

---

# Regulatory Reform and the Political Process

Douglas Hartle

Michael J. Trebilcock

Follow this and additional works at: <http://digitalcommons.osgoode.yorku.ca/ohlj>  
Article

---

## Citation Information

Hartle, Douglas and Trebilcock, Michael J.. "Regulatory Reform and the Political Process." *Osgoode Hall Law Journal* 20.4 (1982) : 643-677.  
<http://digitalcommons.osgoode.yorku.ca/ohlj/vol20/iss4/1>

This Article is brought to you for free and open access by the Journals at Osgoode Digital Commons. It has been accepted for inclusion in Osgoode Hall Law Journal by an authorized editor of Osgoode Digital Commons.

# OSGOODE HALL LAW JOURNAL

Vol. 20

No. 4

December 1982

## REGULATORY REFORM AND THE POLITICAL PROCESS

By DOUGLAS HARTLE\* AND MICHAEL TREBILCOCK\*\*

I. INTRODUCTION .....	644
II. COMPETING VIEWS OF PUBLIC POLICY DECISION- MAKING.....	644
III. DE-REGULATION .....	649
IV. CHANGING THE POLITICAL PLAYERS	
A. Compensating Losers from Regulatory Changes	
1. Losers/Compensation Recipients .....	655
2. Gainers/Compensation Underwriters.....	656
3. Politicians.....	656
4. Bureaucrats .....	657
B. Funding Public Interest Groups .....	658
V. ENHANCING THE INFORMATION BASE FOR PUBLIC POLICY DECISIONS .....	664
VI. ENHANCED POLITICAL ACCOUNTABILITY .....	670
VII. CONCLUSIONS.....	675

---

©Copyright, 1982, Douglas Hartle and Michael Trebilcock

\*Professor of Economics, University of Toronto.

\*\*Professor of Law, University of Toronto.

## I. INTRODUCTION

This article evaluates the political prospects for various major regulatory reform thrusts that have emerged in government reports and academic writings and from experience in other jurisdictions in recent years. The article begins by emphasizing the importance of the political incentives facing policy makers under the "constitutional" rules that govern collective decision-making in Canada. In particular, the difference between incentives imparted by a rule of voter unanimity, which would tend to ensure that only Pareto improving policies are adopted, and majority rule, which creates incentives for politicians to engage in redistributive policies, is emphasized. In light of existing constitutional and electoral rules, the article then proceeds to evaluate the following reform thrusts: deregulation; changing the configuration of political influence through compensation of losers or public funding of thinly spread "public interest" groups; cost-benefit and cost effectiveness analysis; and increased parliamentary scrutiny of existing and proposed regulatory programmes through parliamentary committee review and ministerial directives to statutory regulatory agencies. In each case, the article concludes that in the absence of fundamental reforms to existing political incentive structures, the proposed regulatory reforms are either unlikely to be introduced, or, if introduced, unlikely to have any substantial impact on regulatory policies. The analysis also suggests a rather limited impact for public policy-oriented economic analysis, which is likely to be viewed by political decision makers not as a source of intelligence about the world but as a source of support for, or objection to, various policy options which are likely to be chosen for political rather than economic reasons. However, it will also be seen that to the extent that public policy-oriented economic research provides voters with improved information about the impact of alternative policies, politicians may be compelled to respond to the changes in voter preferences that result from this new information.

## II. COMPETING VIEWS OF PUBLIC POLICY DECISION-MAKING

From the beginning of this century, when the old subject of political economy split into the disciplines of economics and political science, until about twenty years ago, most economists carefully eschewed any interest in the political decision-making process. As Peltzman put it, government was treated as a *deus ex machina*.<sup>1</sup> The appropriate role for economists was taken to be advising the "disembodied Prince" on how to eliminate market imperfections and thus achieve Pareto optimality (the optimal output possible given resource constraints, the prevailing distribution of income and wealth, prevailing individual tastes and preferences and prevailing technology).

The concept of the "social welfare function" was the cornerstone of the logical structure upon which this edifice of welfare economics (allocative efficiency economics) was built. This simple mathematical expression stated that collective welfare, "W", was a function of arguments that included all the weighted objectives of society. Thus,  $W = f(X_1, X_2, \dots, X_n)$ , where  $X_1$  is the

---

<sup>1</sup>Peltzman, *Toward a More General Theory of Regulation* (1976), 19 J. Law & Econ. 211.

first objective,  $X_2$  the second objective, and so on.<sup>2</sup> It was assumed that everybody wanted to maximize total welfare, thus defined. The government, as an ongoing decision-making organization, replete with human beings with their own objectives, was ignored completely.

Soon after Bergson introduced the social welfare function concept,<sup>3</sup> Samuelson set forth mathematically the marginal conditions that must obtain to maximize the function (that is, to make the economy Pareto efficient such that no one could be made better off without injuring one or more others).<sup>4</sup> A complex debate has ensued, however, concerning what can be said about the optimal *distribution* of this optimal (with respect to size and composition) bundle of goods and services. The upshot of the debate is that, with one exception, unless there is a dictator who imposes his or her preferences concerning the desirable distribution of output, nothing can be said about optimal distribution. This proposition holds unless one is prepared to make interpersonal cardinal comparisons of utility. (Ordinal comparisons of greater versus lesser will not suffice.) Because these comparisons are inherently arbitrary and normative, economists *qua* economists have nothing particularly interesting or important to say about them.

An attempt was made by Arrow to derive social welfare functions logically (consistently) from individual preferences (choices) using five basic ethical premises (axioms) that might be thought of as the articles of a community's social contract or constitution.<sup>5</sup> He found that despite the eminently reasonable and consensual nature of the premises, it was impossible to derive the function except under unacceptably stringent conditions, that is, under unanimous choices.

Arrow's "Impossibility Theorem" proved that individual choices could not be aggregated to obtain a collective choice except by abandoning one or more of his five axioms. This led to the question: "What are the implicit axioms underlying majority and unanimity voting rules?" Table I, reproduced from Mueller,<sup>6</sup> captures the outcome of the debate.

Three important points should be noted:

- a) The "appropriate" voting rule depends on the issue at stake.
- b) Even when there is a proposed policy change, such as an improvement in allocative efficiency, that would benefit all (pure positive sum games) and the majority rule is to be applied, it is in the interest of some to coalesce and form a majority. The majority could then insist that a rider be attached to the proposal that would provide for an extra amenity for the majority. Through the rider the majority could extract some or all of the total benefit for themselves. Implicitly, therefore,

<sup>2</sup>For a brief, clear review of the history and developments of the concept see Mueller, *Public Choice* (Cambridge: Cambridge Univ. Press, 1979) at 174-83.

<sup>3</sup>Bergson, *A Reformulation of Certain Aspects of Welfare Economics* (1954), 68 Q.J. Econ. 233.

<sup>4</sup>Samuelson, *Foundations of Economics* (Cambridge: Harvard Univ. Press, 1947) at 230-33.

<sup>5</sup>Arrow, *Social Choice and Individual Values* (2d ed. New York: Wiley, 1963).

<sup>6</sup>*Supra* note 2, at 216-17.

those favouring majority rule either assume that majorities do not form to coerce minorities or, accept the redistributive implications that this coercion permits.

- c) The unanimity rule precludes decisions that involve redistribution. Those supporting the rule obviously assume that redistribution should not take place. They are also assuming that negotiating the compensation of potential losers under a proposed collective decision is not too costly; and, that strategic behaviour where the minority (perhaps one person) coerces the majority does not occur.

TABLE I  
ASSUMPTIONS FAVORING THE MAJORITY  
AND UNANIMITY RULES

Assumption	Majority rule	Unanimity rule
1. Nature of the game <sup>a</sup>	Conflict, zero sum	Cooperative, positive sum
2. Nature of issues	Redistributions, property rights (some benefit, some lose) Mutually exclusive issues of a single dimension <sup>b</sup>	Allocative efficiency improvements (public goods, externality elimination). Issues with potentially several dimensions and from which all can benefit <sup>c</sup>
3. Intensity	Equal on all issues <sup>d</sup>	No assumption made
4. Method of forming committee	Involuntary. Members are exogenously or randomly brought together <sup>e</sup>	Voluntary. Individuals of common interest and like preferences join <sup>f</sup>
5. Conditions of exit	Blocked, expensive <sup>g</sup>	Free
6. Choice of issues	Exogenously or impartially proposed <sup>h</sup>	Proposed by committee members <sup>i</sup>
7. Amendment of issues	Excluded, or constrained to avoid cycles	Endogenous to committee process <sup>j</sup>

<sup>a</sup> Buchanan and Tullock [1962, p. 253]; Buchanan [1966, pp. 32-33].

<sup>b</sup> Barry [1965, pp. 312-14]; Rae [1975, pp. 1286-91].

<sup>c</sup> Buchanan and Tullock [1962, p. 80]; Wicksell [1896, pp. 87-96].

<sup>d</sup> Rae [1969, p. 41, n.6]; Kendall [1941, p. 117]; Buchanan and Tullock [1962, pp. 128-30].

<sup>e</sup> Rae [1975, pp. 1277-8].

<sup>f</sup> Wicksell [1896, pp. 87-96]; Buchanan [1949]. This assumption is common to all contractarian theories of the state, of course.

<sup>g</sup> Rae [1975, p. 1293].

<sup>h</sup> This assumption is implicit in the impartiality assumed by Rae [1969] and Taylor [1969] in their proofs, and in Barry's example [1965, in particular on p. 313].

<sup>i</sup> Wicksell [1896]; Kendall [1941, p. 109]

<sup>j</sup> Implicit.

The implication of Mueller's table is that the ideal constitution should require the application of the unanimity rule for allocative changes and majority rule for redistributive changes. It should be noted that the Pareto optimality rule is tantamount to the adoption of the unanimity voting rule for allocative efficiency issues. The existing distribution of income and wealth is taken as given. It is implicitly assumed to be satisfactory or, if not, that it should be treated as a separate question.

All of this is conceptually tidy, but in practical terms virtually all policy decisions have both allocative and distributional implications. Those actually or potentially involved in making such decisions have no reason to refrain from pursuing both allocative and distributional objectives simultaneously if it is in their personal interest(s) to do so. Furthermore, a constitution that would lay down two sets of voting rules for the two conceptually distinct aspects of each policy proposal is clearly unthinkable.

The lengthy debate about voting rules has been abortive except in clarifying the implications of the implicit assumptions. Of particular importance is the increased awareness of the overriding significance of the "constitution", the set of rules that determines how all the other rules are made. Although perhaps hardly satisfying intellectually, it is now generally admitted that, above all, the constitution must be seen to be fair in order that the derivative rules, and the decisions made under those rules, be perceived to be legitimate.

