Liberate to Stimulate

A Bipartisan Agenda to Restore Limited Government and Revive America's Economy

Competitive Enterprise Institute

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Competitive Enterprise Institute

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Introduction

Reining in America's Regulatory Leviathan: America Gets a Second Chance

By Fred Smith

My grandmother used to tell me, "It doesn't matter whether your socks are red or blue, you should change them frequently." Americans did just that recently. To change metaphors, voters have chosen many new horses to run on the political race track. So far, this new team seems promising. They have killed the House climate-change subcommittee and refused to increase taxes. Yet the Washington race track still veers left. Our challenge is to pull the reins of these new entries toward limited government.

We at the Competitive Enterprise Institute (CEI) have spent 26 years raising the saliency of regulations on our economy. Taxes and spending receive plenty of public scrutiny, which makes regulation an increasingly attractive option for those who favor greater political intervention in the economy. Our goal is to ensure that regulations are subject to the same degree of oversight as taxes, spending, and legislation in general. The Tea Party movement's success in the recent elections suggests that awareness of these burdens is growing. Thus, we are more hopeful that economic liberty and regulatory reform will make some significant headway in 2011. To further that goal, CEI is unveiling a *Liberate to Stimulate* deregulatory agenda, which is summarized in this document.

The mixed economy has weakened market disciplines, while overreaching regulations have encouraged irresponsible and erratic actions. The continuation of the recession owes much to the fact that few entrepreneurs find it prudent to invest in a world where rules change unpredictably and constantly at the whim of regulators.

Opportunities abound for true reform in the new Congress, and CEI is proposing a strategy to pursue them. We are confronting all forms of state intervention head on—including government mandates, regulations, subsidies, private sector rent-seeking, and the moral hazards created by the socialization of risk. To that end, this Agenda for Congress outlines actions to advance a world of freedom and responsibility—a restoration of the Founders' vision of limited government.

Unlike their European counterparts, who sought outright government ownership of industry, 20th-century American Progressives left the illusion of free markets in place, while imposing an array of mandates on businesses via taxes, regulations, and subsidies. Under the European model of direct government ownership, the costs of statist policies are more apparent and easily attributable to politics. In contrast, the American regulatory welfare state hides costs from government balance sheets, and those costs are borne by businesses and consumers. Political failures are blamed on the private sector, making it all the more difficult to rein in the regulatory state. We seek to find creative ways of disciplining the excesses of government, a task needed now more than ever.

In 2011, we will have a new team in Washington. Freshman legislators, backed by their constituents, have promised to reduce the size of government. But that effort will not be easy. After all, the weakening of the limits on government power took over a century, beginning with the Progressive era in the early 20th century. There are no magic bullets to dismantle Leviathan. Decades of overspending, overregulating, and overintervening must be rolled back incrementally, as they were imposed. Recall that in 1994, small-government Republicans roared into Washington with an ambitious reform agenda—and soon became mired in the bogs of the Beltway. If today's Republicans replicate their predecessors' mistakes, their tenure will be even briefer.

Real change is needed. The economic "emergency" measures advanced by the Bush and Obama administrations have done little to alleviate the financial crisis—and likely made it worse. Top-down solutions have failed. Attempts to continue this approach are unlikely to result in political gains. The disasters unfolding in Greece and Ireland, and threatening all of Europe, drive that lesson home. Back home, California, Illinois, and other states teetering on bankruptcy from overspending and unfunded state retirement pensions create pressures for further bailouts that must be resisted.

CEI will work with the new Congress on advancing solutions to these issues. We look forward to sharing our ideas on how to jump-start the nation's economic engine, to reengage America's entrepreneurial spirit. We have a lot of work to do.

Botched, partial deregulations have hampered many sectors of the economy—including such crucial network industries as electricity, telecommunications, and airlines. The solution is not increased state control or infrastructure subsidies, but *true liberalization*. The immediate challenge is to fight against the typical Washington "do something" mantra—that is, to "do something" to expand the government's role—and, instead, ask legislators to remove and reduce the barriers to economic growth. CEI believes that "doing something" can mean doing less: Congress doesn't need to tell the grass to grow; rather it need only move the rocks off of it!

With major opportunities, come major risks. As a Louisianan, I am well aware of populism's allure in the name of "helping the little guy," even when that help hurts everyone else and creates long-lasting economic damage. The Bush-Obama interventions in areas like health, education, finance, and the environment threaten the dynamism of America's market economy. We will work, as we always have, with lawmakers of both parties to oppose bad ideas, and to advance good ones.

In recent Congresses, both Republicans and Democrats massively expanded the federal government—and voters punished them for it. Now the voters have granted the Republicans a tentative trust to set the ship of state aright. They can deliver on this charge in today's globalized world and retain their power only if they succeed in crafting, marketing, and implementing a truly pro-growth agenda.

Economic liberalization must lie at the heart of that agenda. This volume offers policy proposals to the reformers of all parties to help boost economic and personal liberties. It will be an interesting few years. We plan to see this race to the finish.

Secure the Economy

Deregulate to Stimulate

By Wayne Crews

When it comes to our economy, how did we get into this mess and how do we get back to sustained growth? The need to deregulate the nation's productive sector shouts at us, but Congress doesn't seem to hear it.

Government spending is out of control, but when we fail to confront regulation, we are missing most of the story behind the expanding state. Even before the financial crisis and the subsequent huge bailouts and stimulus bills to supposedly address that crisis, government was already expanding to gargantuan levels.

Today, America's government is the largest that has ever existed. President George W. Bush's $3.1 trillion budget was the first ever to reach that level. His administration also produced the first-ever $2 trillion budget. President Obama has shown little inclination to reverse this trend.

Regulations on the private sector continue to mount alongside this spending spree. CEI's annual *Ten Thousand Commandments* report cites regulatory costs of well over $1 trillion—a hidden tax one-third the size of the federal budget!

Yet regulatory costs draw much less public rebuke than taxes, because they are often concealed in the prices of goods. Thus, when politicians find it difficult to raise taxes to pay for their policy goals, they regulate. This is justified under the notion that government must help society manage risks. Yet the state does not provide the answer to every societal risk.

Instead, we must turn to the marketplace's disciplining role in consumer protection, which boosts safety as a competitive feature. We must improve competitive markets' ability to impose discipline in the form of reputation and disclosure.

Consider further that some of our most economically distressed industries have long been overwhelmingly directed by Washington regulators, not market forces. I do not know of a time over the past 100 years when the government did not regulate money, credit, and interest rates in America—yet markets always take the brunt of the blame for financial crises, as the new Dodd-Frank financial reform bill indicates. Markets can deal with firms too big to fail—what we cannot afford is a government too big to succeed!

Until now, most regulatory reform efforts have amounted to going after Moby Dick with a rowboat and tartar sauce. What we need now is sweeping liberalization, to remove the impediments that hobble wealth creation and enterprise on unprecedented scales. We need rational alternatives to interventionism and to the regulatory nanny state. In short, we need to liberate to stimulate.

The issue is not whether industry has to be regulated, or "planned." Rather, it is over who will do that planning, as the legenday Nobel Prize-winning economist F.A. Hayek put it so well. Consciously maintaining a sensible wall of separation between state and economy must guide the agenda to restore America's competitiveness and economic health.

The United States—now only 235 years old—became richer than the rest of the world in a historical blink of an eye. We need to keep in mind how that remarkable achievement occurred, and how it can be sustained as other nations embrace institutions of liberty and create increasingly competitive markets.

We need to hold the federal regulatory state's 60 agencies, thousands of annual rules, and *Federal Register* pages to at least the same standards of disclosure and accountability that apply to the fiscal budget.

Congress should implement a moratorium on non-essential new rulemaking.

It should implement a bipartisan regulatory reduction commission and task it to review the regulatory state as a whole and enact a comprehensive package of cuts.

In addition, Congress should strengthen permanent and automatic rule sunsetting reviews. All rules should have an expiration date like a carton of milk.

Congress must end regulation without representation by requiring fast-track Congressional approval for controversial major business regulations.

Finally, Congress should create a Regulatory Report Card—possibly modeled on *Ten Thousand Commandments*—to accompany the federal budget, in order to shed light on the currently hidden tax of regulation.

Our economic downturns are not attributable to market failure but to the the failure to have markets. The bold political action and genuine leadership needed in today's crisis is different from what has been seen in Washington to date. Indeed, the political price can be too high for election-bound lawmakers or career bureaucrats. Yet we must make every effort.

As Hayek pointed out, the politicians blamed during an inevitably bumpy transition to something closer to healthy free enterprise will be the ones who stop the flow of government benefits to the politically connected, bring down inflation, and unwind market-distorting regulations—not the ones who started those costly interventions decades earlier.

Real stimulus—involving comprehensive liberalization of a fettered economy—requires politically difficult changes in what people expect from government. Leadership requires taking on that challenge.

Capitalism is one of the greatest democratizing innovations in human history, a way for individuals unknown to one another to work together to create unprecedented wealth. We need to defend it as the precious value it is. In that spirit, the Competitive Enterprise Institute is proud to lead this fight for capitalism's future.

Rein in the $1.75 Trillion Regulatory State

Regulations are frequently anti-competitive and anti-consumer. They cost consumers hundreds of billions of dollars every year. Policy makers still largely do not know the full benefits and costs of their regulatory enterprise. Meanwhile, regulatory agencies grow in power and budget like feudal baronies. This situation must not go unchallenged.

From transportation to trade, from communications to banking and technology policy, policy makers of both parties have at times challenged the moral legitimacy, intellectual underpinnings, and economic rationality of federal regulatory intervention. Democrats helped spearhead transportation deregulation. Lawmakers from both parties rolled back unfunded mandates in the 1990s. The time is now ripe for a new round of reform.

There are many avenues for reform. Cost-benefit analysis, while informative, does not actually bring the largely unaccountable regulatory state under congressional control. Greater congressional accountability and cost disclosure matter most for regulatory reform.

Congress should vote on every major or controversial agency rule before it takes effect. Regulatory cost transparency, through such tools as improved annual cost and trend reporting, would help voters to better hold Congress responsible for the regulatory state. Reining in excessive delegation of power to federal agency bureaucrats would help close the breach between lawmaking and accountability, while forcing Congress to internalize the need to demonstrate regulatory benefits. Congress should:

- Establish a bipartisan Regulatory Reduction Commission to survey and purge existing rules.
- Develop a review and sunsetting schedule for new regulations and agencies.
- Explicitly approve major agency regulations with an up-or-down vote.
- Publish an annual Regulatory Report Card to accompany the federal budget.
- Require that agencies report costs (Congress itself must assess relative benefits and compare agency effectiveness).
- Have agencies and the Office of Management and Budget rank rules' effectiveness, and recommend rules for elimination.

Wayne Crews and Ryan Young

Reform Federal Agriculture Programs

With America's economy struggling to roar back to strong growth and a deficit approaching $1 trillion, policy makers need to take a hard look at reforming one of the most wasteful and egregious government programs—the 2008 Farm Bill, which expanded U.S. agriculture support programs significantly, with dire effects.

This nearly $300-billion (over five years) boondoggle paid off every special interest. Farmers got their direct payments, their counter-cyclical payments, their price support loan amounts, their disaster funds, and much more. Cities and towns got their nutrition programs and their food stamps. Environmentalists got their conservation programs, though not as many as they wanted. Energy producers got some biofuel monies.

Some producers who were not subsidized before—such as fruit, vegetable, and nut producers—received significant R&D money that opens the door to future subsidies. The bill includes what was lauded as the "first-ever livestock title" for yet another group that was not previously subsidized. And special earmarks got some others on board—the "trail to nowhere," a taxpayer-funded land swap; forests that house fish got some money, as did salmon fisheries.

And for what? Many farm subsidies go to rich farmers. The per-person annual limit for subsidy eligibility is $500,000 for non-farm income and $750,000 per year for farm income. Thus, a married couple could have farm income of $1.5 million per year and still collect taxpayer-funded payments.

The U.S. sugar program—one of the most egregious farm programs—needs drastic reform. The 2008 Farm Bill increases sugar price supports, provides incentives for using sugar for ethanol rather than food, further restricts imports of sugar, and may violate existing trade agreements.

Thus, many agricultural producers continue to enjoy subsidies and price supports, which cost taxpayers, increase food costs, and disproportionately impact low-income consumers who pay a larger percentage of their income for food. And many government agricultural programs continue to restrict imports of various products, such as sugar and ethanol. This leads to higher costs for food and fuel. This situation must change.

With the current financial crisis and recession, policy makers should immediately address ways to reduce large-scale government waste. Congress will negotiate the 2012 Farm Bill in 2011. Policy makers should take a hard look at existing farm programs that waste taxpayers' money, increase consumer costs, threaten U.S. credibility in promoting open trade, and harm developing countries' ability to compete in the world market.

