

October 25, 2010

California Regulatory System Challenges and Potential Reforms

Testimony to the Little Hoover Commission

By Dr. Adrian Moore

Vice President, Reason Foundation



The extent and costs of regulations in California are a frequent topic of debate. For example the latest *Small Business Survival Index* ranks California 49th and the latest *Freedom in the 50 States* report ranks California 46th in regulatory policy, while at the same time the state is hailed by some for being a leader in crafting and implementing new environmental regulations.

Whether or not you agree with the extent of California's regulatory reach, I think all would agree that California regulates more than the average state, and is often first to adopt new regulatory approaches. Given that, the state should take a keen interest in having a top-notch process of analysis in developing new regulations, and a strong culture of assessing the implementation and effectiveness of regulations that are in place. But we do not.

Analysis used to craft regulations is of widely varying quality across agencies in California government, and often does not follow globally available best practices. Even worse, we have not culture of ex-post regulatory evaluation in California, indeed it is rare that the actual effect of regulations is compared to predicted effects.

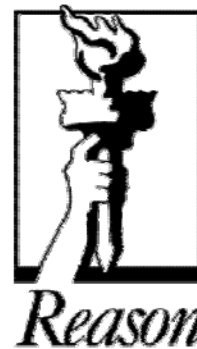
I'd like to briefly suggest three changes to how California utilizes regulations.

1. Use rifles, not shotguns. If a problem should arise that appears to require regulatory intervention, the goal should be to develop measures that, like rifle shot, accurately and effectively target the problem. Of course, it may take multiple "shots" to adequately address a problem. But if each is targeted for best effect, the number of regulatory interventions needed should be kept as low as feasible. All too often however, we use a shotgun approach instead, responding to a problem with a spray of regulations, developed simultaneously, to "shoot" as many parts of the problem as possible. I have seen this approach particularly in how our non-attainment areas tackle reducing air pollution.

The problem with the shotgun approach is that it spreads the analytical effort across many measures at once, diluting the quality of analysis, and does not allow prioritization based on effectiveness. In the many instances where elected or appointed board members ultimately approve new regulations, a shotgun blast of measures does not allow those board members to adequately asses and evaluate each measure. The same is true for review and comment by stakeholders.

3415 S. Sepulveda Blvd., Suite 400, Los Angeles, CA 90034 • 310-391-2245 • Fax: 310-391-4395 • www.reason.org

3415 S. Sepulveda Blvd Suite 400 Los Angeles, CA 90034 • 310-391-2245 •
TRUSTEES
William A. Dunn, *DUNN Capital Management, Chairman* • Thomas E. Beach, *Beach Investment Counsel* • Drew Carey • Derwood S. Chase, Jr., *Chase Investment Counsel Corporation* • James R. Curley, *Financial Conservatism International, LLC* • Richard J. Dennis, *Dennis Trading Group* • David Fleming, *Latham & Watkins, LLC* • James D. Jamison • Manuel S. Klausner, *Lew Offices of Manuel S. Klausner, PC* • David H. Koch, *Koch Industries* • James Lindott, *Sterling Foundation Management, LLC* • Stephen Modzelewski, *Maple Engine, L.P.* • David Nott, *Reason Foundation* • George F. Ohrtstrom • Robert W. Poole, Jr., *Reason Foundation* • Carol Sanders • Vernon L. Smith, *Chapman University* • Richard A. Wallace, *Freedom Communications, Inc.* • Fred Young, *Former Owner, Young Radiator Company* • Pierluigi Zappacosta, *Sierra Sciences* • Walter E. Williams, *Trustee Emeritus*



A “rifle” approach allows prioritization of measures, ideally focusing on the ones with the most potential “bang for the buck.” I have often seen as much time, effort, and debate spent on a complex measure that solves one percent of the problem as was spent on an equally complex measure that solves 40 percent of the problem.

2. Use peer review of rulemaking analysis. When staff or consultants develop analytical reports in support of a rulemaking process, those reports should be peer reviewed by knowledgeable but disinterested parties. And peer review comments and changes made, or not made, to the reports, should be part of the rulemaking public record. Such is typically the case with regulatory rule making in the EU.

Some of you may recall the notoriously controversial case of regulations governing water use in the Upper Klamath River in Oregon to protect endangered fish species. In that case a peer review conducted after the rules became controversial severely questioned the quality of the analysis used in crafting the rules. Closer to home, the recent retraction by CARB of diesel fuel standards due to faulty analysis may have been prevented by peer review prior to finalizing the rules.