Rawls's *A Theory of Justice*<sup>7</sup> has been of great influence in the discussion surrounding the development of a "just social contract" or constitution. Unlike most of his predecessors, Rawls, a political philosopher, has emphasized the process or context in which decisions are made, as much as, if not more than, the outcome of the process.<sup>8</sup> As Mueller puts it, "our quest for a theory of the unanimous agreement to the rules and procedures underlying the collective decision-making process is [not] at an end."<sup>9</sup> The same can be said for the works of Harsanyi,<sup>10</sup> Varian<sup>11</sup> and Buchanan<sup>12</sup> to name only a few. What has emerged, however, is an awareness of the kinds of considerations involved in constitution making. Of the essence is the notion that because the constitution is "forever", those formulating "the rules determining the rules" must proceed impartially because of the overwhelming uncertainty about virtually everything except the ever present necessity of appearing to be just in their application and effect. To quote Mueller again:

Beyond simply emphasizing the importance of consensus, however, these studies have suggested how it might be reached. Despite all of the criticism of these works, the ideas of justice as fairness, impartiality, and equiprobability have survived largely unscathed. This is no mean achievement. For it suggests a shared view

<sup>7</sup> (Cambridge: Harvard Univ. Press, 1971).

<sup>8</sup> *Id.* at 227.

<sup>9</sup> *Supra* note 2, at 246.

<sup>10</sup> *Can the Maximin Principle Serve as a Basis for Morality? A Critique of John Rawls's Theory* (1976), 69 *Am. Pol. Sci. Rev.* 594.

<sup>11</sup> *Equity, Envy and Efficiency* (1974), 9 *J. Econ. Theory* 63.

<sup>12</sup> *Hobbesian Interpretation of the Rawlsian Difference Principle* (1976), 29(1) *Kyklos* 5.

toward individualism, a shared view toward the setting in which social choice takes place, and further basic agreement on the underlying properties of the social decision problem. If agreement does exist at this intuitive level, then it should be possible to extend our shared intuitions and design a process for drafting a constitution which would achieve consensus. The studies reviewed here have not carried us very far in this process, but they have pointed us in the right direction. A logical place for collective choice work to proceed is in the design of such processes.<sup>13</sup>

Having been led to consider the logic of voting rules as a result of their interest in the properties of the normative social welfare function, it was perhaps not surprising that some economists were led to apply basic economic concepts to the analysis of political behaviour. Why not assume that politicians are self-interested individuals who seek to maximize the likelihood of their election or re-election? Is it not reasonable to suppose that bureaucrats have personal interests that they pursue when advising politicians and when implementing political decisions? Is it not reasonable to suppose that voters cast their ballots for the party or candidate that they expect to do them the most good or the least harm, in other words, that they maximize their "utility income"? Under what conditions do voters and others coalesce to put pressure on governments for favourable decisions? Under what conditions are they likely to be successful? Because voters must choose on the basis of the expected future behaviour of those elected, voter perceptions are of the essence. And these perceptions are engendered, of course, by information which is always costly, limited and frequently biased. This raises questions about the role of the media in the political decision-making process. These kinds of assumptions and problems are the stuff of what is now widely termed "public choice" economics.<sup>14</sup> This is the conceptual framework underlying the analysis in this article.

Leaving aside the part of public choice economics that is concerned with optimal constitutions (for example, voting rules), attention has been directed towards explaining, and preferably predicting, political behaviour under existing rules. In short, while conventional welfare economics seeks to specify what should be done by government to improve economic efficiency, public choice economics seeks to analyze why governments do what they do and *why* they frequently fail to follow the injunctions of economists. Fundamentally, yet strangely, the same basic concepts are involved with both approaches. The theory of consumer behaviour, for example, assumes that individuals seek to maximize their utility within their budget constraints when selecting among goods with given relative prices. Similarly, the theory of the firm assumes that entrepreneurs seek to maximize their profits when selecting among factor inputs and product outputs with given relative prices. In the same way, public choice analyses assume that politicians seek to maximize their personal utility by, at least in the first instance, maximizing the likelihood of their election given the preferences of the marginal voters in marginal constituencies. It is in the self-interest of politicians to select the most *politically* efficient policies just as it is in the entrepreneur's self-interest to select the most economically, as distinct from technically, efficient method of production. The prices of electoral success, although mostly implicit, are of the essence too.

---

<sup>13</sup> *Supra* note 2, at 260.

<sup>14</sup> See Mueller, *supra* note 2; Frohlich and Oppenheimer *Modern Political Economy* (New Jersey: Prentice Hall, 1978).

Economists are wedded to the "self-interest" postulate to the point where they usually give little credence to "moral suasion". In their anxiety to disentangle their subject from politics, however, mainstream economists have adopted the "maximize economic efficiency" credo with gusto. Pareto optimality as *the* relevant economic goal has been accepted almost without question. Indeed, virtually all of the economic analysis carried out for the Economic Council of Canada in its recent study of regulation was based on this normative premise. There is no doubt that the adoption of the premise allows economists to draw normative implications with rigour. Curiously enough, adoption of the Pareto standard places economists in an anomalous position. Their analytic conclusions are, for the most part, normative and the recommendations can be looked upon as attempts at moral suasion. Although incentive structures are of paramount importance in their analyses of market behaviour, in their policy recommendations most economists seem to treat political incentives as either irrelevant or favourable. Certainly the latter assumption seems precarious in light of all of the contrary evidence and the constitutional rules, particularly the majority voting rule, within which political decisions must be reached. The analysis of regulatory reform presented here, which adopts a public choice perspective, takes precisely the opposite view. It is from this perspective that this article will review the prospects for several major thrusts in regulatory reform that have recently emerged in policy debates, academic literature and the Council's two reports on regulatory reform.<sup>15</sup>

### III. DE-REGULATION

In the final report of the Economic Council of Canada, *Reforming Regulation*,<sup>16</sup> published pursuant to its Regulation Reference, the Council recommends sweeping de-regulation policies with respect to trucking, taxicabs, airlines, telecommunications, agricultural marketing boards and the professions. Thus far, federal and provincial governments have been noticeably non-committal with respect to the implementation of these detailed sectoral recommendations except in the case of airlines, where the federal government has, in effect, recently rejected the Council's recommendations. Newspaper reports have given prominence to strongly voiced industry opposition to the Council's recommendations in the areas of taxis, airlines, telecommunications and agricultural marketing boards. What are the political prospects for the de-regulation portions of the Council's report?

In assessing such prospects, it is appropriate to point out that the terms of reference from the Prime Minister to the chairman of the Council for its study of regulation stated: "As you know, there has developed in Canada a strong concern that increasing government regulation might be having serious adverse effects on the efficiency of Canadian firms and industries and on the allocation of resources and the distribution of income."<sup>17</sup> This view echoed the view

---

<sup>15</sup> Economic Council of Can., *Responsible Regulation* (Ottawa: Min. of Supply and Services Can., 1979); Economic Council of Can., *Reforming Regulation* (Ottawa: Min. of Supply and Services Can., 1981).

<sup>16</sup> *Id.*

<sup>17</sup> *Responsible Regulation*, *supra* note 15, at 119.



of the First Ministers at a meeting in February of the same year, who, in a communiqué proposing a study of regulation in Canada, stated: "The burden of government regulation on the private sector should be reduced and the burden of overlapping federal and provincial jurisdictions should be eliminated. Procedures will be instituted to review the effects of regulatory action on jobs and costs."<sup>18</sup> Thus, political forces generally perceived as favouring de-regulation appeared to represent a major part of the rationale for the study. How deep do these forces run?

First, it is worth noting that de-regulation, like tax reform, tends to mean different things to different interests. To producer interests, it probably means reduced emphasis on health and safety regulation, environmental regulation, consumer protection regulation and "paper burden" requirements. To consumer interests, it probably means maintaining or enlarging the policy emphasis in these areas while reducing anti-competitive regulations which restrict entry, price competition and innovation in a number of sections. For example, the tenor of the Prime Minister's letter and especially the First Ministers' communiqué implies a concern principally with the adverse impact of regulation on Canadian firms and industries and thus, a sensitivity to the producers' view of the case for de-regulation. Significantly, the Council's de-regulation recommendations are animated almost entirely by the consumers' view of the case for de-regulation. Producer interests concerned about increased health, safety, environmental and consumer protection regulation have had to settle for a complex set of recommendations in the Council's interim report favouring increased use of *ex ante* and *ex post* cost-benefit studies of the effectiveness of regulations of this kind.

The probable impact of the Council's recommendations is that they will quickly dissolve any apparent political consensus favouring significant degrees of de-regulation. The same political forces that led to initial regulatory intervention will, in general, be able to resist de-regulation. This is not to deny that political preferences change over time, or that some established political constituencies fade while new constituencies emerge, or that these changes in the political landscape will have some impact on the configuration of regulatory policies that are observed. There is, however, absolutely no reason in theory to predict that these changes in political forces will — over time — uniformly lead in the direction of less, rather than more, regulation. Despite the difficulty of predicting changes in the absolute level of regulation in our economy, it is possible to identify some forces that seem likely to shape the nature of prevailing patterns of regulation.

First, the consumer interest — as a widely-dispersed, thinly-spread interest faced with serious problems of transaction costs and free riders in attempting to organize an effective political lobby<sup>19</sup> — will probably continue to be systemically under-valued in policy making. This suggests that consumers will in general be hard pressed to secure the reduction (or prevent the expan-

---

<sup>18</sup> *Id.* at 120.

<sup>19</sup> Trebilcock, *Winners and Losers in the Modern Regulatory System: Must the Consumer Always Lose?* (1975), 13 *Osgoode Hall L.J.* 619.

sion) of anti-competitive forms of pro-industry regulation in areas such as agriculture, transportation, telecommunications and the professions. Similarly, consumers may be hard pressed to retain or expand gains made in areas of social regulation such as health, safety and disclosure regulation — although public consternation over recent safety mishaps, such as the DC-10 crash in Chicago and the incident at Three Mile Island, suggest that safety issues (if dramatic enough) are capable of catalyzing consumers into effective political action.

Second, it seems likely that politicians, to accommodate increased public apprehensions about the size of government, will be forced to oppose new legislative or regulatory programmes, while largely resigning themselves to living with existing programmes where “client” groups, regulators and bureaucrats have vested interests which are more difficult to repudiate than interests which are merely prospective.

Third, where de-regulation of existing programmes is undertaken the programmes in question will likely be of trivial significance, (for example, the Ontario Pregnant Mare Urine Licence Review Board) where retention or repeal is a matter of little moment, or the programmes will be those where producer interests have been successful in defining de-regulation as “privatizing” regulation by the substitution of legally sanctioned forms of industry self-regulation for direct regulation by the State.