Fran Smith

End Bailouts and Government Ownership in Fannie/Freddie, GM, AIG, and Other Entities

On October 3, 2010, the federal government's authority under the Troubled Asset Relief Program (TARP) officially expired. Rushed through amid fears of financial Armageddon, the thrust of the program shifted several times from buying "toxic" mortgage securities no one would touch to buying ownership stakes in order to provide a "capital cushion" to relatively healthy financial institutions—and even to propping up automakers.

Supporters are now hailing the program as a success because they claimed it calmed a panic and cost the taxpayers "only" about $50 billion. But this figure doesn't include the $700 billion that many prominent economists say the taxpayers will have to spend to rescue the government-sponsored enterprises Fannie Mae and Freddie Mac, which were put into a government conservatorship a few weeks before TARP was enacted in 2008.

While it is true that many financial institutions paid the TARP money back with interest, many never wanted to take it in the first place. They were pressured into doing so by then-Treasury Secretary Henry Paulson or bank regulators, so that the truly troubled banks would not carry the stigma of a government bailout on their own.

And it is hard to say this program program "saved" the economy, when unemployment persists at nearly 10 percent two years after it was enacted. Supporters claim that had TARP not been enacted, unemployment would have skyrocketed to 20 percent. But it is also plausible that without TARP's channeling of money toward established financial institutions considered "too big to fail" by the government, other financial institutions would have emerged to get the economy moving faster. As Stanford University economist John Taylor wrote in his book, *Getting Off Track*, TARP's passage likely "increased risks and drove the markets down."

The remaining companies under government ownership continue to damage the American economy, and the harm is not confined to the spending of taxpayer money. Firms operating with government support create a skewed playing field that disadvantages their competitors, undermining both job growth and innovation. AIG has been accused of using its $183 billion in taxpayer funds to undercut its unsubsidized competitors by slashing premiums. General Motors—now derisively known as Government Motors—has used its $50 billion in taxpayer funds to buy subprime auto lender AmeriCredit, giving it a possible competitive advantage over private-sector rivals, including Ford, Toyota, and other major automakers with plants in the U.S. And Fannie and Freddie are now virtually the only firms securitizing mortgages.

As important as recovering taxpayer money is, more important is an exit strategy to get the government out of these private firms before they can do more damage to their private-sector competitors and to the economy as a whole. Congress should:

Set firm time limits for the bailouts for Fannie Mae and Freddie Mac, General Motors, American International Group, and other bailouts and require the government's shares in companies to be sold as of a date certain. The U.S. government should not own banks or other firms. Permanent nationalization has not worked too well in places like Cuba or Venezuela in promoting stable and sustained economic growth. The fact that the government sold its first tranche of shares in GM at a considerable discount demonstrates that government ownership is bad for the company and bad for taxpayers.

Make the bailout deliberations transparent and make government-owned firms abide by the same rules as those in the private sector. Insist on open meetings whenever possible, quick compliance with the Freedom of Information Act, and judicial review of the Federal Reserve Bank and Treasury Department's actions. The initial public offering to sell part of the government's stake in General Motors disturbingly stated that the government was shielded by sovereign immunity from laws against stock fraud and securities fraud lawsuits. Congress should enact legislation waiving this sovereign immunity for the government so that investors have the same protection from fraud committed by government-owned corporations as by those in the private sector.

Respect property rights and private contracts in financial and housing policies. The government is one of many owners in the corporations participating in the TARP. It should not interfere with any firm's fiduciary duty to shareholders to deliver profits by pushing it to achieve politically determined social goals. And it should not favor some creditors over others, as it did in the GM and Chrysler bankruptcies when unions were given disproportionate equity stakes in the reorganized firms at the expense of bondholders and secured creditors.

Similarly, in trying to help families with foreclosures, the government should not require or encourage the abrogation of contracts to investors in mortgages. Congress should halt funding for President Obama's Home Affordable Modification Program, which subsidizes mortgage-servicing banks to modify a borrower's loan but disregards the interests of the investors who own the mortgages. Many of these investors are also middle-class families, holding mortgage-backed securities in their 401(k) accounts and mutual funds.

John Berlau

Free Smaller Companies to Go Public by Rolling Back Burdensome Sarbanes-Oxley Accounting Rules

In CEI's last Agenda for Congress, we recommended that "smaller public companies be exempt from Sarbanes-Oxley's Section 404." Indeed, despite the rampant fervor of the past Congress to reregulate, enough members of both parties in Congress were concerned about the impact of the Sarbox accounting rules on smaller firms that they permanently exempted firms with market valuation of $75 million or below.

This was a significant step, but Congress needs to go much further to lift Sarbox barriers to business and job growth. For new firms to expand and create more jobs, they need to be able to go public. And right now, Sarbox is one of the biggest barriers to small and midsize firms going public.

Sarbox was rushed through Congress in 2002 following the Enron and WorldCom scandals. These costly rules did virtually nothing to prevent the careless risks taken with mortgage securities that led to the financial crisis. "How can we have these levels of fictions in financials after Sarbanes-Oxley?" asked Jim Cramer, the colorful host of CNBC's "Mad Money." The answer is because Sarbanes-Oxley is actually counterproductive at ensuring financial transparency. As the *Financial Times* noted, the inordinate amount of time boards of companies such as the former Bear Stearns spend on Sarbox compliance came at the expense of their scrutinizing overall business risk.

Mid-size companies need access to equity markets. The Act's Section 404 requirement for accountants to sign off on vaguely defined "internal controls" is costing American companies $35 billion a year in direct compliance costs, according to the American Electronics Association. And it adds 35,000 extra man-hours for the average public firm, according to Financial Executives International. Congress should relieve this heavy regulatory burden by doing the following:

- **Expand the modest relief for smaller companies in the Dodd-Frank financial reform law so that more firms are exempt from Sarbanes-Oxley's Section 404 and other SEC rules that are a drag on the economy**. As seven Democratic members of the House Small Business Committee have noted, senior managers at these smaller companies "now have to choose between spending their time on vital business development functions or Section 404 compliance."
- **Repeal the "internal control" rules of Section 404 or make them voluntary**. The term "internal controls" is undefined in the statute and has been broadly defined by regulators. The Securities and Exchange Commission (SEC) has found that internal

control practices are seldom a tip-off to fraud.

- **Abolish the unaccountable Public Company Accounting Oversight Board (PCAOB) and make accounting standard setters accountable to the President and Congress.** Although the Supreme Court put some limits on the authority of the PCAOB—it made the agency subject to at-will removal by the SEC—the PCAOB still wields tremendous power without accountability. It levies taxes on all public companies, it can discipline and fine auditors, and it is responsible for the broad interpretation of Section 404's "internal control" provision. And the PCAOB wields this power without any presidential supervision and minimal SEC oversight. Congress should abolish the Board—giving authority over accounting back to the presidential appointees at the SEC, where it was before Sarbanes-Oxley.

John Berlau

Suspend Mark-to-Market Rules and Make Accounting Regulators Accountable

In CEI's last Agenda for Congress, we noted that "mark-to-market accounting—which requires financial instruments such as loans to be valued at the price of an ill-defined "market"—has been blamed by both Democrats and Republicans for spreading the credit contagion from bad banks to good." We recommended, "Congress should require regulatory agencies to suspend mark-to-market accounting mandates such as Financial Accounting Standard 157 until better guidance is developed for illiquid markets."

In the spring of 2009, Congress came pretty close to doing just that. The Financial Accounting Standards Board (FASB) was hauled before Congressional hearings and members of both parties expressed concern that FAS 157 was exacerbating the crisis by causing banks to take huge paper losses and tighten lending unnecessarily. Sensing the threat of legislation, FASB announced a relaxation of the rule, an action that sent the Dow Jones Industrial Average soaring that day to above 8,000 for the first time in months. This simple change to accounting rules led to a stabilization of the economy that billions in bailouts had failed to achieve.

But now that the legislative focus on accounting rules has faded, FASB is trying to push through an expanded mark-to-market rule that would cover virtually all bank loans. Mark-to-market mandates have generated questions about their accuracy and their economic impact. They exaggerate losses by forcing financial institutions to write down performing loans based on another institution's fire sale even if the market for such loans is highly illiquid and the financial institution in question has no plans to sell the loans.

Underlying all these problems is the fact that there are relatively few checks on the accounting standards body that makes these rules. FASB is a private body, yet Congress requires public companies to support it through a type of tax, known as an accounting support fee. Moreover, federal regulatory agencies like the Securities and Exchange Commission and the Federal Deposit Insurance Corporation almost always defer to FASB in setting standards for everything from investor reports to solvency rules.

Earlier this decade, FASB greatly limited the use of employee stock options—which are very effective at creating wealth and giving more people access to it—by requiring companies to "expense"—that is, subtract the estimated value of stock options—from current earnings, even though stock options never result in a cash outflow. This policy has had little effect on levels of executive compensation, but has caused companies to greatly reduce stock options for rank-and-file workers. It has also resulted in misleading financial reports for investors of companies that utilize stock options, as companies are required to report phantom "losses" when there has been no money leaving the firm's coffers. Congress should:

- Require regulatory agencies to suspend FASB's mark-to-market accounting mandates until better guidance is developed for illiquid markets.
- Reverse the options expensing standard.
- Hold hearings to examine FASB's process of setting accounting standards and whether the agency should continue to have a de facto monopoly on setting those standards.

John Berlau

Recognize the Value of Hedge Funds and Private Equity for Entrepreneurs and Shareholders

Hedge funds and private equity are vehicles for wealthy investors to take risks and potentially reap high returns. But the benefits of these types of funds—and of funds that combine features of both—extend beyond their investors to all entrepreneurs and shareholders. Private equity funds build wealth in distressed and startup companies. Hedge funds have forced incentivized companies to create more wealth for shareholders through streamlining—cutting costs and, when necessary, selling off divisions.

In addition, both types of funds provide liquidity and have reduced risks of disruptions to capital markets. Private equity firms have helped to ease the credit crunch by helping to recapitalize commercial banks and stepping in to fill the void of investment banks in financing new business growth. Hedge funds were ahead of the curve in short-selling subprime securities—thereby sending out valuable market information about the risks of those instruments. Cumbersome restrictions would impede their ability to perform in these vital roles. Rather than curtail these vehicles, Congress should consider how to make their benefits available to more investors, by doing the following:

- **Reject attempts to subject hedge funds and private equity to the Security and Exchange Commission's (SEC) one-size-fits-all registration process for ordinary investment vehicles.** These entities are already subject to securities fraud statutes, as well as numerous regulations from agencies, such as the Commodity Futures Trading Commission. Congress should modernize this regulatory structure to get rid of overlapping jurisdictions for more effective oversight. Since the Dodd-Frank financial reform law gave the Securities and Exchange Commission open-ended authority to require registration of some hedge funds, Congress should make sure such rules don't burden capital formation and distract the SEC from more pressing systemic threats.
- **Stop the SEC from raising the minimum income requirements for hedge fund and private equity investors.** On several occasions, the SEC has proposed raising the minimum net worth needed to invest in hedge funds from $1 million to $2.5 million. Obviously, the SEC does not need to protect "poor" millionaires. This increase will further drain the pool of capital for innovative new businesses. An attempt to codify this foolish increase was stripped from Dodd-Frank after concerns expressed by the "angel" investor community attracted bipartisan opposition. But the SEC still has the authority impose this draconian increase, and Congress

should reject any proposed rule taking such an action

- **Revise the Investment Company Act of 1940.** This would allow mutual and exchange-traded funds more freedom to pursue some of the strategies of hedge funds and private equity, such as short-selling, and give some of the hedge fund benefits to ordinary investors with minimal risk. This allows useful information to get out to the market earlier. For instance, had mutual funds had more freedom to engage in short selling during the subprime boom, the mortgage bubble likely would never have grown as large as it did.

John Berlau

Encourage Credit Access Innovation

The abuses of the subprime crisis have made it all too easy to overlook the myriad benefits of consumer credit. Innovations in mortgages, credit cards, and unsecured loans such as payday advances have made it possible for more people to borrow money they need for a variety of purposes—from starting a business to advancing one's education. In the mid-1990s, a college student named Sergey Brin used personal credit cards to start the search engine business that would become Google.

In 2007, Austan Goolsbee, now a top economic adviser to President Barack Obama, warned in *The New York Times* that, "regulators should be mindful of the potential downside in tightening too much." Such restrictions, he wrote, would hurt "someone with a low income now but who stands to earn much more in the future" with the help of access to credit.

The Obama administration and Congress have seemingly ignored this advice. The Credit Card Accountability, Responsibility and Disclosure (CARD) Act of 2009 limits card issuers' ability to raise rates and impose penalty fees on high-risk borrowers. It has limited overall credit—working against other policies aimed at getting credit flowing—and caused overall rates to rise sharply for responsible card holders who pay on time or who pay their entire balance. Rules issued by the new Consumer Financial Protection Bureau (CFPB) will likely have the similar effect of punishing the prudent with more costly credit as a result of paternalistically protecting the imprudent.

