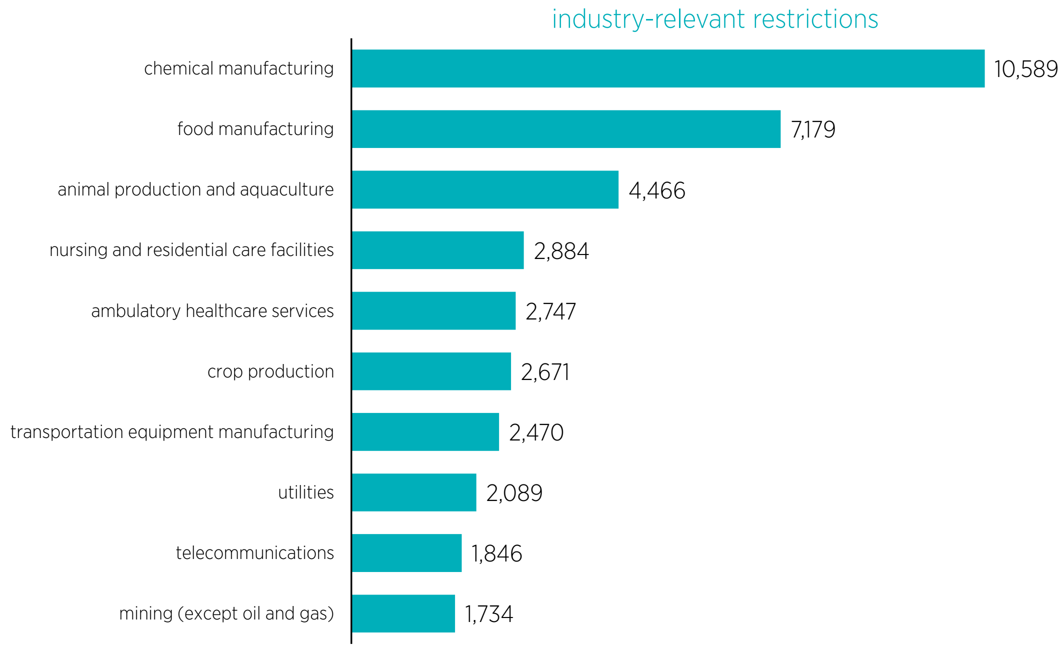
Figure 1. Top 10 Industries Targeted by Ohio State Regulation in 2018



Source: State RegData, "Ohio," http://www.quantgov.org/data/.

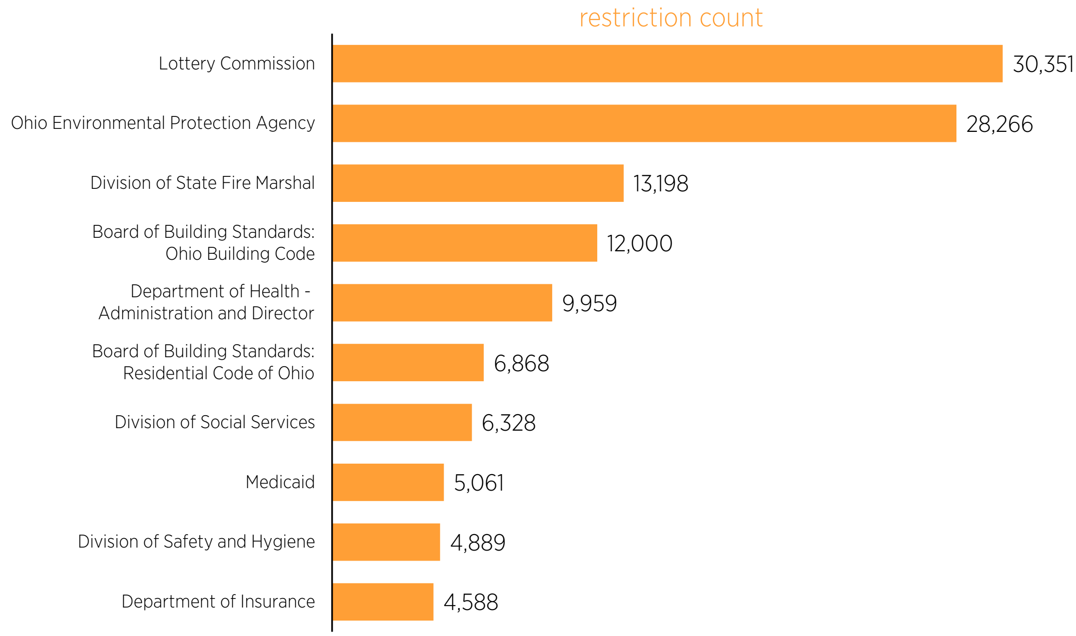
State RegData also reveals that the OAC contains 246,852 restrictions and 15.2 million words. It would take an individual about 847 hours—or more than 21 weeks—to read the entire OAC. That's assuming the reader spends 40 hours per week reading and reads at a rate of 300 words per minute. By comparison, there are more than 1.08 million additional restrictions in the federal code.[5] Individuals and businesses in Ohio must navigate these different layers of restrictions to remain in compliance.