Fourth, one might predict that major de-regulation is most likely to occur where the political support for it comes from concentrated (and thus politically well-organized) business interests, rather than non-business consumer interests. This appears to have been the case in the general de-regulation of brokerage rates on United States stock exchanges and in the partial de-regulation of brokerage rates on the Toronto stock exchange where the pressure came from major institutional investors. This is also the case with the de-regulation of oil and natural gas prices in the United States, where the pressure has come from the major oil companies and has recently been the case in Canada in the CN/CP — Bell interconnection issue.<sup>20</sup> Some analysts of airline de-regulation in the United States argue that the evidence shows widely dispersed consumer winners and highly concentrated industry losers, thus confounding the conventional public choice hypothesis of the predominance of concentrated interests over dispersed interests in political decision-making.<sup>21</sup> Under this public interest explanation of airline de-regulation, a theory of mistake is offered to explain the initial decision by Congress to regulate the airlines, a mistake which became apparent with the passage of time and the accumulation of experience. There is reason to be sceptical of the explanatory breadth of theories of political “mistakes” given the existence of vigorous competition amongst parties and interest groups. Certainly, there is no evidence of any inclination towards general airline de-regulation in Canada despite the learning experience offered by the United States, and in cases like

---

<sup>20</sup> *CNCP Telecommunications, Interconnection with Bell Canada*, Telecom. CRTC Decision 79-11 (May 17, 1979).

<sup>21</sup> Levine, *Revisionism Revised? Airline Deregulation and the Public Interest* (1981), 44 *Law and Contemp. Prob.* 179.

agricultural marketing boards, the allocative inefficiencies of current policies have been pointed out repeatedly to politicians without inducing any suggestion of revelation, recantation or re-evaluation. What may be true in some cases, such as airlines and trucking, is that the deadweight costs of regulation mount over time, thus reducing industry returns from regulation and perhaps creating some industry constituencies for de-regulation. For example, the costs of non-price competition in the airline industry together with changes in technology making new entry feasible on certain routes may have substantially changed industry attitudes to regulation, at least in the United States.<sup>22</sup> In the case of trucking, problems of policing "gypsy" trucks and preventing substitution of "own-trucking" capacity by shippers may, over time, have substantially reduced the gains from regulation to regulated trucking firms. However, if these factors in part explain de-regulation in the airline and trucking industries in the United States, one is still left with the puzzle, explored by Stanbury and Thompson elsewhere in this symposium,<sup>23</sup> of why these same factors have not led to similar pressures for de-regulation in Canada. In the case of airlines, the presence of major Crown corporations (national and regional) and a historically persistent and currently rising tide of economic and cultural nationalism prompting interventionism in many areas of the economy, may make it politically more difficult to promote a climate that acknowledges the virtues of competitive forces in particular sectors.

Fifth, where United States de-regulation policies generate major spillovers in Canada because of the international or continental nature of the markets involved, additional pressures for change are likely to be created in Canada. For example, lower airfares in the United States have an impact on patterns of airline travel in Canada, at least with respect to transcontinental routes. Reduced brokerage rates in the United States create incentives for investors to place Canadian brokerage business for jointly listed securities through United States exchanges. De-regulation of oil and natural gas prices in the United States, if not met by countervailing shifts in Canadian policy, reduces the incentives for oil companies to invest in exploration activities in Canada.

These factors suggest some prospects for limited de-regulation in Canada in areas such as the airlines industry, telecommunications, oil and gas prices, and brokerage rates, but probably little prospect for de-regulation in areas such as trucking and taxi regulation, agricultural marketing boards and the professions. In these latter areas there are few highly concentrated economic interests with a major stake in change, and no major spillovers at present from de-regulation in the United States or other interconnected markets which might dictate change in order to preserve Canada's competitive position. In short, it is doubtful that much de-regulation of any consequence is likely to occur in Canada in the foreseeable future. Indeed, the federal government's espousal of its National Energy Program and massive corporate bail-outs of, for example, Chrysler Canada, Massey Ferguson, Dome Petroleum and Maislin Trucking, appear, if anything, to signal a new level of interventionism in federal economic policy making.

---

<sup>22</sup> See generally, Becker, *A Theory of Political Behaviour*, Univ. of Toronto Law and Econ. Workshop, Oct. 22, 1981.

<sup>23</sup> *The Prospects for Regulatory Reform in Canada: Political Models and the American Experience* (1982), 20 Osgoode Hall L.J. 676.

#### IV. CHANGING THE POLITICAL PLAYERS

Two major sets of recent reform proposals attempt to address directly the political dynamics surrounding regulatory policy making by proposing changes in the configuration of political players in the process. One set of proposals would attempt to neutralize certain classes of players and thus remove them from the game. These proposals relate to the compensation of losers from proposed regulatory change. Another set of proposals would attempt to inject certain classes of players more forcefully into the game. These proposals relate to the public subsidization of the political activities of thinly-spread interest groups ("public interest groups"). Both sets of proposals are reviewed below.

##### A. *Compensating Losers from Regulatory Change*<sup>24</sup>

In a recent article,<sup>25</sup> Tullock argues, primarily with reference to the example of de-regulation of the United States airline industry, that efficiency, equity and political considerations all support a case for compensating the losers or perceived losers from de-regulation. From an efficiency perspective, by requiring that losers be compensated, we ensure that a regulatory change will go forward only if the total of its benefits exceeds the total of its costs; that is, that such a change would be made only if it would increase social welfare. From an ethical perspective, because regulatory reform imposes a burden on some people (who in all good faith may have adjusted their lives or investments to a set of government policies) in order to serve the public interest, compensation may be in order to ensure that the cost is more widely shared. From a political or public choice perspective, compensation of losers from regulatory reforms may be a necessary prerequisite to overcoming their political opposition to the changes. Thus, by "buying off" the losers, a welfare-maximizing move that might otherwise have been politically blocked becomes possible.

Thurow, in a recent book, *The Zero Sum Society*,<sup>26</sup> argues in a similar vein: if we want a more dynamic economy, then those who suffer localized costs that generate universal benefits should be generously compensated in order to remove their opposition to the adoption of such policies. Schultze also argues<sup>27</sup> that public policy makers should, in the future, pay much more attention to developing compensation arrangements that mitigate transition costs of government policies so that cost bearers are not induced to distort or deflect these policies. Buchanan,<sup>28</sup> adopting a more radical position, argues for a new constitutional compact that would constrain the functions of government to welfare-maximizing (rather than redistributive) policies and suggests a one-time buy-out of the recipients of benefits from non-welfare maximizing policies through compensation arrangements designed to secure their endorsement of a new social contract. Tullock concludes his argument for compensation by asserting:

---

<sup>24</sup> This section of the article is drawn from Quinn and Trebilcock, *Compensation, Transition Costs and Regulatory Change* (Ottawa: Econ. Council of Can., 1981).

<sup>25</sup> Tullock, "Achieving Re-regulation: A Public Choice Perspective" *Regulation Magazine*, Nov./Dec. 1978.

<sup>26</sup> (New York: Basic Books, 1980). See especially c. 8.

<sup>27</sup> *The Public Use of Private Interest* (Washington: Brookings Institution, 1977). c. 5.

<sup>28</sup> *The Limits of Liberty* (Chicago: Univ. of Chi. Press, 1975) c. 10.

We have a coincidence of efficiency, ethical, and practical arguments, all pointing toward the same action. All of this may seem too good to be true. That St. Francis of Assisi, Boss Tweed, and a board composed of the last three winners of the Nobel prize in economics would all advise the same course of action is both good and true.<sup>29</sup>

It is proposed, in these comments, to confine the analysis to the political virtues of an expansive compensation principle.

Despite the view of Tullock and others that *explicit* compensation of losers from regulatory change is good politics, in fact, very little of it is happening. Why is this? Are politicians and other policy makers incorrigibly stupid or is there rationality in their apparent resistance to the concept? In order not to overstate the thesis of this article, it is probably important at this juncture to acknowledge the difficulty of distinguishing implicit from explicit compensation arrangements. Political markets already widely deploy implicit compensatory tendencies in that the distributional effects of a series of functionally unrelated collective decisions may tend to offset each other. This occurs as a result of an ongoing process of political accommodation in which log-rolling plays a central role. Forms of compensation which are more functionally related to the losses to which they are responsive are also to be commonly observed, even though they may fall short of direct lump sum cash payments. For example, manpower retraining programmes, job placement services, community relocation programmes, regional development grants to firms willing to locate in depressed areas, subsidization of infra structure development in such areas, may all, depending on the circumstances, be designed to cushion or offset the costs associated with a change in government policy that affects the economic health of a community or industry (for example reduction of the level of tariff protection of a regionally based industry).

Similarly, the tying of the scale of unemployment insurance benefits to the rate of unemployment in a region, as the *Unemployment Insurance Act*<sup>30</sup> provides, can be viewed in the same way, especially if unemployment can be considered as the unavoidable and thus foreseen cost of certain government stabilization policies. Postponed implementation of a policy change may also be conceived of as a form of at least partial compensation to eventual losers from the change, as can "grandfathering" in the form of exemptions from rule changes for individuals and firms that had operated under the old rules. In-kind compensation, such as the provision of state or subsidized housing to people forced to move by, for instance, highway construction, may come closer to explicit compensation. Compensation through tax concessions (tax expenditures), such as the granting of deductions to firms in respect of the cost of complying with particular government regulations, such as environmental regulations, may be closer still.

The point to be made here is that the compensatory responses of our political system to losses generated by regulatory changes must be seen as arrayed along a wide continuum from highly implicit forms of "compensation"

---

<sup>29</sup> *Supra* note 25, at 541.

<sup>30</sup> S.C. 1970-71-72, c. 63, s. 37.

(not functionally, but perhaps politically), related to losses a group has suffered from a particular action; to forms of compensation which are functionally related to the losses in question but remain to varying degrees implicit; to explicit lump sum cash payments directly and functionally related to particular kinds of losses.

Tullock appears to argue that the political system makes insufficient use of this last form of compensation, especially in a de-regulation context. Observably, implicit forms of compensation are widely deployed, at least in other contexts. Why then are explicit forms of compensation not more widely used to facilitate welfare maximizing forms of de-regulation? This question will be addressed by analyzing the incentive structures of the principal classes of actors in the political marketplace who may be affected by a compensation policy.

### 1. Losers: Compensation Recipients

Where the prospective losers from a regulatory change face a choice between accepting direct compensation or opposing the change it would often seem rational for them to adopt the second strategy. Consider, for example, a proposal to reduce the tariff protection of a regionally based industry, such as textiles. Owners of textile factories, employees and their families, local businesses and social organizations may be amongst those who will suffer losses if the economic base of the region contracts.

Employees of textile factories, in deciding whether to accept compensation payments for foregone wages in lieu of opposing the change, face an extremely difficult calculus:

- a) Does the offered payment fully reflect all wages that will be foregone before alternative employment can be found?
- b) Does the offered payment fully reflect foregone non-monetary job satisfactions?
- c) Does the offered payment fully reflect non-job economic losses such as losses that may be sustained on the sale of their homes or additional costs that may be incurred in acquiring comparable accommodation in some other area?
- d) Does the offered payment fully compensate for losses of various amenity values and disruptions to family and social relationships?
- e) To the extent that the payments offered assume other action by the government to cushion the costs of change (for example, phasing out of the industry over time, phasing in of support for a new industry in the area), with what confidence can politicians' commitments on these matters be treated and how certain are the benefits assuming these commitments are acted on?