Government certainly has a role in preventing fraudulent lending practices, but it should leave payment terms and interest rates up to the interested parties to negotiate. It should also reduce the paperwork burden of traditional lending institutions that raises costs that are passed on to borrowers. It should lift the cap on business lending by credit unions and lift the moratorium on retailer-affiliated industrial lending companies to spur competition among credit providers. Congress should:

- **Reject attempts to put interest rate or price controls on credit vehicles.** Repeal most of the CARD Act and prevent the CFPB from imposing nanny-state prohibitions on innovative credit products.
- **Repeal or scale back a variety of regulations that impose myriad paperwork requirements on financial institutions**. Such regulations—from Sarbanes-Oxley provisions to the Internet gambling ban—indirectly make services more expensive to borrowers and depositors at all income levels by adding to their overall costs. These rules hit small community banks and credit unions especially hard.

- **Reduce "know your customer" requirements on banks and other financial institutions to investigate their customers' backgrounds.** These rules often overwhelm law enforcement with useless reports and have adverse impacts on the low-income "unbanked" population by making it more difficult to open a bank account.
- **Lift the cap on lending that credit unions can make to member businesses**. The cap currently stands at just 12.25 percent of a credit union's assets, keeping these institutions from competing to serve the small business lending market. The cap has only been in place since 1998, and no such cap exist for other types of loans, such as mortgages and car loans. From a safety and soundness perspective, there is nothing about business lending that is inherently more dangerous than other loans.
- **Lift the moratorium on nonfinancial businesses forming limited-purpose banks, known as Industrial Lending Companies (ILCs).** This moratorium, first imposed by the Federal Deposit Insurance Corporation and then codified for two years by the Dodd-Frank Act, has led some of the nation's most well managed firms—including Wal-Mart, Home Depot, and Berkshire Hathaway—to shelve plans to form ILCs to offer financial services to their customers. Consumers suffer from this lack of competition in the banking sector. It is laughable to argue that somehow these banks pose an inherent risk, given the risks that practices of traditional banks posed during the financial crisis.

John Berlau

Avoid Energy and Global Warming Policies that Pose Greater Risks than Global Warming

Global warming has been described as the greatest threat facing mankind, but the policies designed to address global warming actually pose a much greater threat. The international and domestic policies to ration carbon-based energy would do—and are doing—little to slow carbon dioxide (CO_2) emissions, but would have enormous costs. These costs would fall most heavily on poor people, not only in the United States, but also in the world's poorest nations. The correct approach is not energy rationing, but rather long-term technological transformation and building resiliency in developing societies by increasing their wealth.

Since the Kyoto Protocol was negotiated in 1997, atmospheric CO_2 concentrations have increased by over 5 percent. The global mean temperature peaked in 1998 and has since remained flat. Precipitate and colossally expensive measures to reduce greenhouse gas emissions are not warranted at this time—and likely never will be warranted.

Per capita carbon dioxide emissions in the United States have remained flat since 1980, according to the federal Energy Information Administration. Meanwhile, the U.S. population has increased by slightly more than 1 percent per year. Population growth means that the U.S. needs more energy, not less.

The European Union (EU) ratified the Kyoto Protocol and has implemented mandatory greenhouse gas reduction programs, but emissions in the EU-15 (the 15 member countries before the recent EU expansions) have risen considerably since Kyoto was negotiated in 1997. The EU's Emissions Trading Scheme has raised energy prices for consumers and producers, but has not lowered emissions. Gasoline taxes have been raised to $3 to $4 per gallon in most EU countries, yet emissions from transportation continue to increase.

The most thorough economic studies by leading academic economists (who are not global warming skeptics) have found that mandatory emissions reductions add to the total potential costs of global warming. For example, Yale economics professor Dr. William Nordhaus, one of the world's leading resource economists, concluded that attaining the emissions reductions advocated by former Vice President Al Gore would avert $12 trillion of the projected costs of global warming impacts, but at a cost of $34 trillion.

A cap-and-trade program would be the biggest government intrusion in the economy since the rationing system adopted during the Second World War. It would also be the biggest government limitation of, and interference with, people's personal freedoms since that war.

Rapid economic growth in major developing countries has been accompanied by rapid emissions increases. Total Chinese emissions have surpassed U.S. emissions, according to several international agencies. The Chinese government has made it clear that it will not undertake mandatory emissions reductions because it would limit the country's economic growth. Instead, China hopes to be paid by developed nations, and corporations in developed nations, to reduce its emissions.

The economic rise of China and India is lifting hundreds of millions of people out of poverty. Hundreds of millions of more people in poor countries hope to follow down a similar path. That requires much more affordable energy than can be provided by non-carbon sources, like windmills, solar panels, and nuclear plants. Any successor agreement to the Kyoto Protocol requiring emissions reductions in developing countries would consign billions of people to prolonged poverty.

Recommendations:

- Do not enact cap-and-trade legislation or a carbon tax in order to reduce greenhouse gas emissions.
- Do not enact further mandates, subsidies, or incentives for alternative energy technologies or for "green jobs" programs.
- Do not close more federal areas for energy production.
- Do not place regulatory obstacles in the way of building energy infrastructure, including transmission lines, pipelines, coal-fired power plants, nuclear plants, and windmills.
- Revoke the federal government's authority to regulate greenhouse gases.
- Reject any new international agreement to succeed the Kyoto Protocol that would require mandatory emissions reductions by the United States.
- Repeal existing mandates, subsidies, and incentives for all types of energy production, efficiency, and conservation.
- Require the Department of Interior to open federal Outer Continental Shelf areas and the coastal plain of the Arctic National Wildlife Refuge to oil and gas exploration and production.
- Replace the current depreciation schedules for investments in new capital stock and equipment with immediate expensing.

Myron Ebell

Increase Access to Energy

Economic prosperity and our standard of living depend on affordable energy. However, since the 1970s, successive Congresses have largely pursued anti-energy policies to constrict energy supplies and raise energy prices. The 112th Congress should strike out in a new direction.

Mandates and subsidies for renewable, alternative, and conventional energy technologies have done far more harm than good. Tens of billions of taxpayer dollars have been wasted on subsidies, and subsidies and mandates together have provided a disincentive for alternative technologies to become competitive. It is unlikely that wind and solar power will ever become viable means of energy production as long as they can count on continuing subsidies and mandates. Congress should:

Repeal all energy mandates and subsidies. The 2005 and 2007 ethanol mandates, coupled with the 45-cents-per-gallon refundable tax credit, have had particularly unfortunate indirect consequences. The exact contribution of the ethanol mandate to world hunger due to higher grain prices is uncertain, but still real, and quite evident in food riots around the world in recent years. The ethanol mandates should be repealed immediately. All other mandates, subsidies, and incentives—including those for conventional energy—also should be repealed. Subsidies and mandates for uncompetitive forms of energy pose grave threats to our future electricity needs. Wind and solar power can at most provide only a fraction of additional electricity demand over the next decade.

Open the nation's infrastructure to private investment. Congress should remove regulatory obstacles that are preventing private investments in new energy infrastructure. A "smart grid" will never be built until Congress changes regulations so that investors have an opportunity—but not a guarantee—to profit from the hundreds of billions of dollars of investments required.

Allow access to America's domestic energy resources. Having vowed to "never let a crisis go to waste," the Obama administration has used the BP Gulf disaster to inhibit all domestic oil and gas production. Bureaucratic procrastination has slowed permitting to a trickle in deep water, shallow water, along the Rocky Mountains, and in Alaska. Congress should vigorously investigate this de facto moratorium on all domestic oil and gas production. In addition, Congress should push the administration to put offshore federal water with high oil and gas potential up for leasing through competitive bidding. Congress also should open the coastal plain of the Arctic National Wildlife Refuge to oil and gas exploration and production, and repeal many of the administrative withdrawals of federal lands from energy production in the Rocky Mountains. Together, these actions will increase domestic oil and gas production, create hundreds of thousands of high-paying jobs, lower the trade deficit by tens of billions of dollars annually, and contribute billions of dollars in royalty payments to the federal Treasury.

Enable technological innovation. The most effective way to increase energy efficiency is to replace existing technology with new technology. One of the reasons that greenhouse gas emissions have been rising more slowly (in percentage terms) in the United States than in most European countries is more rapid technological turnover because of higher economic growth. Congress can accelerate this trend by changing the tax code to allow immediate expensing of investment in new technology instead of according to a depreciation schedule over a number of years.

Myron Ebell

End Federal Support for Renewable Energy

Eliminate mandates and subsidies for biofuels. Congressional legislation has given much unnecessary support for biofuels. The 2007 energy bill greatly expanded the Renewable Fuel Standard in the United States, requiring almost 13 billion gallons of ethanol and other renewable fuels to be blended into the gasoline supply by 2010—ramping up to 36 billion gallons by 2022. The mandate has increased the cost of driving. Meanwhile, the diversion of nearly a third of the corn supply from food to fuel use has raised food prices. The mandate comes on top of favorable tax treatment for ethanol and other biofuels, including a 45 cents-per-gallon tax credit, as well as protectionist tariffs that shield domestic corn ethanol from global competition. Few experts think that ethanol produced from corn in the United States is a scalable replacement for foreign petroleum imports. Its environmental benefits are minimal at best and come at a huge cost. Ironically, ethanol remains highly reliant on petroleum and natural gas for its production and delivery.

Do not enact a Renewable Electricity Standard and repeal renewable subsidies. As with biofuels, the very fact that wind power and other renewable sources of electricity need mandates and subsidies in order to compete indicates that they have serious limitations. In addition to being costly to produce and transmit, wind power is intermittent and thus must be backed up by conventional energy sources sufficient to carry the entire load. In nations like Denmark and Spain that have mandated renewable electricity, as well as states that have done so, the mandates have raised the cost of producing electricity and have destroyed more jobs than they have created. Congress should not follow their lead and enact a federal Renewable Electricity Standard (RES, nor should it extend existing subsidies for renewables.

The supposed greenhouse gas emissions reductions and other environmental benefits from a RES are also questionable. The backup sources of power, like coal and natural gas, have to be operated in an inefficient—and thus higher emitting—manner in order to accommodate the fickle nature of wind. Thus, the difficulties of integrating wind into the larger electricity system make it both an economic and environmental disappointment—two good reasons for Washington to let the marketplace decide how to generate electricity. Congress should:

- Cap the Renewable Fuels Standard at 2010 levels or remove it completely.
- End biofuel subsidies.
- Refrain from enacting a federal Renewable Electricity Standard.
- Repeal subsidies for wind, solar, and other renewable sources of electricity.

Ben Lieberman

Oppose Efforts to Impose Pro-Organized Labor Rules through Regulation

One of the American economy's greatest strengths is individuals' and businesses' ability to adapt to changing conditions. However, in the case of labor markets, many workers and employers remain subject to an array of obsolete New Deal-era labor regulations that discourage innovation and hamper flexibility. The old adversarial model of labor relations has little to offer to the 21st century workforce, which is characterized by horizontal company structures and greater job mobility—flexibility which employers and workers need to better ride out economic downturns.

The collective bargaining model that has predominated in the U.S. since the New Deal, when 1935 the National Labor Relations Act (NLRA) was enacted, has been one based on compulsory monopoly representation. Under this system, when employees at a given workplace vote on whether they want to be represented by a union, that union becomes the exclusive bargaining agents for all the workers there—including workers who did not vote to be represented by the union.

This violates workers' First Amendment rights to freedom of association and freedom of speech—by forcing them to join unions as a precondition of employment and to support political activity with which they may not agree through the compulsory payment of union dues. Abolishing unions' monopoly bargaining privilege, which is codified in the NLRA would end this anachronistic system.

Meanwhile, Congress should resist measures that would make the situation worse, such as the misleadingly named Employee Free Choice Act (EFCA), which would allow unions to circumvent secret ballot elections through "card check organizing, enjoin a federally appointed arbitrator to impose a contract on a newly unionized companies if the union and management do not reach an agreement after 120 days, and increase employer penalties for "unfair labor practices," which would give unions another blunt instrument with which to pressure employers.

Having failed to enact EFCA into law, organized labor and the Obama administration have indicated a willingness to make an end run around Congress by imposing some of EFCA's provisions through the regulatory process, mainly through the National Labor Relations Board (NLRB).

The NLRB is now considering allowing remote electronic voting (E-Voting), which would allow unions to conduct organizing elections via phone or the Internet. The NLRB says it wants to keep the voting secret but it would not be hard for a union organizer using a laptop computer or some other mobile device to pressure an individual worker to vote for the union. Allegations of mail fraud and voter intimidation were rampant in a 2009 mail election fight in California. E-Voting could lead to similar intimidation and fraud.

The NLRB is also considering expedited elections, which essentially would function as ambush elections. Employers would have very little time to respond to union organizing campaigns, thus giving the union a significant advantage.

In addition, the NLRB has decided to revisit its 2007 *Dana Corp.* decision, which affirmed employees' right to call for a secret-ballot decertification election in instances where a union has been certified through card check.

