

What Are the True Costs of Regulation?

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MANY RESEARCHERS AND CLINICIANS working in cybertherapy create their own businesses, which allow them to protect their intellectual property. In the United States, small businesses create the majority of jobs but bear proportionally more of the cost burden of implementing laws and regulations than do larger companies. This is true primarily because larger companies enjoy economies of scale. However, estimates of the true costs of regulation vary widely.

A new study* found that companies with fewer than 20 employees pay 42% more per employee than companies with between 20 and 499 employees, and 36% more than companies with 500 or more employees. For small businesses, the average cost per employee was \$10,585 compared to \$7,454 for medium-sized and \$7,755 for large businesses.

According to the study, environmental regulations cost 364% more in small versus large companies, and tax compliance is 206% higher. Occupational safety and health and homeland security are other top cost drivers.

The researchers calculated that some types of industry pay more than others. For example, small manufacturers (such as small manufacturers of medical devices) pay 110% more for compliance than medium-sized manufacturers and 125% more than large manufacturers. Small health-care firms (such as cybertherapy clinics) pay 45% more than medium firms and 28% more than large firms.

The authors say the total cost of regulation is \$1.75 trillion, and note that businesses must close shop, reallocate activity, absorb the cost, or pass on the costs to customers. They estimate the per-household cost of federal regulation and taxes at \$37,962.

The report notes, "If federal regulations place a differentially large cost on small business, this potentially causes inefficiencies in the structure of American enterprises and the relocation of production facilities to less regulated countries, and adversely affects the international competitiveness of domestically produced American products and services."

Some say that the above numbers are inflated and the study methodology is questionable, pointing to the annual report of the Office of Management and Budget (OMB) on the costs and benefits of regulation† for a truer picture of the cost of regulation.

The OMB report notes that "The estimated annual benefits of major Federal regulations reviewed by OMB from October 1, 1999, to September 30, 2009, for which agencies estimated and monetized both benefits and costs, are in the aggregate between \$128 billion and \$616 billion, while the estimated annual costs are in the aggregate between \$43 billion and \$55 billion," and that "Most rules have net benefits, but some rules have net costs."

Regardless of which of these estimates is closer to the true cost of regulation, the truth is that many regulatory costs are fixed: they are the same whether a company has 20 employees or 20,000. And the 89% of U.S. companies that have fewer than 20 employees produce a significant number of innovations. As President Obama has said, "Small businesses are the heart of the American economy."

In fall 2010, President Obama signed the Small Business Jobs Act, designed to help small businesses have easier access to credit and to provide more tax breaks. While a worthy effort, it does nothing to stem the tide of ever more regulation coming out of Washington.

Regulation per se is neither good nor bad. Rather, regulation in which the benefit outweighs the cost is good; regulation in which the cost outweighs the benefit is bad. Not all benefits can be quantified, which further complicates the picture.

It is time to start a serious dialog about the true cost of regulation, one that uses methodologically sound benefit-cost ratios as a starting point. I encourage readers to become involved in commenting on proposed regulations, so that only those regulations that pass the benefit-cost test are implemented. It is important to do so: the very future of innovation in health technology is at stake.

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*Crain NV, Crain WM. The Impact of Regulatory Costs on Small Firms. Prepared for the Small Business Administration Office of Advocacy under Contract SBAHQ-08-M-0466, Sep 2010, 83 pp. www.sba.gov/sites/default/files/rs371tot.pdf (accessed Dec. 31, 2010).

†Office of Management and Budget, Office of Information and Regulatory Affairs. 2010 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities. www.whitehouse.gov/sites/default/files/omb/legislative/reports/2010_Benefit_Cost_Report.pdf (accessed Dec. 31, 2010).