Given the substantial uncertainties that surround all of these, and probably other, questions, it may well be rational for employees to take the position that investing resources in lobbying for the maintenance of the *status quo* may yield bigger pay-offs than accepting a lump sum payment (unless this payment is extremely generous to compensate for the uncertainties involved).

Suppose the government, in order to allay some of the concerns engendered by the above questions, commits itself to compensating for actual losses on an ongoing basis. First, from the perspective of the recipients of this commitment, a measure of uncertainty surrounds the question of how much to discount the reliability of promises by politicians of future actions. Even assuming utmost good faith, there will be uncertainty as to how particular losses will be measured in the course of future administration of the policy. Second, and more important perhaps, making compensation payments contingent on proof of actual losses creates strong incentives for the recipients to magnify the losses; for example, by remaining unemployed for longer than necessary, or by selling homes at under-value. Efficiency losses, including the monitoring costs of attempting to contain these effects, might well be substantial. Thus, the long-run political viability of a programme of case-by-case compensation of actual losses is doubtful.

## 2. Gainers: Compensation Underwriters

Will the persons or interests who are asked to bear the costs of compensation, even assuming they are also the same persons or interests who stand to gain (and let us assume further, gain more) from the proposed regulatory change, find a compensation principle congenial?

At one level, it is obvious that the gainers would prefer to obtain their gains for nothing rather than to pay for them. But suppose the gainers understand that unless compensation is forthcoming the regulatory change from which the gains derive will not be forthcoming. Will they support a compensation arrangement which they themselves underwrite? Much may depend on how the compensation is arranged. If the gainers are required to make lump sum payments to the losers at the outset of the regulatory change, they may be bearing substantial costs of uncertainty. They face a certain cost (in terms of the compensation payments required) in return for the prospect of uncertain future benefits. One possibility is that both the costs and benefits of the policy change to the gainers could be deferred, for example, by the general body of taxpayers underwriting the initial compensation costs, with these costs recouped from future purchasers of the product or service in question through some form of tax. In this case, however, the general body of taxpayers will perceive an immediate and certain impost in return for a commitment of uncertain reliability to recoup the expenditure in the future. Moreover, the process of recoupment may engender misallocative effects of the kind that the policy change is designed to remove.

## 3. Politicians

It is assumed here, as well as by many other commentators elsewhere (Tullock being prominent among them), that politicians are motivated by vote-maximization objectives in choosing policies. In general, this will entail choosing policies that: a) confer benefits on marginal voters while imposing costs on infra-marginal voters, and; b) given information imperfections in the political marketplace, confer benefits on marginal voters in highly visible form while disguising the costs from other marginal voters to the extent the latter are cost-bearers. In other words, a strategy of "magnifying the gain while disguising the pain" is a politically rational approach to policy choice.

The implications of this strategy in the present regulatory context suggests a general political predisposition against explicit compensation arrangements. Explicit compensation for losses associated with a new policy, for example, deregulation, renders the cost of that policy extremely visible without necessarily making the benefits of the policy any more visible. Under a compensation principle of the kind being considered here, the losers from the new policy are at best left indifferent to the policy as a result of compensation. At worst, for reasons earlier canvassed, the losers may remain strongly opposed to the policy. This opposition from the losers will have to be weighed politically against the support of the beneficiaries of the policy. If the benefits are both widely dispersed and substantially deferred, it is not clear that the support for the policy will countervail the opposition to it.

Depending on how the compensation is financed, the underwriters of the compensation scheme may represent another source of opposition. The more explicit, and hence the more visible the compensation arrangements, the more strenuous the opposition from the underwriters of the compensation is likely to be. In order to contain opposition to a new policy from these sources, politicians will face strong incentives to disguise the compensation payments from them, perhaps by deploying implicit rather than explicit forms of compensation.

A more general factor tending in the same direction, at least in a deregulation context, is the costliness to politicians of acknowledging past mistakes. Very explicit forms of compensation to losers from the withdrawal of a prior regulatory programme may be, or may be perceived to be, a clear acknowledgement of fallibility; costs, in terms of political credibility and confidence, that extend beyond the parties immediately affected by the change in policy, may also be incurred.

All these doubts about the political returns from an explicit compensation principle must be viewed in the broader context of alternative expenditure choices that are available to politicians. If, through a highly visible expenditure policy in some other context, greater political returns can be realized, it would be politically rational to prefer this other policy. Given budget constraints and the unavailability of such choices, it would not be surprising if politicians generally concluded that public expenditure programmes could more profitably be directed to ends other than underwriting compensation schemes for losers from regulatory reform. Moreover, even if compensation of losers from regulatory reform were to be politically rational, it certainly does not follow that it would be politically rational to pay full compensation for all losers. The political calculus would only require that sufficient compensation be paid to strategically placed losers to defuse their political opposition to the point where further compensation would yield no further marginal political returns.

#### 4. Bureaucrats

It is difficult to see why bureaucrats would, in general, be strong supporters of proposals to terminate regulatory programmes given the reduction in bureaucratic inputs typically involved in programme termination. Only if bureaucrats themselves were included in compensation arrangements might



they become indifferent to the change. But in this instance, as with other recipients of compensation, they are likely to be left bearing substantial costs of uncertainty (unless the compensation arrangements are made extremely generous to offset these costs).

Bureaucrats, like politicians, will view the compensation issue in the light of all other policy choices open to them. Would an expenditure of a portion of a bureau's budget on compensating losers be as attractive as expenditures on any other possible programme or policy? While the incentive structures of bureaucrats are far from clear, other programmes or policies would often seem to yield higher returns in terms of power, pay and prestige, to the extent that these factors are important in a bureaucrat's utility function. Moreover, explicit compensation arrangements directed to the termination of an existing regulatory policy or programme may be perceived by politicians, media and voters as signalling a prior mistake in policy on the part of the bureaucracy in question. Because of the greater permanence of bureaucrats relative to politicians, this perception may be more costly to the former than the latter in terms of career ambitions. Thus, if compensation is to be made at all, one would expect bureaucracies to favour implicit rather than explicit forms of compensation.

These factors suggest that bureaucrats would generally tend to be predisposed against compensation proposals for de-regulation. Where these are a political given, however, these factors would suggest that bureaucrats would tend to favour compensation arrangements that attach substantial weight to their own interests both in terms of ensuring personal coverage and in terms of high degrees of implicitness.

With respect to compensation and political pragmatism, it was suggested that the recipients of explicit compensation might not, on that account, be rendered indifferent to regulatory change, if the compensation arrangements impose substantial costs of uncertainty on them. Only extremely generous payments are likely to render losers indifferent to these costs. On the other hand, ongoing compensation payments, designed to underwrite actual losses, are also likely to increase substantially the amount of compensation involved. The payers of compensation — presumably the gainers from the regulatory change — may well cease to be a strong political constituency for the change if the compensation arrangement substantially attenuates the net benefits from the reform. Politicians, in deciding whether to support the payment of explicit compensation to the losers from regulatory change, will find it rational to ask whether the expenditure of resources elsewhere is likely to yield higher political returns. In very few cases, it is suggested, will explicit compensation be a rational policy for politicians to pursue. Experience appears to bear out this hypothesis.

#### B. *Funding Public Interest Groups*<sup>31</sup>

If one takes the view of collective decision-making advanced here, then public policy making is not a technocratic, consensus-based exercise seeking to

---

<sup>31</sup> This part of the article is derived from Engelhart and Trebilcock, *Public Participation in the Regulatory Process: The Issue of Funding* (Ottawa: Econ. Council of Can., 1981).

respond only to economists' notions of market failure. Rather, it is a value-laden, conflict-ridden process of inter-group political mediation. In such a process, it seems clear that political interests that do not participate actively in efforts to influence the mediators (or other voters whose preferences may be material to the mediators) are likely to be heavily discounted in policy outcomes.

The term "public interest group", while well sanctioned by usage, is unfortunate to the extent that it implies some special claim on virtue. It is not used here with this connotation. Instead, the term is used to refer to groups with very diffuse memberships where the aggregate interest of a group in an issue may be very substantial but the interest is thinly spread over a large number of members whose individual stakes in the interest may be very small. For example, consumers of telephone services may have a large aggregate interest in resisting an unjustified rate increase but small individual interests to the same effect. On the other hand, the telephone company has a highly concentrated interest in securing the rate increase. In situations involving highly concentrated interests on one side and thinly spread interests on the other, representational imbalances are almost inevitable. Two factors principally explain this — transaction costs and free riders.

The costs to thinly spread interest groups of communicating with members, soliciting contributions, and maintaining group solidarity are very high relative to similar transaction costs faced by highly concentrated interest groups in organizing themselves. If a consumer of telephone services stands to be prejudiced to the extent of five dollars *per annum* by an unjustified rate increase, this implied ceiling on any contribution that he is prepared to make to group efforts to resist the increase may be largely or wholly offset by the costs of soliciting his membership.

The other major organizational disability of public interest groups is the free-rider problem. By not contributing to a group which shares his interests, an individual may be no worse off than if he had joined, in terms of his ability to share in the gains from group activity, and he will have saved his contribution. This is not nearly as severe a problem with concentrated groups because their members' efforts are highly interdependent. Failure by one member to contribute his share to the group's needs may easily jeopardize (and be perceived as jeopardizing) the entire group enterprise.

Engelhart and Trebilcock<sup>32</sup> argue that subsidization of representational efforts by public interest groups must be analyzed and prescribed for in two separate but related contexts. First, there is a need to ensure adequate representation of public interest groups in the shaping of policy within the bureaucracy, amongst politicians and before legislative committees, Royal Commissions and the like. Second, there is a need to ensure adequate representation of public interest groups in formal regulatory proceedings. As a general proposition, participation in the first set of governmental activities poses fewer costs for such groups than participation in the second set. Influencing policy at the legislative stage often entails lower information and organization costs for interest groups as the issues are often more visible and the course of decision-making less protracted and less resource intensive than in formal regulatory decision-making.

---

<sup>32</sup> *Id.*

With respect to general representational activities (the first class of cases) two broad options in the way of funding approaches might be considered. The first entails direct government grants to groups engaged in representational activities. For example, the Federal Department of Consumer and Corporate Affairs now allocates almost one million dollars a year to consumer groups, a significant portion of which is spent on representational activities. Although one could contemplate development of a more ambitious group grants program, fundamental difficulties confront this approach.

First, there are real dangers that the political independence of groups so funded will be compromised by dependence on the continuing goodwill of the government in sustaining them. Second (and related), a full diversity of viewpoints reflecting major thinly spread interests may not be encouraged by this mechanism. Heavily centralized administration of the program, and the danger that the government will only be disposed to fund those groups with views congenial to it, may truncate representation of all major public interest groups. Third, because group grants are allocated to organizations and their representatives (and not to individual members), it is difficult to ensure that funds are spent by organizations to represent their members' views rather than those of the alleged representatives. In other words, constituency accountability is attenuated under this form of funding. These disadvantages of direct group grants lead to consideration of a second broad option for subsidizing general representational activities by public interest groups — a tax incentive approach.