Congress should resist any efforts to impose parts of EFCA, or other rules that tilt the playing field in favor of unions against employers.

Ivan Osorio and F. Vincent Vernuccio

Eliminate Wage Ceilings for Unionized Workers

Workers need incentives to perform to their utmost capability. Working hard and performing your job well is usually rewarded with greater compensation. Unfortunately, this is not the case at many unionized workplaces, where collective bargaining agreements impose a wage ceiling, in addition to a wage floor. The vast majority of these agreements grant pay increases based on seniority rather than merit.

The National Labor Relations Board and the courts have held that employers with collective bargaining agreements can only deal with a union and not with an individual employee. This means in most cases an employer cannot reward a union employee for being more productive without violating the National Labor Relations Act (NLRA).

The Rewarding Achievement and Incentivizing Successful Employees (RAISE) Act, sponsored in the 111th Congress by Rep. Tom McClintock (R-Calif.) and Sen. David Vitter (R-La.), would amend the NLRA to allow employers to pay especially productive workers more than the base amount set in the union's collective bargaining agreement. If the RAISE Act becomes law, union workers' earnings could rise by between \$2,600 and \$4,300 per year, according to an estimate by Heritage Foundation labor expert James Sherk. This is a common sense idea that is long overdue.

Ivan Osorio and F. Vincent Vernuccio

Oppose Taxpayer Bailouts of Underfunded Union Pension Funds

In trying to attract new members, labor unions often tout the promise of a secure retirement to their members in the form of defined benefit pensions. However, many union pension plans today are severely underfunded. Some have been in trouble for years, and the latest economic downturn has only exasperated the problem. In 2008, the Department of Labor listed the status of 230 union plans as either endangered—less than 80 percent funded—or critical—less than 65 percent funded. In 2009, Moody's Investors Service estimated all union pensions to be underfunded by $165 billion.

As a result, one of organized labor's top policy priorities is to get taxpayers to bail out these severely underfunded union pension plans. In the 111th Congress, this effort took the form of the Create Jobs and Save Benefits Act, introduced in the House by Rep. Earl Pomeroy (D-N.D.) and in the Senate by Rep. Robert Casey (D-Penn.). The Pomeroy-Casey bailout bill would create a new fund within the Pension Benefit Guaranty Corporation (PBGC), an agency chartered by Congress that insures private sector pensions.

The PBGC is funded through premiums paid by private employers to insure retirees if a plan sponsor were to become insolvent. The Pomeroy-Casey legislation would direct taxpayer dollars to shore up some underfunded union pension plans. It would create a new fund to the PBGC, known as the "fifth" fund, whose obligations would be "obligations of the United States"—that is, taxpayers. The use of public funds to insure private pension plans is a first for PBGC and stark departure from the way it has operated since its creation in 1974.

Earl Pomeroy lost his reelection bid, but just because unions lost one champion of this legislation does not mean they cannot find another in the incoming Congress. Pomeroy was an odd sponsor of such legislation anyway—unions are not exactly political powerhouses in North Dakota. Still, given enough support from the national Big Labor establishment, another unlikely lawmaker could take this up. Members of Congress who are serious about reining in spending and protecting taxpayers should oppose any revival of this legislation.

Ivan Osorio and F. Vincent Vernuccio

Resist Forced Unionization of Public Safety Personnel

Today, for the first time in American history, a majority of union of union members work for governments. In January 2009, the Bureau of Labor Statistics reported that the number of union members working for government entities surpassed the number of those working for private businesses. This change in the composition of organized labor's membership is significant for the nation's politics.

As unions have become increasingly government employee-based, public sector unions have become an organized, motivated, and well-funded permanent lobby for bigger government. With the federal and state and local governments facing tightened finances, lawmakers must confront this lobby. The first thing they must do is to not feed it.

The so-called Public Safety Employer-Employee Cooperation Act, sponsored in the 111th Congress by Rep. Dale Kildee (D-Mich.) and Sen. Harry Reid (D-Nev.), would indeed feed this behemoth. The bill would have imposed union collective bargaining on state and local public safety—police, firefighter, and EMT—personnel. For states and cities struggling to balance their overstretched budgets, higher labor costs are the last thing they need.

Moreover, such legislation would violate workers' First Amendment rights to freedom of association and freedom of speech by forcing them to join unions and to support, through the compulsory payment of union dues, political activity with which they may not agree.

The Kildee-Reid legislation instructs the Federal Labor Relations Authority, which oversees collective bargaining for non-postal federal employees, to promulgate union representation and collective bargaining regulations for state and local public safety employees in states which have not enacted laws giving unions those privileges. Such legislation, by increasing state and local governments' labor costs, would amount to unfunded mandates upon states, counties, and cities. It is terrible policy. Congress should reject any attempt to revive it.

Ivan Osorio and F. Vincent Vernuccio

Resist Anti-Consumer Antitrust Regulation

Before the recent financial collapse and the massive increase in economic regulation, policy makers were often willing to question the presumption that governmental economic regulation benefits consumers. Over several decades, that pro-competitive mindset helped drive the liberalization of transportation, telecommunications, banking, electricity, and several other sectors. In market after market, consumers reaped the enormous benefits of deregulation as prices fell and competition flourished.

Antitrust regulation, however, continues to enjoy broad support among the business community, in the popular press, and among policy makers. Despite its popularity, antitrust constitutes a serious hazard for successful, wealth-creating businesses, and it threatens to disrupt innovation and economic growth. Recent targets of misguided antitrust interventions—or, in some cases, mere *threats* of intervention—have included Microsoft, Intel, IBM, Google, and the Sirius/XM Satellite Radio merger. These innovative firms have been stopped in their tracks by government regulators for allegedly threatening competition. But as a growing body of economic evidence has demonstrated, mergers, acquisitions, and single-firm behavior—no matter the size or market power of the firm in question—tend to benefit, rather than hinder, competition and innovation. Even when big companies misbehave, they do not act in a vacuum. Providing the necessary competitive responses to successful firms is exactly what markets are for.

Antitrust enforcement and the resulting uncertainties scuttle innovative new product offerings, preclude efficient market arrangements, and thwart the natural evolution of the marketplace and competition itself. The availability of antitrust as a competitive weapon frequently attracts firms seeking entry or price regulation as a means of hobbling more nimble rivals. Persuading antitrust enforcers to penalize successful competitors undermines competition, ultimately harming consumers by driving prices higher and output lower. Antitrust regulation destabilizes the very industries it purports to foster by depriving consumers of competitive marketplace responses to aggressive firms.

Resisting such interventions—whether against “collusion,” “predatory pricing,” or “vertical integration”—should be a top priority for policy makers in today’s competitive, dynamic, global marketplace.

Wayne Crews and Ryan Radia

Regulate Government Data Collection While Avoiding Prescriptive Privacy Regulation

There are two notable ironies in proposals by politicians and self-styled consumer advocates to protect consumer privacy by regulating businesses that handle sensitive personal data. First, the most egregious privacy violations are typically perpetrated not by firms, but by governments against their own citizens. Second, those violations of privacy that do result from business and consumer transactions are often facilitated by government.

The laws safeguarding individuals and businesses from unwarranted law enforcement access to sensitive information stored in the "cloud" (remote Internet-based servers operated by third parties) are woefully outdated. Today, government can compel service providers to disclose the contents of many kinds of private correspondence without first obtaining a search warrant or any other court order authorized by a judge. Lawmakers should revise U.S. electronic privacy statutes to better reflect the realities of the information age by applying robust protections to the contents of all private communications stored electronically.

Government routinely collects and stores individuals' personal information, including Social Security numbers, names, and birth dates—the holy trinity for identity thieves. In some cases, government has even promoted the use of these identifiers by financial and medical institutions. In the name of homeland security, some lawmakers hope to require citizens to disclose even more information that would be stored in federal databases. Some policy makers have proposed mandatory biometric national identification cards. Yet the real key to safeguarding our privacy is to grant government less access to ever more personal information, not more.

Federal efforts to regulate private sector privacy standards are fundamentally misguided. One-size-fits-all regulations that purport to increase privacy and security invariably have serious downsides. In many cases, privacy regulation actually renders sensitive information even more vulnerable. Evolving digital devices and telecommunications technologies are constantly creating new privacy and security concerns that cannot be properly addressed by static laws enforced by distant bureaucrats. The appropriate level of privacy and data security varies dramatically depending on the type of information in question and on the needs of every specific individual. No two consumers share the same set of privacy preferences. Flexible, voluntary private arrangements, bolstered by the competitive process, are the best means of effectively balancing privacy concerns against other vital interests as the information age evolves.

Technologies that enable users to safeguard their privacy on an individualized basis are constantly improving. The perennial gale of competitive discipline continuously encourages businesses to devise better solutions to tough privacy problems. Federal regulation cannot anticipate or properly address the ever-changing threats to digital information. Legislative or regulatory mandates on data security are more likely to stifle innovation and ossify technology standard than to truly protect our privacy.

Consumers today demand both security and functionality in online commerce and communication. As the public grows more cognizant of privacy risks, market institutions evolve to create more robust and diverse privacy standards. These institutions—including insurance companies, reputational forces, and third-party watchdog groups—are all equipped to punish wrongdoers and incentivize smart privacy practices. And when private agreements are broken, government has an important role to play in allowing injured parties to obtain recourse through the judicial system.

Wayne Crews and Ryan Radia

Forge a Bipartisan Approach to End Corporate Welfare

One of government's primary current undertakings is transferring wealth. Many such transfers are from taxpayers to corporations. Before the financial crisis and recession, these transfers were called corporate welfare. Now they are called stimulus, bailouts, or infrastructure investments. But a rose by any other name has thorns just as sharp. The money for these wealth transfers must come from somewhere. If current taxpayers do not pay the costs for such boondoggles, future taxpayers will.

Direct payments are not the only transfer mechanism. Price, entry, and antitrust regulations benefit politically favored firms at the expense of consumers and competitors that happen to be less politically connected. Even innocuous-sounding health and safety regulations can benefit some firms at competitors' expense.

Corporate welfare, whether in the form of subsidies or competitor-hampering regulations, creates distortions and inefficiencies, injures consumers, and undermines the evolving, competitive market process. Congress should keep a watchful eye on the businesses that set up lobbying shops in Washington, D.C. Are they seeking to reduce burdens on entrepreneurship and employment, or do they seek to add burdens that benefit them at the expense of competitors?

Entry barriers hit smaller companies especially hard. Additional costs that a large company can absorb can cripple its smaller competitors. Congress should be skeptical toward any appeals for political favors, which all too often come under the guise of consumer welfare.

Wayne Crews and Ryan Young

Develop Smart Policies to Help Homeowners Deal with Natural Catastrophes

Natural catastrophes such as hurricanes, forest fires, earthquakes, and severe blizzards threaten nearly every state in the Union. Each year, such catastrophes impose billions of dollars' worth of costs on taxpayers, insurers, and governments; claim scores of lives; and destroy thousands of homes. Congress should:

- **Avoid policies that encourage unwise building.** Lawmakers in both the House and Senate continue to introduce measures in an attempt to add wind coverage to the National Flood Insurance Program and establish an implicitly government-backed entity to reduce reinsurance prices. Neither measure has much promise for providing coverage that would actually cost less than that in the private market. Instead, both would encourage development where it should not occur while sticking taxpayers with the bill. Thus far, none of the measures have made it far in the legislative process, but efforts are likely to reappear in future sessions. Congress should reject any measure that could involve the federal government in the insurance or reinsurance business in disaster-prone regions.
- **Help states decontrol homeowners' insurance rates.** States—not the federal government—perform nearly all oversight of homeowners' insurance rates. In the long term, federal policy should encourage states to let insurers charge risk-based rates that take all relevant risk factors into account. Many state insurance bureaucracies suppress rates in order to cater to homeowners who live in unsafe areas—often simultaneously raising rates for those who live in safer areas. The federal government should offer tax credits over a phase-out period to homeowners in states that act properly and allow rates to rise. This would temporarily offset higher insurance premiums and allow homeowners to secure their homes against natural disasters. The tax credits should expire with the program.
- **Allow private insurers to reserve against catastrophes without paying taxes up front.** Current U.S. tax law makes it difficult for insurers and reinsurers to build up reserves against catastrophes. Larger reserves could make reinsurance more affordable. The United States should implement laws similar to those in Switzerland, Bermuda, and elsewhere that make it possible for insurers to build up "catastrophic" reserves. Money in these reserves could be held tax-free until spent to pay claims stemming from a major catastrophe.

Michelle Minton

Liberalize Homeowners', Automobile, Life, and Commercial Insurance Regulation

Currently, insurance in the United States is governed by a patchwork of regulations. Some states have more cumbersome and confusing rules than others. This hampers innovation, raises insurance rates for those who behave prudently, and needlessly expands government bureaucracy. In the realms of homeowners', automobile, and life insurance—the types of insurance that most Americans buy for themselves—the United States needs a national insurance market that leaves rate regulation to market forces. Two major options exist for creating such a market.