The titles of the OAC are organized by regulatory commission, program, board, or agency. Figure 2 shows that the title of the OAC associated with the Lottery Commission contains more than 30,000 restrictions. By this measure, this commission is the biggest regulator in Ohio. Coming in second is the Ohio Environmental Protection Agency, with more than 28,000 restrictions.

Federal regulation tends to attract the most headlines, but it is important to remember that the more than 104 million words and 1.08 million restrictions in the federal code significantly understate the true scope of regulation in the United States. States like Ohio write millions of additional words of regulation and hundreds of thousands of additional restrictions. State-level requirements carry the force of law to restrict individuals and businesses just as federal ones do.

5. "RegData 3.0"; McLaughlin et al., "RegData 3.0 User's Guide."

Figure 2. Top 10 Regulators in Ohio in 2018



Source: State RegData, "Ohio," http://www.quantgov.org/data/.

Researchers are only beginning to understand the consequences of the massive and growing federal regulatory system on economic growth and well-being in the United States.[6] Meanwhile, the effects of state regulation remain largely unknown. If this snapshot of Ohio regulation in 2018 is a good indicator, then the states are also active regulators, suggesting that the full impact of regulation on society is far greater than that of federal regulation alone.

6. See, for example, Bentley Coffey, Patrick A. McLaughlin, and Pietro Peretto, "The Cumulative Cost of Regulations" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, 2016).

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The Columbus Dispatch

Opinion

James Broughel: Ohio, a leader in cutting red tape, can do more

Posted Apr 19, 2018 at 12:01 AM
Updated Apr 19, 2018 at 6:11 AM

Recently Ohio lawmakers led by state Senate President Larry Obhof, R-Medina, called for a renewed push to modernize the state's regulatory system. Figuring out which rules are necessary to protect Ohioans and which have become outdated is an important and urgent bipartisan issue. Neighbors Kentucky, Michigan, Pennsylvania and West Virginia each carry far less regulation than Ohio, making them tempting destinations for businesses to move or set up shop.

The Trump administration has also made news with its regulatory reform efforts in the past year, and many Ohioans might be surprised to learn that Washington is taking a page from Gov. John Kasich's playbook. In fact, Ohio has been experimenting with regulatory reform as part of an ongoing effort since 2011.

Given that the program has been in place for more than seven years, it makes sense to take stock of its results and the lessons it holds, both for Ohio and for reformers across the nation.

Created by Kasich in 2011, the Ohio Common Sense Initiative exists to foster a more jobs-friendly regulatory environment. Twice a year the program provides updates. A 2017 report, for example, details how 341 rules were rescinded last year out of 2,613 that the CSI office reviewed. That's progress.

Many additional rules have been amended, which likely lowers costs to the public further. Overall, the CSI has reviewed 12,500 rules since 2012 — of which 1,049 were repealed.

And 1,049 repealed rules isn't bad. But what if there are 100,000 rules in total? Or 200,000? Without knowing more about how many regulations are actually on the state's books, it's difficult to say if the CSI has made a meaningful reduction in red tape.

The Mercatus Center at George Mason University has a project to quantify state regulations, because the total in many states is actually a mystery. Our newest report describes how the Ohio Administrative Code contains more than 15 million words. It's so long that an ordinary person would need 21 weeks to read it, assuming 40 hours a week spent reading.

Included in these 15 million words are nearly 247,000 restrictive words like "shall," "must" or "required" — a simple way to count up the staggering amount of commands and prohibitions in a state's code.

Word counts and restriction counts don't compare perfectly to the numbers in the CSI reports, but these figures nonetheless suggest a lot of room to improve Ohio's business climate. Of the 22 state codes analyzed so far, only Illinois and New York have more restrictions than Ohio. Meanwhile, Arizona has about a quarter as much regulation as Ohio, and neighbors West Virginia, Michigan and Kentucky each have at least 100,000 fewer restrictions in their codes.

So how can Ohio demonstrate that it's a welcoming place for entrepreneurs and innovators?

One example comes from Virginia, home of a brand-new regulatory-reduction pilot program. It tasks the state's Department of Planning and Budget with counting up and tracking the various regulations and requirements imposed by state agencies. This simple reform is actually a big deal because it gives legislators a solid grasp of how much red tape is on the state's books.

Additionally, the Virginia law sets a goal of reducing regulatory burdens by 25 percent at two state agencies: the Department of Professional and Occupational Regulation and the Department of Criminal Justice Services. This target is to be met in three years' time.

Not only is the law ambitious, but it is bipartisan as well. It passed the legislature almost unanimously.

Ohio should take note. By counting and tracking how much regulation is actually in place, it is easier to assess whether reductions in red tape are actually meaningful. Moreover, an explicit reduction target tied to a concrete deadline gives policymakers a clearer goal to strive for and makes it easier to hold them accountable later on.

The Common Sense Initiative has certainly taken some good first steps, and Ohioans should be proud of its work. Before Gov. Kasich leaves office, his administration, along with leaders in the legislature, may want to consider updating their approach to keep Ohio at the forefront of regulatory reform efforts in the states.

James Broughel is a research fellow with the Mercatus Center at George Mason University and co-author of the new study "A Snapshot of Ohio Regulations in 2018."