A system using this approach, for example by providing tax credits for membership contributions, would have a number of advantages. The first would be *accountability*. Each donor in effect would get a vote. Those groups that are best able to satisfy the preferences of the largest number of people will get the most funding. Groups who are not in fact representing the wishes of their constituency will see their sources of funding depleted. In this way, public interest groups will be forced to represent the views of their client groups.

At the same time this mechanism would allow for the representation of a *diversity* of views. A group may, for example, espouse the views of a small percentage of the population on environmental or consumer matters. However, this small proportion of the population will be represented to the extent that their aggregate tax credited contributions allow. With other funding mechanisms these less widely held views may not be represented at all.

Further, this mechanism should allow public interest groups more *independence* than would any other mechanism. With direct government grants, the granting authority can vary the amount of funds granted according to very subjective criteria. Especially zealous groups could be classified as "ineffective" or "irresponsible" and would then lose funds. With the tax credit system, the granting authority cannot vary the amount of funds; it can only decide on the eligibility of the organization. The process by which eligibility is judged can be determined in a fairly objective manner, with appropriate grounds of appeal to the courts.

The tax credit system also fosters *internal efficiency*. The more efficient public interest organizations will be able to use their resources to undertake more and better representational efforts on behalf of their client groups than

will less efficient groups. This will win them the support of additional clients and hence these organizations will attract still more funds.

In short, the tax credit system would increase the political influence of members of thinly spread political constituencies by raising the profile of issues with them through competition amongst interest groups for their support and through the greater information likely to be made available to them about these issues through this competitive process. The enhanced political effectiveness of interest groups representing these constituencies, as a result of the tax credit scheme, must ultimately rest on the prospect of enhanced political awareness and mobilization of individual members of these constituencies *qua* voters.

The principal concerns with a tax incentive approach would seem to be three-fold. First, because taxpayers would have to invest resources (time and energy) in evaluating the platforms of groups competing for their subsidized contributions, a tendency may develop to minimize these costs by allocating tax-credit contributions to highly emotive single issue groups, rather than those representing public interest perspectives in more complex regulatory settings. Second, in the case of public interest groups representing interests without taxable income (for example, welfare recipients), the tax credit approach would have little merit. While technically it would be possible to provide a subsidy through the tax system in these cases (as is presently done, for example, with the child tax credit), the administrative costs of processing the additional returns and making the refunds may outweigh any merit in extending the proposal to these groups. Perhaps a form of matching grant system could be considered instead. Third, compared to direct grants, the one dimension where a tax credit scheme may compare unfavourably is with respect to administrative cost. A tax credit scheme may entail the allocation of substantial resources to the investigation of claims by groups applying for public interest group status as a prelude to registration, the issuance of appropriate receipts by groups to members, the monitoring by the tax authorities to ensure that revenues are in fact being spent on representational activities and the validation of membership receipts submitted with tax returns. These cumulative costs are unlikely to be trivial and may make this a high cost form of subsidy.

To meet the case for subsidizing public interest groups through a tax credit scheme, consideration might be given to adapting and extending the present tax treatment of contributions made to political parties.<sup>33</sup> Tax credits for contributions to federal political parties equal: seventy-five percent for the first \$100, fifty percent for the next \$450, and thirty-three and one-third percent for the excess over \$500, with a maximum credit of \$500. These tax credits for donations to political parties became effective in 1974. The Chief Electoral Officer reports that in 1979, 111,632 individuals contributed to the three federal political parties, a forty-eight percent increase in individual donations over five years.<sup>34</sup> The Department of National Revenue reports that for the 1978 taxation year, the tax credits for all political donations (individual and

---

<sup>33</sup> *Income Tax Act*, S.C. 1970-71-72, c. 63, as am. by S.C. 1976-77, c. 4, s. 52(2).

<sup>34</sup> *The Globe and Mail* (Toronto), Nov. 29, 1980 at 1, col. 4.

corporate) to federal parties involved foregone taxes of \$3,973,000.<sup>35</sup> In the present context one might envisage a tax credit of, say, seventy-five percent of individual membership contributions to public interest groups, applied to a maximum of forty dollars in contributions per person per year. Such a credit would direct subsidies principally to broadly based, thinly spread interest groups.

In order to operationalize such a scheme several concerns would need to be resolved. First and foremost, a definition of the groups that would qualify for registration as public interest groups would have to be formulated. The most expansive approach would be to treat as qualified those groups spending a large portion, say eighty percent or more of their revenues (analogous to the present rule applicable to charities) on representational activities before government or any of its agencies. "Representational activities" and "government and any of its agencies" would in turn need to be defined, but expansive definitions could be fairly readily formulated. Perhaps a minimum group membership, for example, one hundred, might be required. Groups otherwise satisfying the above definitions would not qualify for the credit if membership fees or contributions are already deductible as a business expense. This requirement would effectively disqualify producer interests from claiming this subsidy. As well, a group would not qualify if it is a "registered charity" or a "registered political party". Notwithstanding these various definitional difficulties, a tax credit scheme compares favourably with all alternative funding mechanisms, including direct government group grants, in terms of the criteria of independence, accountability and diversity.

In order to recognize the special resource demands that participation in formal regulatory proceedings places on public interest groups, the tax incentive proposals might be supplemented by expanding the powers vested in individual regulatory agencies to award costs on an *ad hoc* basis. These powers would enable agencies to award interim and final costs in favour of public interest groups and against regulated industries in adjudicative proceedings, similar to what is presently envisaged by the Canadian Radio-Television and Telecommunications Commission (CRTC) in its costs procedures. As well, major federal and provincial agencies might be given explicit budget increments to fund public interest group participation in rule-making and similar proceedings.

These proposals are complementary. In the event that some agencies do not exercise their cost powers with appropriate sensitivity to the need to promote representation of thinly spread interests, the availability of base funding for some groups through a tax credit program will mitigate the consequences. To the extent that a tax credit program does not well accommodate new groups or groups organized around discrete or time-specific issues, *ad hoc* cost awards provide at least the potential for assistance in formal regulatory proceedings.

A political system that is predicated upon an equal distribution of voting entitlements cannot easily justify present inequalities in the distribution of access to non-vote forms of political and regulatory influence. Proposals of the

---

<sup>35</sup> Verbal communication of the Department of National Revenue.

kind outlined above seem responsive to these inequalities. These proposals won the endorsement of the Economic Council in its final report<sup>36</sup> following an acknowledgement in its interim report that “funding for ‘public interest groups’ must be considered as an essential component of regulatory reform.”<sup>37</sup> Given the high priority attached by the Council in both its reports to the need for funding public interest groups, what are the political prospects for reforms in this area?

There seem to be reasonably good prospects that the procedures recently introduced by the CRTC for awarding costs to public interest groups and against regulated industries in adjudicative hearings will be extended to other federal agencies. Relatively small amounts of money tend to be involved in these awards, and the approval procedures are likely to ensure that typically only well established, ideologically “mainstream” groups will qualify for awards. Moreover, cost awards, by definition, are confined to a regulatory context and do not facilitate lobbying in a wider political context. This major constraint is likely to reduce significantly political opposition to such a policy. In terms of general representational funding, prospects do not look nearly as bright. It would be surprising if government was prepared to abandon its present small program of direct grants to public interest groups, with its concomitant control over the nature of the groups supported, amount and direction of expenditures, in favour of a relatively automatic form of subsidization such as implied by the tax credit proposal outlined above. Here, the government relinquishes control over which groups get supported to do what, thus risking alienating concentrated interests faced with new antagonists, and moreover is likely to receive less political appreciation from groups receiving financial support from a tax credit scheme, given its relatively non-discretionary nature.

What seems clear is that any substantial expansion in the funding of public interest groups to facilitate their advocacy role in collective decision-making will be bitterly resisted by established interests. Unfortunately, the interest which might stand to gain most from financing reforms are precisely those interests that, in the absence of such changes, are likely to have no effective means of promoting them.

In the spring of 1978, Mr. de Grandpré, Chairman of Bell Canada, wrote to the President of the Treasury Board complaining that the Minister of Consumer and Corporate Affairs, in funding several public interest intervenors to the extent of \$108,000 at an earlier Bell rate hearing, was guilty of “a dilapidation of public funds [which] floods the carburetor and shows he has no control over his department’s expenses.”<sup>38</sup> Mr. de Grandpré did not also point out that, for example, in the 1978 Bell rate hearing, Bell Canada Limited is estimated to have spent \$1,250,000 in direct costs nor that these costs are both a tax deductible cost of doing business and an allowable expense that can be passed on to consumers in new rates. Moreover, these direct costs do not include the cost of maintaining a permanent rate department within the com-

---

<sup>36</sup> *Reforming Regulation*, *supra* note 15, at 134-36.

<sup>37</sup> *Responsible Regulation*, *supra* note 15, at 82.

<sup>38</sup> Cited in Engelhart and Trebilcock, *supra* note 31, at 149.

pany or various other support facilities. It is not clear what Mr. de Grandpré would consider an appropriate deployment of representational resources by public interest groups in this context. Apparently publicly subsidized advocacy of producer interests is justifiable; publicly subsidized advocacy of consumer and other personal interests is politically irresponsible. The uncontested political margins seem extremely thin.

## V. ENHANCING THE INFORMATION BASE FOR PUBLIC POLICY DECISIONS

In the *Interim Report* it is recommended at several places that regulatory programmes be systematically evaluated both before and after implementation. The summary statement, and an important *caveat*, read as follows:

The Council believes that three fundamental benefits could be expected from systematic evaluation of regulatory programs: clarification of accountability of both elected and appointed officials in the operation of the programs; improvement in the efficiency and effectiveness of the programs; and fostering of informed regulatory decision making through the provision of more information concerning the existing impact of the programs.

Central to both prior assessment and periodic evaluation will be the use of cost-benefit analysis. The Council recognizes the difficulty of applying this technique of economic analysis to issues that are not entirely economic in nature. We see cost-benefit analysis as a useful, albeit limited, tool that can serve as an aid to rational decision making. We have no illusions that this analytical technique can accurately assess minor or subtle differences. Cost-benefit analysis, however, is capable of identifying significant differences between costs and benefits, differences that should be considered by decision makers when evaluating new regulations or existing regulatory programs.

Cost-benefit analysis can, of course, be misused. The numbers derived are estimates and are subject to dispute among equally competent analysts. Not all relevant costs and benefits, in the broadest sense, can be incorporated into the calculations. Intangibles are particularly hard to deal with. While recognizing its limitations, we are, nonetheless, convinced that cost-benefit analysis should be utilized to aid and extend the intuition and judgment of public decision makers in the field of regulation.<sup>39</sup>

Executive order 12291 issued on February 17, 1981 by the United States Office of Management and Budget (OMB) requires the use of cost-benefit analysis in most regulatory decisions. The main elements of that Order (subject to explicit provisions to the contrary in existing statutes) can be summarized thusly:

Agencies must apply cost-benefit analysis to all their rulemaking and adopt the least costly regulatory alternative.