Interstate insurance choice. Allowing state-regulated insurers to operate across state lines under the laws of their home state could yield many positive consequences without the need to create a new federal agency to administer it.

State-level liberalization. The second option requires only that Congress stay out of the way of states wishing to improve and harmonize their laws to the point that insurers and consumers have the benefits of a national market for insurance. All 50 states have enacted some form of the Uniform Commercial Code as a way of dealing with transactions of personal—that is, moveable—property. Thus, a sufficiently liberal uniform insurance regulatory law could also accomplish many of the purposes that a national regulatory regime for insurance would create without bringing the federal government into the business of insurance regulation.

Michelle Minton

Phase Out the National Flood Insurance Program

Since it emerged in its current form in 1973, the National Flood Insurance Program (NFIP) has done little to meet its supposed purpose of protecting the nation from flood damage. Instead, it has encouraged development in flood-prone areas, endangered lives, and damaged the environment by suppressing rates and failing to mitigate repeatedly damaged properties in high-risk floodplain areas. Moreover, the program's existence has impeded the emergence of private flood insurance and imposed billions of dollars in costs. As of 2010, the program was deeply in debt to the U.S. Treasury and asking for a bailout of nearly $20 billion. Partial privatization of the program would require three steps: improved flood mapping, rate changes, and a free market auction of policies within the current program.

Improved flood mapping. Writing flood insurance coverage requires complex rate maps that make probabilistic determinations of the risk of flooding in various areas. The current maps that underlie the flood program are out of date and, despite hundreds of millions of dollars spent modernizing them, still are not very good. Good maps would make it possible for private companies to write practical, affordable insurance on a large scale. Because flooding involves so many unknowns, it makes the most sense to allow multiple players to develop flood maps in a competitive market.

Rate adjustment. New improved maps would allow companies that want to write flood policies to adjust rates to make them accurately reflect the risk involved. Some rates would go up based on new data while others would fall. In time, a large portion of the NFIP flood policies could be taken over by private insurers.

Auction of remaining NFIP policies. Following a period under this quasi-private system, the National Flood Insurance Program could auction off its remaining portfolio of policies. Certain high-risk areas likely would be rendered not insurable at rates that would offer any real value to those purchasing insurance, which would discourage building in the highest risk areas—a desirable outcome in terms of both costs and safety.

Michelle Minton

Let Market Forces Regulate Internet Gambling

In June 2010, the 2006 Unlawful Internet Gambling Enforcement Act (UIGEA) was implemented after years of delays. The law regulates banking and credit processes related to online gambling. This does nothing to protect Americans from crime. Instead, it increases the regulatory burden on American banks and obscures the legality of Internet gambling in the United States. Other federal laws, including the Wire Act (which bans interstate wagering) and the Professional and Amateur Sports Protection Act (which bans most states from sports gambling), prevent Americans from operating within the law.

People enjoy gambling and can legally do so in 48 states. Regardless of its legality, Americans gamble for money online and will continue to do so. Banning the activity or making licensing prohibitively difficult will simply encourage gamblers to play on foreign sites and take greater risks. In a country where gambling has become a respected, mainstream pastime, these laws make no sense.

Online gambling of all kinds should be legalized. Letting the free market regulate Internet gambling will result in the best outcome for gamers, Internet casino owners, and payment processing companies. Governments should enforce existing contract and criminal laws against force and fraud. Companies based in the United States and income earned by players should be treated by the U.S. tax code like income from any other lawful endeavor.

Because gambling is essentially an entertainment activity where participants enjoy the possibility of profit, there is no reason to assume that private market oversight or certification programs would be insufficient. Like cruise ship casinos, which voluntarily abide by specific regulations and agree to audits of their operations. Internet casinos could submit to review by a regulator. Inevitably, competition among private auditors would result in greater oversight than one federal watchdog. Auditors could offer a certificate or rating to guide consumers to the sites at which they are most likely to have fair play.

Michelle Minton

Allow Immigrants Full Access to the American Economy

As with the free movement of goods and services across borders, the legally unencumbered movement of people reaps net benefits for all parties concerned. Congress should enhance the benefits of immigration by implementing less restrictive immigration laws, with the ultimate goal of an immigration system that lets non-criminal, non-terrorist, and healthy immigrants from anywhere in the world move to the United States.

Government should have no more control over the flow of people across borders than the flow of capital, goods, and services. Only an unfettered free market in laborers and entrepreneurs can operate without distorting the economy. As in all other areas of the economy, price signals, opportunity and transactions costs, and the interplay of other economic forces will determine the number and quality of immigrants.

The standard argument in favor of our current restrictive immigration laws—that such laws are necessary for security and to protect American workers from an influx of cheap foreign competition—do not hold up to scrutiny. Immigration critics charge that immigrants, regardless of lawful status, depress the wages of American workers. At the most, this is true for a small subset of the American population that competes directly with foreign labor. But for the vast majority of Americans, freer immigration would result in an increase in their wages and returns on investments. This is because the skills immigrants possess tend to complement the skills of American workers. Except in the most menial of jobs, immigrant and American workers are rarely substitutes for each other.

Immigrants are also entrepreneurial. According to the Kauffman Foundation, immigrants are 60 percent more likely to be self-employed than native-born Americans. The benefits of immigrant entrepreneurship spill over into the rest of the American economy, creating employment opportunities for Americans and greater profits for many American service industries, like accounting, financial services, and the legal professions. Failure to reform America's immigration policy risks denying entrance to entrepreneurs like Google co-founder Sergey Brin, who came to the U.S. from the Soviet Union as a child.

Congress should free immigration authorities to focus on security. America's immigration authorities are stretched thin raiding workplaces, checking permits, and screening clearly non-violent people for entrance. Congress should move the immigration system away from work permits and back toward a system that only excludes criminals, terrorists, or those carrying serious, deadly, and highly contagious diseases. In the meantime, Congress should:

- Lift all quotas for work visas.
- Allow employees, rather than employers, to hold work visas.
- Allow visa holders to change jobs without government approval.
- Allow visas to be issued for an unlimited period of time, subject to revocation if the visa holder commits a serious felony.

Alex Nowrasteh

Protect Federalism

The Framers of the Constitution intended federalism to act as a check not only on the national government, but on state governments as well. In addition to the relatively well-known limits on Congress, the Constitution imposes a number of limitations on the states. For example, the Compact Clause (Article I, Section 10) prohibits states from entering into agreements with other states without congressional approval. This was intended to restrict the ability of groups of states to gang up on other states or on the federal government.

But the constitutional restraints on both the federal government and on the states have been severely weakened. Quite clearly, there has been a growing federal intrusion into state and local issues, epitomized by ObamaCare's massive imposition of new obligations on states.

Less obviously, states themselves have begun to create a new level of national regulation through state attorneys general (AGs) acting in concert. In areas ranging from financial regulation and tobacco control to global warming and fuel economy mandates, state attorneys general are entering into new alliances aimed at imposing national regulatory schemes via litigation. These joint litigation campaigns are often fueled by lucrative deals between state AGs and private lawyers, and many states join simply because such lawsuits have the potential to generate huge sums of money. Under the Constitution, such joint campaigns by the states require advance congressional approval. Congress should actively review them, rather than sit on the sidelines while state officials impose new national regulations by default.

Sam Kazman

Avoid Hindering the Internet's Evolution through Net Neutrality Regulation

In 2010, Congress failed to enact legislation authorizing the Federal Communications Commission (FCC) to enforce network neutrality rules. In 2011, Congress is widely expected to again take up net neutrality, a policy that would make it illegal for broadband providers to "unreasonably" discriminate among different kinds of Internet traffic. Net neutrality regulations would obstruct beneficial market arrangements for distributing digital content. Worse, they would stifle infrastructure wealth creation in network industries by undermining property rights and turning market contests over network pricing and access disputes into political battles.

Advocates of neutrality regulation argue that is necessary to prevent Internet service providers (ISPs) from either censoring or degrading certain kinds of traffic. However, neither of these concerns justifies federal regulation of Internet providers.

- **Censorship.** Many consumers do not believe that Internet service providers and other network operators, like wireless telephone carriers, should be in the business of judging the appropriateness of lawful network traffic. But not all consumers oppose filtering at the network level, which can be a valuable tool for safeguarding children from inappropriate content, for example. Broadband providers will not be able to satisfy their users' diverse preferences, if network filtering is regulated by the federal government—whether in the form of an outright ban on filtering or a requirement that providers filter certain types of content. If broadband providers engage in overbroad filtering, they will face consumer backlash and competitive responses. In recent years, a handful of providers—including Verizon Wireless, T-Mobile, and Cox—have dabbled with content filtering. In each instance, popular opposition has been swift and fierce. Like all firms competing in a marketplace, broadband companies care about their reputation. Unreasonably blocking lawful content that users desire is a surefire way to lose friends and make enemies. Firms will make mistakes from time to time, but this trial-and-error process is the only effective method of ensuring that consumers' evolving preferences are satisfied in the long run.
- **Network Management.** Perhaps the most contentious question in the neutrality debate is how network traffic should be managed. Proponents of neutrality regulation believe that Internet providers should be required to obtain the federal government's blessing before engaging in any network management technique that involves the

prioritization of certain types of traffic. This approach would chill innovation and make complex business judgments contingent on the whims of bureaucrats. While courts should enforce the contractual arrangements (terms of service) between broadband companies and their subscribers, neither content providers nor federal regulators should be empowered to coercively dictate broadband network management. In April 2010, a federal appeals court ruled that the FCC lacks the authority to regulate Internet providers' network management practices. However, the FCC remains undeterred and now is considering a new regulatory approach aimed at empowering the agency to regulate broadband networks. As a result, broadband providers have little incentive to adopt novel pro-consumer network management techniques for fear of government intervention.

The win-win scenarios made possible by emerging network structures will ultimately render neutrality proposals obsolete. Many of the major companies that once supported neutrality regulation—Microsoft, Yahoo!, Amazon, and Google—have changed their tune, and are increasingly working alongside broadband providers, and, in some cases, negotiating non-neutral arrangements for delivering their content to end users through techniques such as "edge caching" (distributing content away from a central server to servers closer to the end user). Even several prominent net neutrality advocates, such as Harvard Professor Lawrence Lessig, acknowledge that, "there are good reasons to be able to prioritize traffic."

Congress should resist calls to grant the FCC authority to enforce net neutrality rules. Regulating the broadband market will make it less competitive. In addition, creating a new regulatory regime to address elusive harms would lead to harmful consequences down the road. Net neutrality rules would invariably fail to keep pace with ever-changing technologies. As networks evolve and new technologies emerge, boundaries between "reasonable" and "unreasonable" network management will continuously shift. Consumers will vote with their wallets—if providers cross the line, subscribers will simply go elsewhere. Policy makers should focus first and foremost on how to expand consumer choice in broadband. Liberalizing the airwaves and telecommunications will help stimulate competition in the broadband marketplace.

Wayne Crews, Ryan Radia, and CEI Staff

Protect Free Speech by Rejecting Content Regulation

In recent years, the First Amendment's protections have been increasingly extended to commercial speech, such as product advertisements and even political messages. However, significant gaps in these protections still exist. Many states have attempted to regulate the content of video games in recent years, while federal regulations on drug and medical device advertisements inhibit individuals' ability to learn about well-documented scientific findings.

As new technologies provide an ever-growing array of media, Congress will face increasing pressure to impose content regulations—including regulations on video games, blogs, and social networking websites such as Facebook. As portable devices such as iPods and cell phones become increasingly equipped for video and multimedia playback, regulation advocates will push for laws governing what can and cannot be viewed in public areas, under the guise of protecting children from harmful material. Such regulations should be avoided. Parents, not government regulators, are best equipped to determine what content is appropriate for their children. Moreover, all such regulatory ventures pose a threat to free speech. Regulations aimed at protecting children from "inappropriate" content often have a chilling effect on adult speech as well.

Ryan Radia and Wayne Crews

Advance a Global Pro-Trade Agenda

Increasing liberalization of world trade is a key factor behind the dramatic increase in global prosperity since the 1950s. However, in recent years, free trade and globalization have come under assault from populist politicians. This demagogy has led to some costly real-world consequences. Free trade agreements (FTAs) with friendly nations negotiated years ago remain stalled by Congress. Some lawmakers decry China's currency "manipulation" as an unfair subsidy and seek to impose retaliatory duties on Chinese imports, even though lower prices on Chinese goods benefit American consumers. And internationally, the World Trade Organization's (WTO) Doha Round remains stalled due to rich countries' reluctance to reduce their extensive agricultural support programs, which distort the world market and harm developing countries' ability to compete.

The progress that more open trade can bring is increasingly threatened by efforts to insert environmental and labor standards into trade agreements, which function as a form of disguised protectionism. Imposing American- or European-level environmental and labor standards on developing countries would deprive poor people of jobs and harm the environment in those countries by undermining their economies' varying competitive advantages. There is also a more recent push to introduce carbon border taxes to penalize countries that have not taken steps to enact Kyoto Protocol–like regimes. Yet increasing wealth—via liberalized trade—is a key to raising both labor standards and environmental protection in the developing world.