We rely too much in California on public review and comment by stakeholders and others. This process is often highly politicized and “noisy” in the sense that there is a lot of not very useful comment mixed in with the useful. Public comment is an important part of the process of regulation, but we should not rely on it alone to provide quality independent review of the analysis underlying proposed regulations.

3. Look back and adjust. Regulations are typically enacted based on modeled or projected impacts. They also typically consume scarce resources. We can be certain that some regulations work better than predicted, some work as well as predicted, and some do meet predictions. But in California we rarely perform ex-post analysis to determine the effectiveness of regulations and adjust accordingly. Ideally we would have a system that eliminates regulations that have not been effective and shifts resources freed up by that to ones that have been more effective than predicted.

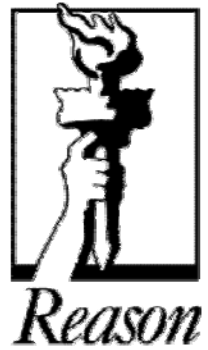
Of course, many agencies would argue that they do not have adequate resources to analyze proposed regulations, let alone go back and analyze the effectiveness of past regulations. So the shift I suggest would entail a major policy change. But the cost of ex-post analysis would likely be offset by allowing us to stop wasting resources on regulations that have not lived up to expectations.

I suggest that regulatory bodies in state government begin to do ex-post analysis of their “biggest” regulations first, and work from there. At the same time, legislative regulations should incorporate sunset provisions, requiring the legislature to evaluate the effectiveness of a rule after it is in place and vote to sustain rules deemed effective and kill or modify ones that are not.

3415 S. Sepulveda Blvd., Suite 400, Los Angeles, CA 90034 • 310-391-2245 • Fax: 310-391-4395 • www.reason.org

3415 S. Sepulveda Blvd Suite 400 Los Angeles CA 90034 • 310-391-2245 •
TRUSTEES
William A. Dunn, *DUNN Capital Management, Chairman* • Thomas E. Beach, *Beach Investment Counsel* • Drew Carey • Derwood S. Chase, Jr., *Chase Investment Counsel Corporation* • James R. Curley, *Financial Consortium International, LLC* • Richard J. Dennis, *Dennis Trading Group* • David Fleming, *Latham & Watkins, LLC* • James D. Jameson • Manuel S. Klausner, *Law Offices of Manuel S. Klausner, PC* • David H. Koch, *Koch Industries* • James Lintott, *Sterling Foundation Management, LLC* • Stephen Modakowski, *Maple Engine, L.P.* • David Nott, *Reason Foundation* • George F. Ohmstrom • Robert W. Poole, Jr., *Rausser Foundation* • Carol Sanders • Vernon L. Smith, *Chapman University* • Richard A. Wallace, *Freedom Communications, Inc.* • Fred Young, *Former Owner, Young Radiator Company* • Pielisigi Zappacosta, *Sierra Science* • Walter E. Williams, *Trustee Emeritus*

There is a theme to my suggestions—they all improve the transparency of the regulatory process. We have a lot of public comment on proposed rules, but that has not proved adequate to ensure that we have the best rulemaking process possible and to ensure that we are getting the most effective rules possible in both solving problems and minimizing the costs of those solutions.



3415 S. Sepulveda Blvd., Suite 400, Los Angeles, CA 90034 ■ 310-391-2245 ■ Fax: 310-391-4395 ■ www.reason.org

TRUSTEES

William A. Dunn, *DUNN Capital Management, Chairman* ■ Thomas E. Beach, *Beach Investment Counsel* ■ Drew Canoy ■ Derwood S. Chase, Jr., *Chase Investment Counsel Corporation* ■ James R. Curley, *Financial Consortium International, LLC* ■ Richard J. Dennis, *Dennis Trading Group* ■ David Fleming, *Latham & Watkins, LLC* ■ James B. Janssen ■ Manuel S. Klausner, *Law Offices of Manuel S. Klausner, PC* ■ David H. Koch, *Koch Industries* ■ James Lintou, *Storing Foundation Management, LLC* ■ Stephen Modakowski, *Maple Engine, L.P.* ■ David Nott, *Reason Foundation* ■ George F. Ohmstrom ■ Robert W. Poole, Jr., *Reason Foundation* ■ Carol Sanders ■ Vernon L. Smith, *Chapman University* ■ Richard A. Wallace, *Freedom Communications, Inc.* ■ Fred Young, *Former Owner, Young Radiator Company* ■ Pielisigi Zaypaxocis, *Sierra Sciences* ■ Walter E. Williams, *Trustee Emeritus*