In the case of "major" rules [a defined term] agencies must publish, along with their proposed and final rules, preliminary and final regulatory impact analyses that set forth their conclusions regarding the cost-benefit balance and feasible alternatives. They must also submit these analyses and the rules to OMB before publication and consult with OMB regarding them if so requested.

Agencies must review rules currently in effect and prepare regulatory impact analyses for those that are major.

---

<sup>39</sup> *Responsible Regulation*, *supra* note 15, at 72.

OMB is authorized to issue guidelines and standards for operation under the order (including standards for the development of regulatory impact analyses); to require agencies to obtain and evaluate additional data; to designate any rule as a major rule; and to schedule existing rules for agency review.<sup>40</sup>

The difference between the recommended Canadian approach and the American Executive Order is stark. The former recognizes that evaluation (at least with cost-benefit analysis) only deals with one dimension of concern and is subject to limitations even on its own terms. The latter is unqualified except for the necessary recognition that existing statutory provisions are overriding. Needless to say, the position taken here is that both of the Council's qualifications are important for reasons which will be explained briefly. To oppose a call for more information and analysis is repugnant assuming the costs do not outweigh the potential benefits — an issue that can only be resolved on a case-by-case basis. One can question in general terms, however, the likelihood that evaluative information will bestow the benefits the Council apparently anticipates.

Correcting or offsetting market failures, in order to move the economy closer to Pareto optimality (that is, achieve greater output through greater economic efficiency), is the principal economic rationale for any type of government intervention. Cost-benefit analysis is the analytic tool devised to assess whether a policy decision would, on balance, increase or decrease efficiency. It follows, therefore, that those espousing efficiency must also espouse the assessment of alternative regulatory and other interventions on this basis. Only when intervention would produce a net benefit is it desirable: the form of intervention that produces the largest net benefit obviously should be selected.

Even the economists' enthusiasm for cost-benefit analysis, however, is tempered by two considerations:<sup>41</sup>

- a) Neither major policy changes that would significantly affect relative prices, nor situations where there are unemployed resources involved can be evaluated by this partial equilibrium technique. Further, there are many other technical limitations.<sup>42</sup>
- b) Although certainly the efficiency criteria is central to much microeconomics this is *not* to assert that distributional and other objectives are unimportant. The "appropriate" weight to be attached to the efficiency goal is *not* an economic question.

The conceptual world of economics is divided into two aspects: the allocative efficiency aspect and the distributional (income-wealth) aspect. Although not logically entailed, with one possible exception, the call for a greater emphasis on the goal of efficiency can usually be taken as a call for a reduced emphasis on a distributive goal or goals. The exception arises from the possibility that some regulations are simply wasteful of resources (create "x in-

---

<sup>40</sup> *Regulation*, Mar./Apr. 1981 at 14.

<sup>41</sup> See *Responsible Regulation*, *supra* note 15, at 72 for references discussing some of the problems.

<sup>42</sup> See Tuohy, *Regulation and Scientific Complexity: Decision Rules and Processes in the Occupational Health Arena* (1982), 20 Osgoode Hall L.J. 562.



efficiencies"). In these instances, greater efficiency could, by definition, be achieved by eliminating the waste without sacrificing distributional goals. A needlessly great "paper burden" would be an example. Assuming a fully employed economy where make-work projects are unnecessary, the removal of waste would probably have well nigh unanimous support. It is not unreasonable to speculate, however, that for many the antipathy towards regulation is, at least in part, antipathy towards the redistributive effects of many regulations. Critics are probably of the view that redistributive objectives have been surreptitiously pursued by means of regulations that had as their supposed purpose the correction of market imperfections. Trebilcock, Waverman and Prichard,<sup>43</sup> citing numerous authorities, argue as follows:

Plausible rationalizations for regulatory interventions in private markets in order to eliminate market failures were presented. . . . However . . . an analysis of a limited number of actual forms of intervention indicate that eliminating market failures does not appear to be the sole or even primary motivation. Studies of the *total* effect on economic efficiency of various regulatory regimes indicate that social welfare is reduced not increased in many cases.<sup>44</sup>

Unless one has reason to believe that the underlying "motivation" has changed, there seems to be little reason to believe that it will be easily suppressed simply to accommodate those who are enthusiastic about greater economic efficiency. As discussed at the beginning of this article, the concept of economic efficiency is essentially a normative standard. It is that state of affairs in which no one can be made materially better off without someone else being made worse off. Inefficiency is therefore some unspecified output forgone by one or more unspecified individuals. To be opposed to greater efficiency, which by definition is costless, would be strange. But to be strongly in favour of it would also be strange because of the complete ambiguity concerning who will enjoy the benefits. Further, if voters have little reason to press for greater efficiency, politicians seeking election or re-election are also most unlikely to be enthusiastic about this highly abstract goal.

Economic efficiency has many of the attributes of a public good. Each person living in a prosperous nation (although not necessarily personally prosperous) can enjoy the benefits thereof without reducing the enjoyment of it by others. It is tempting to add that those who do not pay to achieve this state of prosperity cannot be denied access to the benefits it bestows, for this is the second half of the definition of a public good. However, by definition, greater efficiency is costless. As stated earlier, the losers, if any, from a policy change must be compensated if one is to be sure that the change will increase efficiency. This means that, because the act of compensation itself is not costless, the potential gain from a change must exceed not only the total amount to be paid in compensation, but the transaction costs too. As discussed in Part IV A, transaction costs are likely to be extremely large where compensation is involved. Every economy must therefore operate at a suboptimal level, at least to the extent that the transaction costs involved in moving it to optimality are greater than the benefits that would be realized by so doing.

---

<sup>43</sup> "Markets for Regulation" in *Government Regulation* (Toronto: Ont. Econ. Council, 1978) at 11.

<sup>44</sup> *Id.* at 28.

The political point is that, in the competition for votes, each political party will, of course, promise the greatest prosperity (economic efficiency). The winning party, however, will have to appeal primarily to the marginal voters in the marginal ridings. There is every reason to believe that most voters would accept additional targeted benefits for themselves, even if this means a further general reduction in efficiency, with the costs spread throughout the economy. The winner's "share" of these costs would be trivial. Indeed, in a growing economy, reductions in efficiency are not likely to be perceived. The growth foregone is "out of sight" and therefore "out of mind".

Because the costs of inefficient policies are very diffuse, their imposition is not likely to have a material impact on the voting decisions of marginal voters. Presumably the removal of the costs would not gain much political support either. The marginal voters who had the offending benefit would certainly be aware of their loss, however. This leads to the question of voter information.

The call for the use of cost-benefit analysis as the principal decision rule could conceivably be based on the belief that some inefficient regulations are adopted because of ignorance. This could be the ignorance of the decision makers themselves or ignorance on the part of the public concerning the full costs of some regulations. The latter interpretation seems more plausible. No doubt many losers under agricultural marketing regulations, for example, were and are unaware of the significance of those regulations. Had they been aware of the higher costs they might have to bear, there surely would have been more opposition to their adoption. It would be naive to think, however, that such opposition would have been a decisive consideration.

It is likely that more marginal votes were won in marginal rural constituencies than were lost in marginal urban constituencies. For the former, the political gains were dramatic. For the latter, the costs were spread so widely, and hence so thinly, that their significance was reduced to the point where they were not a decisive consideration. In addition, marketing regulations are of such great potential import to farmers that, despite their large numbers, organizations have been formed to press for the requisite legislation. No doubt these farm organizations are confronted with "free rider" problems. Nevertheless, their organizational problems are insignificant compared with the impossible task of organizing a protest group comprising all consumers of agricultural products.

It is conceded that with more and better cost-benefit information in the public domain, there would have been more opposition from potential losers. Perhaps some regulations would not have been implemented or would have been implemented in a different form. Nevertheless, it is vitally important to recognize that there are available, to a substantial extent, alternative policy instruments that can be used to accomplish efficiency as well as redistributive purposes. Tax expenditures and direct expenditures are two obvious alternatives. There is little to be gained by blocking regulations that do not meet the efficiency criterion if alternative means are open that are not subject to the same analyses and public scrutiny. Yet, if all policy changes were required to be justified on cost-benefit grounds, is it not plausible to suggest that rational ignorance would prevail? How could voters keep reasonably informed in the face of such a barrage of complex studies?

The ambiguities and limitations inherent in cost-benefit analysis pose another problem that those pressing for application of the technique to regulations seem to overlook. The cost-benefit enthusiasts, including Reagan Administration officials, assume that the results are more definitive than they often are or that they will not be subject to question in a highly adversarial process or both. Because conflicting interests are almost invariably involved in any regulation, competing analyses are bound to be introduced. Expert witnesses for the contending parties will give contradictory opinions. All limitations and ambiguities inherent in the methodology will be exposed by one side or the other in an attempt to discredit the results. To illustrate, consider, for example, the ridicule that could be heaped upon any particular rate of discount assumed: is it the private rate, and if so, which one; or is it the government rate? Other limitations and ambiguities include estimates of social costs and benefits where market prices are not available (for example, the value of a human life), the assumption that relative prices are unchanged and the assumption that wealth effects are trivial. The list goes on.<sup>45</sup> It will frequently be the case that the degree of disagreement among the experts is sufficiently great that the "optimal" choice of regulatory instrument will be indeterminate. It would only be necessary to discredit a few studies in the eyes of the public in order to put the legitimacy of the technique as a whole into question.

It is arguable that, if placed in the public domain, and if not too costly relative to the magnitudes of the issues at stake, more and better cost-benefit analyses of possible policy changes would be helpful in rectifying the imbalance between narrow and general interests. One would be hard put to argue, however, that the additional information would come close to offsetting the free rider and transaction cost barriers inherent in all large and amorphous groups — often the losers under economically inefficient policies.

Health and safety regulations in particular pose difficult evaluation problems because many find the notion of valuing human life and health in monetary terms nothing short of blasphemous. As a consequence, cost effectiveness techniques are sometimes proposed instead. With cost effectiveness analysis the benefit is expressed not in dollar terms but in terms of a rate of occurrence (for example, accidents per year) or level of occurrence (particles per volume). The equation is then posed in the following terms. Among the alternatives, which regulation, or set of regulations, would bring about the greatest reduction in the rate or level per dollar spent? That is, given a maximum acceptable rate or level among the alternatives, which regulation, or set of regulations, will keep the rate or level within the upper bound at minimum cost?

The application of cost effectiveness analysis, because it is neutral with respect to the appropriate level of stringency, is likely to commend itself, at least at first blush, to all reasonable men in selecting among alternative kinds and structures of regulations.<sup>46</sup> Even here, however, qualifications are in

---

<sup>45</sup> Tuohy, *supra* note 42.