Some constituencies seek this disguised protectionism. In the United States, organized labor would like to restrict labor market competition for its members by thwarting international trade liberalization as well as bilateral trade negotiations. Environmentalists likewise would like to "export" U.S. environmental mandates to poor countries.

In addition to its economic benefits, trade liberalization can help improve relations with neighbors, allies, and emerging nations. Congress should approve pending bilateral trade agreements with Colombia, Panama, and South Korea. These free trade agreements were negotiated years ago, and all three countries are U.S. allies. The U.S.-Korea FTA has been endorsed by the Obama administration, but its implementing legislation has to be approved by Congress. That agreement would not only be an economic boon to both countries, but would strengthen political ties with one of the U.S.'s staunchest allies in East Asia.If closer ties with trading partners are not negotiated, the U.S. stands to lose out on increased economic growth through trade.

More open trade greatly benefits consumers. Too often, consumers have been neglected in the mercantilist assumptions that frame most trade debates: “Exports good, imports bad.”

Since the end of the Second World War, American presidents and majorities in Congress from both parties have consistently pursued trade liberalization as a key American interest. The Obama administration and the new Congress should resist calls for divisive and misguided protectionist measures that would harm our fragile economy and isolate the U.S. from its international interests.

Fran Smith

Counteract Politicization of Federal Science Policy

The federal politicization of science in many areas is harming science itself. Ethics rules and advisory panel guidelines are imposing significant restrictions on scientists' involvement with for-profit entities, thereby freezing commercial interests out of the science policy debate and in effect isolating the market from the marketplace of ideas. With industry R&D investment now double federal funding for the same, this is a significant problem.

Moreover, government patronage today threatens to distort science in several areas. We have seen stark evidence of this in the Climategate scandal, where a clique of scientists who were recipients of large amounts of federal science funding, even some based overseas, conspired to ensure their interpretation of science remained the dominant one to the exclusion of those outside the system. If science is to be insulated from the risks associated with patronage, a new, innovative system of federal funding needs to be adopted. One option is the replacement of the current grant system with one based on prizes, lotteries, and loans—a system that would reduce the influence of the politician and grant officer and increase the freedom of the scientist.

Iain Murray

Resist New Burdens on the Transportation Sector

The transportation industries—airline, railroad, shipping, and trucking—are networks involving both a flow and a grid. The flow element relates to what is being transported—such as airplanes and trains—and the grid is the physical infrastructure used to manage the flow—such as airports and air traffic control. Some transportation industries have been freed of extensive federal regulation over both elements, including railroads and trucking. However, air travel had only its flow element—the airlines—economically liberalized under the 1978 Airline Deregulation Act.

The Federal Aviation Administration remains a command-and-control government agency that poorly manages air transport infrastructure to the detriment of consumers. Air traffic control services should be privatized, and landing slots and airport space should be allocated using market prices and new technology rather than through administrative fiat.

As air travel is a global industry, the U.S. must continue to open up international markets, especially by implementing a genuine "open skies" agreement with the European Union, and remove laws that restrict foreign investment in American airline companies.

Encourage private investment in freight rail. Attempts to roll back the successful 1980 Staggers Act and reregulate America's freight railroads must be resisted. The Staggers Act has enabled a genuine market to operate in which the railroads are finally able to make a sustainable rate of return and invest in badly needed new infrastructure. Re-regulation would suffocate new infrastructure investment and lead to greater highway congestion. Rail also suffers in that its main infrastructural competition—the nation's highway system— is government-owned. Congress should consider tax reforms to make it easier to invest in rail infrastructure.

Privatize passenger rail. Amtrak is an inefficient waste of taxpayer money. Congress should pursue privatization of Amtrak's routes and infrastructure, through such preliminary reforms as breaking up the network. Competition in passenger rail choices can only benefit travelers.

Liberalize air travel. Congress should reject attempts to tax airlines on environmental grounds, which would be extremely harmful to the industry. Congress should also revise, or repeal, outdated rules that forbid industry consolidation or foreign ownership. Privatization and modernization of the air traffic control system would allow faster flights, reduce delays at airports, save up to 400,000 barrels of oil per day, and reduce greenhouse gas emissions accordingly. There is no need to reinvent the wheel. Canada's successful air traffic control privatization offers a useful model.

Move to a risk-based transportation security model. According to experts, the long lines at airports since the increase in general security following 9/11 cost the U.S. economy $8 billion a year, and divert passengers onto the roads, with a significant increase in road traffic deaths as a result. Yet most of this security effort is wasted, aimed at people who could not possibly pose a security risk. To speed up lines and thereby remove this barrier to air travel, policy-makers should allow private firms to compete with the Transportation Security Administration, introduce a risk-based security model that allows low-risk passengers to move more quickly through the system, and permit a Registered Traveler scheme for those willing to subject themselves to extra security clearance in order to allow business travelers expedited travel.

Iain Murray

Put Mobility First in Surface Transportation

Surface transportation policy has become less rational and more ideological in recent decades. Environmentalists, urban planners, and their allies have succeeded in diverting resources from expanding highway capacity to mass transit, even as road congestion has dramatically increased. Highway user-generated tax revenues are being diverted to fund mass transit, while transportation planners are choking off needed highway infrastructure upgrades by supporting politically favored but economically inefficient programs at the state and local levels.

When the Highway Trust Fund's Highway Account was depleted in 2008, William W. Millar of the American Public Transportation Association ironically claimed a proposal from the Bush administration to loan the Highway Account funds from the Mass Transit Account was akin to "robbing Peter to pay Paul." He got this backwards. In fact, mass transit subsidies largely rely on robbing Peter the driver to pay for Paul's train ticket. Congress should seek to enhance mobility by doing the following:

- **Eliminate the Highway Trust Fund's Mass Transit Account.** The Highway Trust Fund was established to fund highway maintenance and expansion. It captures revenue from excise taxes on products such as gasoline and diesel—in other words, from users of the highway system. The Mass Transit Account receives more than 15 percent of gasoline tax revenue (some in Congress propose increasing this to 20 percent), which subsidizes mass transit capital investment and users in the form of artificially low fares. If there is to be a Highway Trust Fund, revenue should be dedicated to projects that benefit those who pay the excise taxes to fund it.
- **Allow "free" highways to be converted to turnpikes.** Currently, 23 USC 129 prohibits the federal funding of turnpikes on the Interstate system, both construction and conversion. Striking subparagraph (a)(1)(D) would permit Interstate "free-road" conversion to toll roads, allow for fairer and more efficient user-generated revenue, and permit more innovative private-sector involvement in financing and management. Congress should consider a longer-term phase-in period of tolled Interstate highway segments and the phase-out of "free" roads and the Highway Trust Fund. In addition, Congress should encourage the development of high-occupancy toll (HOT) lanes, rather than unpriced high-occupancy vehicle (HOV) lanes.
- **Promote highway concessions and divestitures.** As states across the country continue to struggle with meeting their balanced-budget requirements, easing their trans-

portation expenditure burdens through private-sector involvement should be welcomed and promoted. Congress should allow the Federal Highway Administration to greatly expand the SEP-15 program, which permits the FHWA administrator to waive project compliance obligations under Title 23 on a case-by-case basis, as well as vigorously promote the potential benefits to state transportation authorities. Several states have already implemented innovative public-private partnerships through the SEP-15 process, which has saved taxpayers billions of dollars.

Marc Scribner

Reform the Transportation Security Administration

Reform of the Transportation Security Administration (TSA) is long overdue—as the recent passenger backlash against both the TSA's new backscatter full body scanners and the enhanced pat-downs for those who opt out of the machines suggests. These new measures merely attempt to "fight the last war" rather than genuinely increase security for flyers. Meanwhile long lines at airports impose a significant economic cost on the nation and force some people on to the roads, where they are more likely to die in traffic accidents. Racial profiling, which some have suggested, is not the answer, as it is far too blunt a tool to provide genuinely increased security.

Instead, the TSA should be reformed to allow more flexibility and to introduce risk-based security into passenger flights. A comprehensive TSA reform package would have three elements:

- **End the TSA's monopoly on airport screening**. A 2007 study for the TSA found that private screeners consistently outperformed the TSA bureaucrats, so the TSA suppressed it, earning the agency censure from the Government Accountability Office. Airports should be allowed to opt out of the federal system and hire their own screeners, who will be more responsive to customers, and must comply with federal regulations in any event.
- **Remove certain categories of passengers from the intensive screening process**. As international security guru Edward Luttwak put it in a *Wall Street Journal* op ed, "easily recognizable groups that not even the most ingenious terrorists could simulate" should not be viewed as equal in risk to others groups or individuals. Examples include "touring senior citizens traveling together (a category that contains a good portion of all American, European and East Asian tourist traffic), airline flying personnel who come to the security gate as a crew, families complete with children." As Luttwak suggests, the critical question would be whether members of those groups "recognize each other as such."
- **Introduce a robust frequent traveler system**. This would enable members who undergo extensive background checks to bypass certain security checks. Background checks similar to those required for airport workers would be appropriate.

Removing large numbers of travelers from the pool of potential suspects would enable airport screeners to concentrate on those who might pose genuine risks. It would also reduce the number of agents needed, in turn enabling the hiring of more highly qualified personnel, who would treat people as customers rather than cattle. These reforms would in turn make Israeli-style screening far more achievable, something that might otherwise turn into a tedious box-checking exercise for the agents if it were implemented under the current security regime.

Iain Murray

Protect the Environment

Restore the Constitutional Right to Property

The right to property is an essential part of a free society, and widespread private property ownership is a chief limitation on government power and growth. Property rights have traditionally been more secure in the United States than in any other country. However, this is being severely eroded with respect to ownership of real property, as the Supreme Court dramatically underscored in its 2005 *Kelo* decision, which deprived homeowners of their right to private property to allow commercial development. Private property has also been undermined by the Endangered Species Act (ESA), wetlands regulation under the Clean Water Act, and other environmental laws and treaties.

- Lawmakers should advance the constitutional principle of private property by reforming laws that adversely impact landowners to demand that government at least provide compensation when property values are decreased by regulatory measures.
- Lawmakers should ensure that governments—at all levels—do not have the right to seize private property for the purposes of commercial development. When the Framers of the Constitution established eminent domain, they did not intend it to be used to allow one private party to benefit at the expense of others. Public policies should ensure that use of eminent domain be restricted to cases of legitimate public use.

Angela Logomasini

Embrace Private Conservation of Land and Natural Resources

Private stewardship and markets play a critical role in land and natural resource conservation. Much of America's land and other natural resources have suffered because government ownership encourages mismanagement and overuse, because no individual has a long-term stake in protecting resources owned in common. In addition, public lands are managed based on political priorities that often produce misguided political management decisions. Examples include the devastation caused by uncontrolled forest fires, overgrazing, and destruction of species and habitat.

- Lawmakers should consider marketplace incentives and private property-based approaches to encourage land and natural resource conservation.
- Existing laws impede private conservation by making property owners lose use of their land. These laws should be reformed. These include measures in the Endangered Species Act, wetlands regulations, and potential invasive species laws.
- Lawmakers should look for ways to privatize resources owned in common to allow private conservation. Areas in which this has been done successfully but could be expanded include the establishment of fishing rights, privatization of coral reefs, and privatization of species and their habitats in private wildlife refuges.

Angela Logomasini and CEI Staff

Protect Endangered Species

The Endangered Species Act (ESA) of 1973 is bad for wildlife, because it is bad for people. It has largely failed to protect endangered plants and animals because the threat of regulatory "takings" creates perverse incentives, inducing property owners to ensure that their land never becomes habitat or potential habitat for an endangered species.

- Congress should replace the ESA with a non-regulatory, incentive-based conservation program to encourage private landowners to protect and provide habitat. Property owners' natural incentive to be good stewards of their land can work in concert with effective species protection.
- Absent reforms that eliminate the ESA's punitive land use regulations, policies should require just compensation for landowners who are deprived of the right to use their land and whose lands are devalued by government regulation.
- Another policy change that would help species would be elimination of the estate tax. The costs of these taxes often force families to sell off estate properties to developers to pay for the estate taxes on the property. In many cases, individuals would rather keep the properties free from development, but high inheritance taxes make that impossible.

Angela Logomasini and Robert J. Smith

Clarify the Role of Invasive Species

In the past, policies addressing problem plants and animals followed a rational path: They focused on controlling organisms that posed serious threats to agricultural crops and other valued American plants and animals as well as public health. However, the issue associated with so-called invasive species is moving in a new direction, leading to an almost religious crusade to rid the nation of all "non-native" plants and animals. Despite claims to the contrary, many non-native species provide valuable public benefits. Wholesale eradication, instead of management, promises to cause more problems than it would solve. It would result in wasted taxpayer dollars and reduced access to many valuable plant and animal products. In addition, these polices are likely to expand federal land use regulations, undermining the constitutional right to property.

Policy makers in Congress and in the administration should focus on developing a scientifically sound definition of invasive species—one that focuses on harmful and noxious characteristics rather than on country of origin.

In addition, lawmakers should include language in all legislation involving this issue stating that all affected landowners will receive compensation for any economic costs placed on them to meet any invasive species regulations.

Angela Logomasini and Robert J. Smith

Develop New Approaches to Preserve Ocean Resources

The world's fisheries face severe decline. Because many of the world's ocean resources are not "owned," they tend to be overexploited—as everyone attempts to fish out of the ocean as much as possible before competitors can consume the resources. Several governments actively subsidize such destructive practices in attempts to protect traditional fishing industries. However, where genuine, tradable rights have been assigned to ocean resources (as in New Zealand), owners of these rights help ensure long-term conservation and at the same time increase their profitability. Meanwhile, where those rights are bureaucratically controlled, as with the National Oceanic and Atmospheric Administration's (NOAA) "catch share" program, fishermen have instead suffered needlessly.

Similarly, private establishment and ownership of artificial reefs have helped preserve habitats, while government attempts to create artificial reefs have been catastrophic failures. Many of these man-made structures provide critical habitat and ensure plentiful fish supplies.

Such promising policies hold the key to ensuring long-term sustainability of the world's fishery resources. A recent study published in *Science* magazine found that if property rights in fisheries had been instituted globally from 1970, then the incidence of fishery collapse would have been reduced by two-thirds. Fish stocks, furthermore, would be rising rather than falling. Failure to implement such schemes—or implementing such schemes in a distorted manner—for ideological reasons represents a gross disregard for the future of our oceanic ecology and resources. Congress should end NOAA's bureaucratic schemes and extend genuine property rights to this valuable resource.

Iain Murray

Trash Counterproductive Waste Disposal Policies

Solid waste. Many of the nation's current solid waste policies follow an outdated, politicized, and government-centered model. State and local regulators focus on deciding how much waste should be recycled, placed in landfills, or burned in incinerators. This approach fails to discover the most environmentally and economically sound mix of options. Policy makers lack the necessary information and therefore focus on misplaced perceptions about the various disposal options. As a result, they produce recycling programs that cost more than they save and use more resources than they save. In contrast, private sector competition between recycling, landfilling, and incineration produces a market that reduces costs and saves resources.

Federal policy makers should resist attempts to increase federal regulation in solid waste disposal. Local governments should seek ways to increase private markets in the waste disposal industry. They should change waste policies to allow market-driven competition between various disposal options—allowing recycling, landfilling, and incineration companies to complete so that the most environmentally and economically sound mixture of disposal options results.

Electronic waste. Increasingly, news reports and environmental activists claim that we are facing a new solid waste crisis. As a result of such rhetoric, Europe has passed several "e-waste" laws, U.S. states have begun looking into their own regulations, and members of Congress have proposed federal legislation. Unfortunately, misinformation and the misguided notion that government is positioned to improve electronic waste disposal is leading to misguided policies and legislation.

- Despite claims to the contrary, there is no "e-waste crisis." E-waste risks and costs are manageable by allowing private recycling and disposal efforts to continue.
- Manufacturers should not be forced to take back electronic equipment, since they are in the manufacturing, not disposal, business. Some firms have voluntary programs for recycling computers, which offer a market-based approach for some products.
- Congress should avoid creating new government e-waste programs, as they promise to promote inefficiencies, increase environmental problems, and hinder market solutions.
- Consumers should not be taxed when they purchase computers or other electronics, but they should be responsible for disposing of discarded products in a safe and legal fashion. Disposal may include paying somebody to dispose of the product via a voluntary private party agreement or disposal through local government trash collection.

Hazardous waste. Federal hazardous waste policy—as embodied in the Superfund law and the Resource Conservation and Recovery Act—has long been governed by federal mismanagement, perverse incentives, unjust liability schemes, and misuse of science. The Superfund regime of randomly taxing and suing parties not actually responsible for hazardous waste contamination needs reform. Policies should target those who have produced harm—an approach that rewards good behavior and discourages bad.

- Hazardous waste sites are exclusively a state and local concern. Given the demonstrated success of states in managing such sites locally, there is little reason for federal involvement. Thus, Congress should seek ways to further devolve the program to the states.
- Absent devolution, hazardous waste programs should be reformed to provide regulatory relief by setting standards that consider the use of the land and that are not needlessly onerous.
- Liability schemes should be reformed to ensure that only the parties directly responsible for polluting should be held liable. Currently, the Superfund law holds anybody remotely connected to a disposal site liable even if that party did not have any control over the site or the contamination. Parties unfairly held liable include generators of waste that was eventually disposed of at a site, parties that hauled waste to a site, and parties that gained ownership of polluted property.

Angela Logomasini

Recognize the Elitist Nature of Anti-Sprawl Measures

For the greater part of the last century, many people have sought the American Dream by raising their families in suburbs. But today, anti-sprawl activists blame the suburbs for a host of environmental and social ills, and push initiatives to limit housing growth to high-density patterns. In fact, the heads of the Environmental Protection Agency and the Departments of Housing and Urban Development and of Energy have jointly issued a set of "livability principles" for "sustainable communities."

Such initiatives often end up raising housing prices while exacerbating the very problems they claim to fix, such as traffic and pollution. Their main effect is to make suburban living affordable only for the well-to-do.

Federal programs that subsidize suburban development should be restricted or eliminated, but so should programs that boost urban development, whether via subsidies or outright coercion.

Sam Kazman

Affirm the Role of Property Rights in Water Rights Policies

Battles over limited water supplies in the United States and around the world have long produced conflicts and costs to affected communities. While limited supplies are a problem in and of themselves, political management of water is the key problem. Government control of water allocation generally produces inefficient and unfair results.

- A property rights-based system could alleviate water shortages and pollution problems by properly pricing water resources and giving parties a stake in ensuring water quality.
- Policy makers should rethink current approaches to facilitate water markets, which have developed in some areas and show great promise.

Angela Logomasini

Reform Wetlands Policies

Wetlands regulations do a poor job of protecting wetlands habitat. Much federal regulation focuses on preventing development on lands that are dry most days of the year and that do not provide useful habitat for wildlife. In contrast, private initiatives have successfully ensured the protection, restoration, and creation of vital wetlands habitat around the nation. Yet federal wetlands regulations have seriously impeded such private wetlands protection initiatives, and even have forced some parties to abandon attempts to provide such habitat. Policies that can better ensure private wetlands protection, while eliminating destructive and needless red tape, include the following.

- Congress should replace the Section 404 regulatory program, which regulates the dredging and filling of lands, with a non-coercive, incentive-based program.
- At a minimum, the federal government should provide financial compensation to property owners who lose the use of their land due to wetlands regulations.
- State efforts, non-regulatory federal programs, and private conservation would do a better job of protecting ecologically significant wetlands than could the existing federal regulatory approach. These steps would enhance the protection of wetlands and private property without increasing the costs of conservation to taxpayers or to landowners.

Angela Logomasini and CEI Staff

Improve Health and Safety

Reject the Precautionary Principle, a Threat to Technological Progress

Increasingly, governments and environmental activists are demanding that producers of both new and old technologies prove that their products are totally safe. Although this "better safe than sorry" attitude may seem like a reasonable approach to risk regulation, health and environmental risk issues are not so simple. Nothing is totally without risk, and the reason for adopting new technologies in the first place is that they often improve our well-being by protecting us from the risks of older, more established products and practices. Even very risky new technologies may often be better than the alternatives. However, from industrial chemicals to consumer products and everything in between, advocates of precautionary regulation insist that the mere possibility of one increased risk should be sufficient to take useful products off the market or prevent them from ever being used.

New medicines protect us from diseases, even though there is always a risk of side effects. Automobile innovations, from airbags to antilock brakes, make traveling safer, even though they pose their own risks. And food and agriculture technologies—such as preservatives, pesticides, and bioengineered crops—help make our food supply safer and less expensive, and lighten farming's impact on the environment. So, by demanding perfect safety, a precautionary regulatory philosophy can actually make our world less safe by denying society the benefits of new technologies. Regulation's proper goal should be to permit experimentation and the introduction of new technologies, while balancing the risk of moving too quickly into the future against the very real risk of lingering too long in the past.

Just as importantly, the precautionary principle too often is applied in a highly politicized manner to disadvantage technologies that are unpopular or controversial. Although many established practices—such as organic farming, "natural" and homeopathic remedies, alternative energy sources, and countless others—pose known risks that are often far greater than those posed by the new innovations that might supplant them, the precautionary principle has never been applied to rein in those risks. The principle contains no procedural protections for innovators, and it gives regulators nearly unbridled discretion to ban or burden technologies and practices they disfavor.

A better approach to risk regulation would be to more explicitly recognize the human health and environmental benefits that new products bring with them, while recognizing that existing practices are not risk-free. Where possible, regulatory authorities should be required to demonstrate with clear and convincing evidence that new products and practices will do more harm than good before they can keep those products and practices off the market.

Gregory Conko

Reduce Burdensome Regulation of Medicines and Medical Devices

Over the past century, American consumers have benefited from thousands of new pharmaceuticals and medical devices to help them combat disease, alleviate the symptoms of illness and infirmity, and improve their well-being. However, the public often demands that such treatments meet a near-perfect level of safety at bargain basement prices. In turn, Congress and the federal Food and Drug Administration (FDA) have steadily raised the regulatory hurdles that medical product manufacturers must clear before they can market a new treatment.

A strong dose of over-caution when the FDA approves new drugs and devices may sound like a virtue, but for patients in need of new treatments, regulatory over-caution can be deadly. Patients can be injured if the FDA approves a treatment that is later found to be unsafe, but they are also harmed when needed treatments are delayed by regulatory hurdles.

FDA, however, is predominantly focused on the first of these two risks, for political reasons. Agency approval of a drug or device that turns out to be unsafe will lead to front-page headlines and congressional hearings, while delay or denial of a needed new treatment stirs little public notice. Patients may suffer or die as a result of FDA delays, without them or their families ever knowing that a possible treatment exists, let alone that it was blocked by the agency. As a result, the FDA is under constant pressure to assure the safety of new medical products, but under little pressure to speed up their availability.

Many doctors, patient groups, and public policy experts recognize that FDA's lengthy process for approving new drugs and devices often costs lives by denying patients potentially beneficial new treatments. Polls of medical specialists commissioned by the Competitive Enterprise Institute over the past 15 years have consistently found that majorities of doctors in various specialties believe that FDA is too slow in approving new medical products and that these delays mean that patients are not receiving the best possible care.

When making safety evaluations, the FDA is required, by statute, to determine the appropriate balance between patient safety and medical product effectiveness. But more thorough study of drugs and devices during clinical trials (both pre- and post-approval) has its own weaknesses. First, even very large clinical trials generally cannot include enough subjects to detect rare side effects. Second, large trials involve diverse populations with many subgroups that often are not easy to identify. Consequently, a few individual adverse events do not necessarily mean that a product is inherently unsafe for all patients. A given adverse event may not have been caused by the treatment, or if it was, it may be confined to a small subpopulation.

Each patient is different from all others, both in physiology and in risk-level preference. Not only will a given drug or device affect each patient slightly differently, but each patient will place a different value on the product's benefits and the attendant risks associated with it. Therefore, treating the entire population of the United States as identical means that FDA inevitably makes regulatory decisions that will be too cautious for some and not cautious enough for others. Significant political pressure generally pushes the agency toward over-caution, and the end result is fewer new drugs and devices, as well as greater loss of life to what should be treatable illnesses. Those who view the FDA's approval process as too quick may freely choose to use only products that have been on the market for several years with a more well-established record of safety and efficacy. Unfortunately, those who seek access to medical products before the FDA has fully approved them have little or no choice.

Beginning in the early 1990s, the tremendous social cost of FDA overregulation had become apparent, so Congress and the agency took several steps to streamline the approval process. The Prescription Drug User Fee Act of 1992 sped up the drug approval process, saving an estimated 180,000 to 310,000 years of life for patients who relied on newly approved products. The 1997 FDA Modernization Act, for example, granted the agency authority to reduce the number of clinical trials needed for approval and to expedite the review of treatments for serious conditions. But today, FDA is again under tremendous pressure from Congress and self-styled consumer advocates to slow down the approval process and to reject drugs that appear to offer only modest benefits or benefits for only small patient sub-populations.

In 2007, Congress passed the FDA Amendments Act, which provided the agency with additional authority to make pre- and post-market safety studies and clinical trials stricter. The Act also requires FDA to announce publicly even very minor or hypothetical safety concerns, which tends to raise undue alarm among patients. It also requires the agency to consider using Risk Evaluation and Mitigation Strategies for each new approved drug, which can restrict which doctors may prescribe new drugs, which patients may use them, and which pharmacies may fill certain prescriptions. Rather than increase drug safety, these changes, combined with the FDA's innate risk aversion, tend to harm patient health by reducing the availability of new medical products.