<sup>46</sup> MacAvoy, "The Nondecision Cotton Dust Decision", *New York Times*, July 5, 1981 at F3. MacAvoy discusses a recent U.S. Supreme Court decision involving OSHA and cotton dust regulations. The problems of enforcement enter the picture in complex ways.

order. Cost effectiveness analyses necessarily are explicit about "feasible" total costs or about "acceptable" maximizing rates or levels (standards). Obviously, any limit on cost, or any standard below perfection, means that some probability of damage is being deemed acceptable. This in turn means that human life and health is not being taken as infinitely valuable; this is painful to admit on a public platform. Competition among parties could lead to ever higher standards or even higher cost ceilings. It is easier for politicians to be tough minded when the limits are implicit and difficult to determine. This is an instance where more information may result in more stringent or expensive regulations or both, not the converse, which presumably is not what the deregulation enthusiasts had in mind.

Becker<sup>47</sup> has argued recently that even if policy objectives are not chosen by reference to economic efficiency criteria, the competition among political parties will induce them to adopt the most *economically* efficient instruments in the pursuit of policy objectives (whatever their nature). The idea is that if there are unexploited, costless gains to be had in achieving given policy objectives at lower cost, an opposing party could offer to capture them and bestow vote-getting benefits without imposing vote-losing costs. This argument misses the mark. One would expect that the competition among the parties would produce *politically* efficient policies. There is no reason to think that political and economic efficiency are synonymous for the reasons stated above, even in relation to the choice of instrument as opposed to the choice of objective. As we have argued elsewhere,<sup>48</sup> vote maximizing politicians will subject both the choice of objective and the choice of instrument to a calculus of political efficiency. Given that almost invariably any given instrument that might be deployed in the pursuit of any given objective (that is, a politically salient set of interests) will impinge to some extent on other policy objectives (that is, politically salient interests), the choice of objective and the choice of instrument tend to become politically interdependent exercises where instruments are chosen that effect compromises between conflicting objectives that in turn maximize political support for those policies. This will typically entail choosing policy instruments that bestow benefits on marginal voters and impose costs on infra-marginal voters, as well as exploiting information asymmetries among voters in terms of their perceptions of the costs and benefits of alternative policies.

For example, in choosing pollution control instruments to achieve a given level of pollution abatement, effluent taxes, regulatory standards, and industrial subsidies will have, or will be perceived to have, very different impacts on very different interests.<sup>49</sup> An effluent tax may be strongly resisted by industry, in part because financial penalties will be incurred even with respect to cost-justified pollution, and in part because existing firms may find themselves placed at a disadvantage relative to new entrants if the latter face lower abatement costs. The general public, on the other hand, may view the benefits of an effluent tax as dubious, regarding the tax as a licence to pollute, especially

---

<sup>47</sup> *Comment* (1976), 19 J. Law & Econ. 245.

<sup>48</sup> Trebilcock, *et al.*, *The Choice of Governing Instrument* (Ottawa: Econ. Council of Can., 1981).

<sup>49</sup> Trebilcock, *et al.*, *The Choice of Governing Instrument: Some Applications* (Ottawa: Econ. Council of Can., 1981) c. 4.

given the information costs they face in understanding firms' likely responses to changes in relative prices. Regulatory standards may be appealing to the general public because of their strong symbolic connotations. Existing firms in the industry may find them attractive, especially if more stringent standards are imposed on new entrants and if the low visibility day-to-day enforcement process permits an attenuation of the standards over time. Industry subsidies to clean up will be attractive to industry but may be opposed by taxpayers who perceive their tax dollars being allocated to firms to encourage them to stop doing what they should not have been doing anyway. The choice amongst these instruments to achieve a given degree of pollution abatement is clearly more than a technocratic apolitical exercise designed to identify the least costly means of achieving a given policy objective.

## VI. ENHANCED POLITICAL ACCOUNTABILITY

Even if public interest groups became more effective, both as a result of greater public funding and the availability of evaluative information on regulations, little would be accomplished unless the government of the day could be held accountable to the elected representatives of voters and, ultimately, to the voters themselves. Reasons have already been advanced as to why a tax credit scheme subsidizing the activities of public interest groups may enhance awareness of, and sensitivity to, issues bearing on the welfare of members of these constituencies *qua* voters. However, apart from these effects, the Council in its *Interim Report*<sup>50</sup> sought to make the oversight role of Parliamentary Committees a cornerstone of its proposals for enhanced political accountability for regulatory performance by recommending that:

- a) "[A]ll evaluation reports be tabled in the legislature and be referred automatically to a legislative committee . . .";
- b) This committee "should be empowered to hold hearings, receive briefs and commission its own analytical work with respect to the regulatory evaluation reports it chooses to scrutinize in detail";
- c) "Upon completion . . . a report should be submitted to the legislature with recommendations for action".

The *Report* acknowledges the additional burden on departments and agencies that such a procedure would entail but decides that the benefits would more than cover the additional costs.

Recommendation 63 of the *Final Report*<sup>51</sup> reaffirmed this position. Subsequent to the *Interim Report* a House of Commons Special Committee on Regulatory Reform had recommended to the Government that such a permanent committee of the House be established pursuant to the *Interim Report's* proposal, pending the introduction of an overall reform of Parliament.<sup>52</sup> In November of 1979 the Clark Government tabled a set of reform proposals in the House in a document entitled "Position Paper: The Reform of Parlia-

---

<sup>50</sup> *Responsible Regulation*, *supra* note 15, at 80.

<sup>51</sup> *Reforming Regulation*, *supra* note 15, at 134.

<sup>52</sup> House of Commons Special Committee on Regulatory Reform, *Report* (Ottawa: Min. of Supply and Services Can., 1981).

ment".<sup>52a</sup> In October of the previous year the Liberal Government of the day, in the Speech from the Throne, had promised to place a proposal before the House "to provide for the review by Parliament of evaluations by the Government of major programs."<sup>53</sup> The latter was, no doubt, in response to the recommendations of the "Lambert Commission" — the Royal Commission on Financial Management and Accountability.<sup>54</sup> The Clark proposals died with that Government. The Liberals' earlier-promised change with respect to committee review of evaluations has not been implemented.

Assume, however, that the requisite changes will be made. Would they make a perceptible difference?

House committees have done useful work in the past. The Justice and Legal Affairs Sub-committee conducted an inquiry into the penal system during the Thirtieth Parliament. Its Report was widely recognized as valuable. Partisanship did not, as they usually do, rule the deliberations — presumably because all parties accept the overwhelming complexity of the problem. Disconcertingly though, it is difficult to recall other notable examples. This is not because there are only a few committees or because they meet infrequently: there is a plethora of committees that meet frequently when the House is in session. There are half a dozen Standing Committees — the Public Accounts Committee to name but one — that deal with the Estimates alone. For the most part, their deliberations go unreported and hence unnoticed. Their reports to the House are seldom debated.

Four factors seem to account for the ineffectual activities of committees:

- a) Time is of the essence in the House: There is invariably a glut of bills waiting consideration that the Government deems to be more pressing than routine matters such as committee reports: the Government will not make time available for committee reports that could embarrass it; Opposition parties are most reluctant to give up their few assigned days to debate issues that are unlikely to be reported by the news media;
- b) The members obtain little, if any, return for their labours on the committees. Because the committee proceedings are largely "non-events" as far as voters are concerned, for the most part they are also non-events for the members;
- c) When a Government has a majority in the House, it also appoints a majority of the members on each committee. The majority members block every effort by the opposition members that could conceivably embarrass the Government. Leaving aside such things as delaying tactics, the majority members can block obtaining staff support, the calling of witnesses and controversial recommendations;

---

<sup>52a</sup> *Can. H. of C. Deb.* Nov. 23, 1979, at 1642.

<sup>53</sup> *Can. H. of C. Deb.* Oct. 11, 1978, at 3.

<sup>54</sup> *Can., Royal Commission on Financial Management and Accountability: Final Report (Lambert Report)* (Ottawa: Min. of Supply and Services Can., 1977).

- d) The Committees labour without professional staff assistance. That is probably an important facet of committees, although Dobell, who is more familiar with the situation, is skeptical.<sup>55</sup>

Other, more fundamental, issues are no doubt involved. The basic structure of the Parliamentary system is closely related to the party loyalty question and the degree of party loyalty is closely related to election financing. Until more fundamental changes are made in these areas<sup>56</sup> it must be concluded that even if evaluation reports were made available to committees, they are not likely to have much impact on public awareness of their substance.

Historically, Parliamentary control of the Government has centred on control of the public purse. For several hundred years it has been accepted that the Crown cannot spend public moneys for purposes or in amounts not approved by Parliament. Tabling and "voting the Estimates" largely dominate the Parliamentary calendar. In point of fact, even minority Governments seldom, if ever, fall over the proposed expenditure Estimates. The publication of the figures after they are tabled, however, does attract attention. The forecast changes in the budgetary surplus or deficit are, as is well known, much discussed and have, recently at least, resulted in considerable pressure for reduced expenditure. Certainly the expenditure budget, because it is so explicit (at least to those with a modicum of understanding and considerable patience), is one of the few means of holding the Government accountable, although in an extra-ordinarily crude way, as the Lambert Commission emphasized.

Following United States Congressional practice initiated about ten years ago, the Federal Department of Finance estimated, and published in December, 1979, a set of so-called "tax expenditures".<sup>57</sup> The term denotes the estimated value of revenues foregone through tax concessions. Three reasons underlay this decision:

- a) A tax expenditures account is a logical part of a complete accounting system;
- b) Publication of the amounts increases public awareness of the materiality of these concessions and thereby reduces pressure for them in periods when the size of the deficit is of concern;

---

<sup>55</sup> "Committee Staff — What Else is Needed", Conference on "Legislature Studies in Canada", Simon Fraser Univ., Burnaby, B.C., Feb. 1979.

<sup>56</sup> For a thoughtful discussion of Parliamentary reform, see Thomas, *Theories of Parliament and Parliamentary Reform* (1979), 14 J. Can. Studies 57. The views of a number of former parliamentarians were canvassed and summarized in "Special Inquiries — What Parliamentary Committees Can and Can't Do", *Parliamentary Government* Vol. 1, No. 2, Jan. 1980 at 3. For a discussion of the Lambert proposals see Hartle, *The Report of the Royal Commission on Financial Management and Accountability (the Lambert Report): A Review* (1979), 3 Can. Pub. Policy 366 and the symposium issue of (1979), 22 Can. Pub. Admin. 511.

<sup>57</sup> Maslowe, "The Other Side of Public Spending: Tax Expenditure in Canada" in Doern and Maslowe, eds., *The Public Evaluation of Government Spending* (Montreal: Institute for Research on Public Policy, 1979) at 149; and Smith, *Tax Expenditures* (Toronto: Can. Tax Foundation, 1979).

- c) Following from b), the existence of the concessions forces the new cabinet committees that allocate direct expenditures within policy "envelopes" to recognize that demands for tax expenditures must be met by equal reduction in envelope limits for direct expenditures.<sup>58</sup>

There seems little doubt that by providing the tax expenditure estimates, the Government did bring a greater degree of "accountability" to the deliberations of the Committees. It would be a mistake, however, to assume that the whole concept of tax expenditures is not fraught with difficulties. When conflicts arise, as they surely will, the very definition will no doubt be challenged. Adherents are in a vulnerable position because the notion of a concession implies a recognized standard; the fact is, one such standard does not exist.

Moreover, data with respect to levels of tax revenues, tax expenditures and direct expenditures are an extraordinary weak reed as far as accountability is concerned. The amounts involved provide virtually no indication of their ultimate effects; yet, they are sturdy measures indeed compared with the information available concerning regulations counts of numbers of statutes or page counts.<sup>59</sup>

It has recently been proposed that departments be allocated "regulatory budgets".<sup>60</sup> These so-called budgets would set upper limits on the "costs" a department could impose on the economy through its regulatory activities. Despite the aesthetic appeal of the idea, there is no possibility whatsoever that a set of even crudely comparable "regulation accounts" could be estimated on anything approaching a comprehensive basis. Compliance costs give no indication of the full costs and are more likely to mislead than guide. To produce accounts that included the full costs would require detailed econometric "modelling" of each major statute separately in order to produce quantitative estimates. Millions of man years would be required and it is doubtful that the result would have any general acceptance. Because there will always be this loophole in quantitative accountability, the temptation will remain for governments to use regulations the consequences of which are difficult to assess rather than the other policy instruments that leave "dollar tracks".

Generally, proposals to strengthen Parliamentary Committee oversight are likely to have extremely marginal impacts on the formulation and administration of regulatory policies. Adequately subsidized public interest groups along with other interest groups may be able to take advantage of this forum to publicize their views of present or proposed Government policies, but the Committees themselves, as presently structured, have few immediate incentives to play the role of independent critics, let alone that of unrewarded defectors or saboteurs.

Apart from the Council's recommendations on Parliamentary Committee oversight, the Council, in its *Interim Report*, also recommended that appeals

---

<sup>58</sup> Doern, ed., *How Ottawa Spends Your Tax Dollars: Federal Priorities, 1981* (Toronto: Lorimer, 1981) Appendix A at 280-85.

<sup>59</sup> See *Responsible Regulation*, *supra* note 15, Appendix B.

<sup>60</sup> Discussed by De Muth, "The Regulatory Budget" *Regulation* Mar./Apr. 1980 at 29.



to the Cabinet on the decisions of statutory regulatory agencies, and the right of the Cabinet to alter or set aside such decisions, be withdrawn. Instead, it proposed that the Cabinet issue *ex ante* policy guidelines to agencies, restricted, of course, to the range of authority given in the statutes. The House Special Committee on Regulation opposed the Council's recommendation aimed at prohibiting *ex post* cabinet involvement. In the *Final Report* the Council stated: "[I]f Cabinet appeals are to be retained, then procedural safeguards should be established to ensure political control and accountability."<sup>61</sup> In a footnote the Council stressed the urgency of the matter in the light of the Supreme Court of Canada's decision in *A.G. Can. v. Inuit Tapirisat of Canada*.<sup>62</sup> In that decision the Court rejected the notion that there should be judicial safeguards imposed on a political act of this nature.

It is as easy to feel sympathy for the Council's concern as it is difficult to conceive of a remedy. Obviously the present arrangement is politically expedient. Leaving aside the question of work load, particularly with respect to highly technical regulatory issues, the present arrangement provides the Government with the best of both worlds. "Hot potatoes" are handled by so-called independent agencies. The Government can disclaim responsibility for their mildly unpopular decisions. When there is an uproar the Government can step in without introducing new legislation. It is difficult to imagine that a Government would give up this strategic advantage except under great public pressure and there is no evidence to suggest that such pressure exists. To create it, presumably the Cabinet would have to make a grievous political error, and be widely seen to have abused its power. A broad gauge rule providing for *ex ante* directives and precluding *ex post* political review appears to deny some of the political advantages associated with the utilization of independent regulatory agencies and is unlikely to be politically appealing on that account. In particular, to the extent that the analysis of technocratically complex facts is a necessary prelude to a rational political judgment, and to the extent that there is uncertainty about the impact of a policy on different interests, or about voter preferences and the intensity thereof, it may be rational for politicians to treat an agency decision as a kind of "weather-vane". *Ex ante* directives are thus not a perfect political substitute for *ex post* political reviews. The chances of a government agreeing to forego the latter appear slim as the attitude of the House Special Committee suggests.

Another factor that should be taken into account is the timing of a regulatory decision *vis à vis* the electoral cycle. Majority governments can, in the period immediately following an election, "afford" to let stand the unpopular decisions of regulatory agencies (assuming, of course, that they appear to be in the Government's long-run interest). As election day approaches, however, Cabinet's manoeuvring room contracts. This phenomena is based on the presumption that the marginal voters who may lose under the decision have relatively short memories and are likely to give recent losses "undue" weight from the point of view of the Government of the day.<sup>63</sup>

---

<sup>61</sup> *Reforming Regulation*, *supra* note 15, at 134.

<sup>62</sup> [1980] 2 S.C.R. 735.

<sup>63</sup> See Trebilcock, *et al.*, *supra* note 49, c. 3.

## VII. CONCLUSION

It might be argued that the behavioural postulates that are attributed to politicians in this article are deficient in that they depict politicians as essentially passive agents reacting uncritically to the whims of, but not attempting to shape the goals of, the electorate. It is acknowledged here that there is room for political leadership — in effect for politicians attempting to change, rather than simply cater to, voter preferences. Like preachers, proselytizers and psychotherapists, politicians clearly have some ability to propagandize the electorate on behalf of personal and initially unshared beliefs. However, the scope for successful pursuit of this kind of strategy in the political arena seems likely to be relatively limited. First, it seems likely that more political resources are required to attempt to change voters' preferences rather than simply to communicate attempts to respond to them. Apart from higher costs faced by political messiahs, voters also face higher costs in attempting to evaluate the merits of abandoning one set of preferences and adopting another. Given political competition, we would assume the existence of incentives to minimize both sets of costs. Thus, attempting to change, rather than respond to, voter preferences, at least where firmly formed, is likely to prove to be a politically inefficient, high risk strategy. This is likely to be less true where voter preferences are weakly formed, incoherent or difficult to ascertain. Here, there is clearly more room for politicians to promote personal preferences and shape public preferences. Moreover, whether politicians are predominantly influenced by voters' preferences, interest group preferences or personal preferences, may in part be a function of the point in time in the political cycle when decisions are being made. Interest group preferences, and perhaps personal preferences of politicians, are likely to be more influential at earlier stages in the electoral cycle; voter preferences are likely to be more influential late in the electoral cycle.<sup>64</sup>

If the basic postulate of this article — that the choice of regulatory policy is motivated principally by the search for electoral success rather than social welfare or "efficiency" consideration is valid, it would seem to follow that this holds true for all policy decisions. This implies that if one wishes to change policies in a significant and lasting way, it is necessary to change some extremely fundamental dimensions of the political system. In particular, changes in the rules and incentives that constitute the political system would seem to be required. The policy outcomes are unlikely to be altered until the structure and processes that generate them are also altered.

Could fundamental changes in the political system occur without concomitant changes in the economic system? Would the myriad special interest groups that have accommodated themselves to universal suffrage, within or through the prevailing political system, countenance a major change in the system? To what extent are divergences in our political system from an egalitarian theory of democratic entitlements conscious social compromises with the inequalities of wealth required by an economic system driven by

---

<sup>64</sup> Breton, *The Economic Theory of Representative Government* (Chicago: Aldine, 1974). See references cited at 222.

private incentives? As interesting and important as these questions are, to pursue them would be to launch another article.

While this extensive domain of issues cannot be explored here, it is possible to ask another question. If the key to policy change involves making changes in the political and economic systems — of an unspecified sort — what are the implications for economic research?

A large body of economic research is undertaken as part of an inward-looking professional game. Presumably that is unaffected by changes in perceptions about the role of economics (and the other social sciences for that matter) in that policy-making process. Turning to the work that has been oriented towards policy improvement, it would seem to be implied by the line of argument advanced here that, for the most part, the work of economists will inevitably not be viewed by politicians primarily as a source of intelligence about the world. Rather, it will be construed as posing a problem if it lends support to an opponent or as part of the “solution” if it lends support to the particular politician. In short, the flow of economic research might perhaps be thought of as a flow of expert witnesses appearing in an endless adversarial proceeding — sometimes helping one side, sometimes another, sometimes being suppressed, sometimes being distorted, twisted and trivialized for the benefit of a “user”.

One perception seems essentially puerile: the notion that governments can be looked upon as ignorant, benevolent dictators who want to do the “right” thing, who are all powerful and who are simply waiting for the economists to tell them what to do. If the competition amongst parties is vigorous, and if the pressure of competing interest groups is intense, the policy vacuum just described seldom, if ever, exists. This is not to say that the policies under consideration at any one time are in any sense optimal, although the meaning of optimal in this context is far from clear. What is implied, however, is that, with rare exceptions, policy proposals based on the results of economic research are in competition with proposals based on other considerations.

There would seem to be one general area where economic research has a unique role to play even under the “electoral success maximizing” assumption. Policies adopted today for short-term political reasons can later produce major, unforeseen negative effects or side effects. If the time horizon of the electorate is short the politician can afford to make decisions on that basis. Future adverse consequences can be ignored. Should that not be the case, and if the politician believes he will probably have to cope with the negative effects, then these will bulk larger in the decision. It is here that economic research can make a significant, and perhaps unique, contribution. The discipline of economics bestows, admittedly most imperfectly, some comparative advantage in inferring the longer term and indirect consequences of alternative policy actions. Although the views of economists and social scientists on normative matters have no particular merit, disentangling the full and longer term implications of alternative policies can presumably improve policy when politicians have options that do not compromise their chances of political survival. Despite what may appear to be the somewhat cynical tone of some of this article, it is probably reasonable to assume that when politicians perceive that they have such choices, they are likely to choose, *on the basis of the information*

*available to them*, policies that affect broadly based longer term interests rather than policies that pander to narrow, short-term interests. Economists and others can assist them in making these choices by providing them with more or better information on the policy implications of the options.

When thinking of policy-making, one tends to think of politicians and their supporting bureaucrats. In fact, of course, casting a ballot is a policy decision for the voter, as is the decision to join a pressure group and so on. It is assumed here that all these decisions are based on the pursuit of the individual's self interest — individuals are assumed to be rational and to choose the alternative that they expect will give them the most satisfaction (utility). The information upon which such decisions are made is inherently limited (for example, bounded rationality and rational ignorance). Economic research, by providing a public good, can add to the information available and improve these "private" decisions — just as it can for politicians — if it is disseminated.

It is important to realize that by influencing voter knowledge and understanding, and hence voter decisions, the insights of economic research, and social science research generally, can be brought to bear on the ultimate decision-making process. Indeed, these effects of new information may be much more effective than the direct provision of information to bureaucrats and politicians. When few voters are aware of it, the latter often can ignore new information when it does not suit their convenience. Politicians cannot, however, easily ignore voters armed with the relevant information. One might wonder why so much research is written and "published" with little if any attention being paid to the dissemination of the results generally. So many economists write, when not writing to one another, as though their task were to advise the Prince rather than the public.