Individual patients and their doctors are in a far better position than the FDA to balance the risks and benefits of individual new treatments. The agency should focus on providing them with information rather than on restricting their choices. In forthcoming legislation, Congress should seek to accelerate the pace at which the FDA reviews new drug and device applications, and it should repeal many of the recent policies that make FDA regulation dangerously overcautious.

Greg Conko and Sam Kazman

Purify Federal Water Policies

Drinking Water. Drinking water policy should focus on how best to ensure that Americans have clean and safe water to drink. Currently, many communities are forced to spend limited resources to meet misguided and scientifically questionable federal mandates. States and localities are better able to set priorities based on their particular needs. Moreover, drinking water policy would benefit from a more market-driven model, one that allows for more private innovation in the provision of drinking water services:

- Congress should return full authority to set standards to the states, allowing them to work with localities to meet their specific needs.
- Should the federal government remain involved, there are ways to help empower localities within a federal framework. Congress should engage in greater review of safe drinking water rules to ensure that the Environmental Protection Agency has employed the "best available science" as demanded under the law. If large questions remain over science, and standards are likely to impose considerable costs, Congress should preempt overly stringent standards.
- Congress should consider ways to grant states discretion on how to regulate naturally occurring contaminants, such as radon and arsenic, to reflect localized levels of risk.

Water Quality. Waterways throughout the United States have suffered from various pollution problems because they have long been held in common, so no one was in charge of keeping them clean. Congress passed the Clean Water Act in the 1970s, which has been a mixed blessing. While many waterways have seen improvements, the program is very bureaucratic, and it has promoted too much expensive litigation that focuses on paperwork violations rather than on improving water quality. The science underlying many of the regulations is weak. In addition, parts of the Act have proven ineffective, such as programs addressing non-point source water pollution (water runoff from lands). Policy makers should look at innovative, market-based systems for advancing water quality:

- Instead of focusing on paperwork violations, policy makers should hold polluters liable for the actual harm they cause to other persons or to their property.
- States need flexibility. Because the science of water pollution control is evolving, and because each state and watershed has different needs and problems, Congress should give states flexibility in water quality management approaches.

Angela Logomasini and CEI Staff

Ensure Consumers' Access to Bottled Water

Bottled water offers many important benefits—including portability, emergency applications, and convenience. The bottled water industry had been particularly valuable during major crises, such as the September 11, 2001, terrorist attacks, Hurricane Katrina, and other calamities. Nonetheless, recent attacks against bottled water by environmental activists threaten to undermine this industry and impede consumer freedom.

Some states have enacted regulations and taxes largely on the basis of unfounded claims about bottled water. For example, some environmental groups claim that most bottled water is simply re-bottled tap water. Yet only 25 percent of bottled water comes from municipal sources—the rest comes from springs and underground sources—and most of the municipal-source water undergoes extensive treatment before bottling that involves additional purification and other processing to improve flavor and quality.

In addition, all bottled water must meet specific standards before bottling, and unlike pipe delivery systems for tap water, sanitary packaging enables transport of bottled water with a very low risk of contamination. All bottled water must also meet Food and Drug Administration (FDA) regulations—most of which mirror Environmental Protection Agency (EPA) tap water regulations and some of which exceed those regulations. Accordingly, the EPA and the Centers for Disease Control and Prevention recommend bottled water as a safer alternative to tap water for individuals with compromised immune systems.

Because of the hype, Congress may consider regulation of bottled water such as new labeling mandates. Yet most bottles of water contain information on water source. Consumers who care to do so can choose bottles with such information on the market, thus creating demand for specific types of labeling. Currently, FDA regulates the terminology to prevent fraudulent claims. Regulations requiring additional information are unlikely to change consumer purchasing habits and could simply increase confusion and costs.

Bottled water is popular with the public for its convenience, freshness, and healthfulness. Congress should not impose new regulations that will impede consumer choice and raise costs. Consumers who do not want to drink bottled water can choose other alternatives rather than regulate options for others.

Angela Logomasini

Enhance Auto Safety

Automotive safety is the primary mission of the National Highway Traffic Safety Administration (NHTSA). In recent decades, however, NHTSA's mission has increasingly become distorted by political correctness and environmental agendas. For example, the agency has focused on the alleged safety hazards of sport utility vehicles while paying little attention to the safety risks of subcompact cars. Moreover, NHTSA has moved to mandate safety features that are already becoming widely adopted due to consumer demand, such as electronic stability control systems. Such mandates end up limiting design flexibility and constitute little more than an exercise of regulatory muscle.

One major NHTSA program actually increases traffic deaths by significantly reducing vehicle crashworthiness. The agency's auto fuel economy standards, known as CAFE (for corporate average fuel economy), force vehicles to be downsized in order to boost miles per gallon. Downsized vehicles have less mass to absorb collision forces and less interior space in which to safeguard passengers. As a result, CAFE causes several thousand additional traffic deaths per year in the name of saving gasoline. Several years ago the agency reformed CAFE to reduce its downsizing incentive, but this reform is now being overwhelmed as the Obama administration seeks ever higher—and therefore more lethal—fuel economy standards. Unbelievably, 62 mpg is now under study as a possible target for 2025. Congress should halt any increases in CAFE standards. At a minimum, NHTSA should undertake a comprehensive study of the deaths attributable to CAFE, both on a yearly basis and over its 30-year history.

Sam Kazman

Improve Food Safety and Quality through Greater Information, Consumer Choice, and Legal Accountability

Few issues are as important to consumers as the safety and quality of their food—from microbial contaminants to pesticides, and from organics to obesity. Recent health scares—from salmonella-contaminated eggs to E. coli-contaminated spinach and tomatoes—show just how fragile the food chain can be. But, while these tragic events have led to calls for greater government oversight of the food supply, the nature of these scares shows that additional regulations or inspections are likely to do little to improve food safety. Poorly conceived government regulation often does as much to compromise food safety, affordability, and choice as to promote it—especially when the regulatory framework is focused on a fear-driven activist agenda rather than on basic principles of science and genuine safety.

Too often, the government's regulatory agenda favors politically expedient outcomes over those that would actually promote safety and availability. For example, the U.S. government maintains outmoded visual examination and "poke and sniff" food inspectors whose methods are incapable of detecting microbial pathogens. At the same time, heavy regulatory burdens make it difficult to introduce technologies, such as irradiation, that could cut the incidence of those pathogens by half or more. Americans consume nearly 1 billion meals every day, and microbial pathogens can be introduced at any stage in the food production and distribution system. Merely adding additional inspectors cannot realistically be expected to prevent future contaminations. Instead, the legal system should punish producers and sellers who are negligent in the handling or purchasing of the foods we eat. Food companies should be allowed the flexibility to adopt technologies and practices that can cut the incidence of food-borne contaminants.

In addition, regulators control the content of food labels so stringently that sellers are often forbidden from informing consumers of many beneficial product attributes. Food safety and labeling regulations should be designed with maximum flexibility, to allow food producers to use the production methods and labeling information that best meet their customers' demands. Government studies have shown that liberalizing labeling and advertising restrictions on food products actually leads producers to supply healthier and more nutritious products, increasing consumer well-being.

Lawmakers should eliminate regulatory barriers that make it harder to adopt beneficial new food production technologies, such as irradiation and crop biotechnology. Mandatory labeling of irradiated food provides no useful or material information to consumers, but it does scare consumers and retailers away from safe irradiated foods. Existing U.S. Department of Agriculture rules make it impossible for cattle ranchers to voluntarily test their herds for mad cow disease and then advertise the attribute to consumers.

Policy makers should abandon the misguided notion that natural products are inherently safe and synthetic products inherently dangerous. Synthetic compounds, as a class, are no more toxic or carcinogenic than compounds that exist in nature. The dose makes the poison—many substances that are dangerous at very high levels are totally harmless at lower levels. This is true for both natural and manmade substances. Rules that mandate labeling of even trace amounts of certain synthetic chemicals are based on a faulty understanding of science and are therefore bad public policy.

Government should not make lifestyle choices for consumers regarding the foods they eat. All foods, whether they contain large amounts of fat, calories, sugar, sodium, or other constituents, can be a part of a healthy diet. Consumers may benefit from having accurate information about nutrition, calories, and fat content, but government should not ban or otherwise limit consumer access to certain foods simply because public health officials believe that some consumers overindulge in them.

Gregory Conko

Protect Incentives for Pharmaceutical Innovation

In recent years, Congress has faced mounting public pressure to "do something" about the rapidly rising prices of prescription drugs and to rein in what are believed to be excessive industry profits. Although prescription drug spending comprises just 10 percent of overall health care costs, it has been one of the fastest growing components of overall health care spending during the past two decades—rising by an average of 11 percent annually during the 1990s and by 9 percent in 2006, compared to just 6 percent for spending on physician services, according to the Kaiser Family Foundation.

Faced with this public pressure, as well as mounting federal and state government expenditures on drug purchases, members of Congress have proposed a variety of measures to cut the price of prescription drugs. These include reimportation of lower-priced drugs from foreign countries with price controls, direct negotiation of reduced drug prices by the Centers for Medicare and Medicaid Services, and direct restrictions on drug and medical device industry marketing and promotion practices. More recently, would-be health care cost cutters have proposed integrating cost-benefit and comparative-benefit analysis into government-run health programs and in the Food and Drug Administration's (FDA) approval process. For example, the Patient Protection and Affordable Care Act created a new Patient Centered Outcomes Research Institute (PCORI) to study the comparative effectiveness of different treatment options with the expectation that drugs and other treatment options that do not deliver what it considers sufficient "bang for the buck" will cease being prescribed.

Unfortunately, most advocates of such policies have a tunnel-vision dedication to reduce drug costs, with little concern for the effect that forced price reductions would have on industry incentives for innovation. Pharmaceutical prices are high because drug development is expensive, many new drugs treat relatively small patient populations, and most pharmaceuticals fail in laboratory tests or clinical trials before ever making it to market. A 2006 study by U.S. Federal Trade Commission economists concluded that the average cost to develop and test a new drug is between $839 million and $868 million. Thus, policies such as reimportation and comparative-effectiveness analysis would, in the short run, result in lower prices for drugs already on the market, but in the long run reduce both the number of treatment options available and the flow of new drugs entering the marketplace.

The primary argument for incorporating comparative-effectiveness or cost-benefit analysis into government purchasing and approval decisions is that many expensive new drugs offer little therapeutic advantage over older drugs, but that they cost far more than the closest comparable older drugs. If government health programs paid for only the "best in class" medicine for each therapeutic category, the higher volume of purchases would justify significant price reductions. However, while on average the therapeutic benefit of various drugs in a particular class may be similar, individual patients will often respond quite differently—even to very similar drugs. While it is advisable for public programs to trim excessive costs, implementing cost-benefit or comparative-effectiveness analysis in purchasing or approval decisions would negatively affect patient care.

Although the health care reform legislation stipulates that PCORI recommendations shall not be used as the basis for rationing care, the Act also created a new Independent Payment Advisory Board for the purpose of reducing the growth rate in Medicare spending. That body is expected to rely, in part, on PCORI recommendations to evaluate physician and hospital quality, which means that PCORI recommendations will covertly be used as the basis for restricting available treatment options for patients. Even more pernicious is a proposal by the Centers for Medicare and Medicaid Services and FDA to establish a parallel review process for medical products, which many fear could result in comparative-effectiveness or cost-benefit considerations being improperly introduced into the new drug and medical device approval process.

The argument for reimportation is no more convincing. Although the prices of off-patent and generic drugs—which comprise more than half of all prescriptions filled in the U.S.—are typically higher in other countries, the prices of the latest on-patent drugs is often much lower in countries that impose direct or indirect price controls. Consequently, reimportation advocates promise to relieve high drug costs by allowing American consumers to free-ride on other nations' price controls. But allowing reimportation would effectively import foreign price controls, resulting in less revenue for the industry and a reduction in the capital available to drug companies for continued research and innovation.

Finally, drug industry profits are not "excessive" by any honest measure. Pharmaceutical industry critics like to point out that, in 2005, pharmaceutical firms in the Fortune 500 placed ninth out of the 50 industries ranked by return on assets, 12th in 2004, and second in 2003. However, as the Congressional Budget Office (CBO) notes, "those figures misrepresent the industry's actual profits." Standard accounting measures overstate profitability for R&D-intensive industries by treating most research spending as an expense rather than as a capitalized investment that increases the company's value. "Not accounting for that value overstates a firm's true return on its assets," says the CBO.

Ultimately, high pharmaceutical retail prices reflect the vast expense of developing those products and getting them approved for sale. Without correspondingly high prices, few investors would be willing to take the risks inherent in supplying capital to the pharmaceutical industry. The result would be fewer and fewer lifesaving medicines.

Gregory Conko

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