DIVISION OF THE HUMANITIES AND SOCIAL SCIENCES

CALIFORNIA INSTITUTE OF TECHNOLOGY

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THE DILEMMA OF CONSUMER ADVOCACY*

Roger G. Noll

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Roger G. Noll*
California Institute of Technology

In the past few years political leaders from the full range of the ideological spectrum have begun to give serious consideration to several proposals to overhaul the scope and structure of regulation. In some instances, significant reductions in the scope of regulation have either been adopted (brokerage commissions) or are being seriously considered (trunk airlines). These and other examples reflect the growing opinion that regulation, no matter how effective, has nothing beneficial to contribute to the performance of some regulated industries.

Another class of reform proposals reflects a somewhat different criticism of regulatory agencies. These proposals seek to change the structure and process of regulation. They are motivated by the belief that, while some unregulated markets do not perform well, regulatory institutions have not been very successful in improving matters. Reform proposals of this type take many forms, such as changes in the number of administrators of an agency, in the agency's location in the governmental organization chart, and in the allocation of responsibilities among agencies. Perhaps the most novel

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reform is the creation of a governmental agency to intervene in the proceedings of regulatory agencies as an advocate of the consumer.

This paper focuses on the likely behavior and effects of a consumer advocacy agency. In so doing it abstracts from three related issues except insofar as they bear directly on the performance of a consumer advocate. These other issues are: (1) the case for substantial deregulation in several areas; (2) the reasons for governmental intervention in private markets; and (3) the various structural reform proposals, such as those proposed by the President's Advisory Council on Executive Organization (the Ash Council). This paper presumes that all reasonable men can agree that some current regulatory activities are unnecessary (e. g., the Federal Communications Commission favors cutbacks in the extent to which radio and television licenses are regulated), while others are probably desirable (e.g., Ralph K. Winter, Jr., believes in certain standard-setting regulatory activities, such as those affecting children's safety [1]). The paper avoids issues relating to changing the internal structure of agencies since I have expressed my generally pessimistic view of the likely benefits of these reforms at tedious length elsewhere.[2]

[1] Ralph K. Winter, Jr., The Consumer Advocate vs. the Consumer, Special Analysis #26, American Enterprise Institute, 1972.

[2] Roger G. Noll, Reforming Regulation: An Evaluation of the Ash Council Proposals (Washington, D. C.: Brookings Institution), 1971.

The following two sections review and elaborate upon the arguments for and against a consumer advocacy agency. The final section synthesizes these partial analyses, attempting to provide a somewhat more complete and coherent theory of the agency than either side of the controversy has presented. The conclusion of the

paper, as intimated by the title, is that the creation of the agency has both costs and benefits to consumers, the relative magnitudes of which can not be determined on the basis of theoretical and empirical information currently at hand. In the end, the debate over the wisdom of creating the agency is one of competing judgments, not scientific fact -- just like so many of the regulatory issues that the agency is supposed to tackle.

Before proceeding, a definition is in order. By consumer advocacy agency, I mean an agency with a separate budget and separate legislative program that is concerned with the direct, private effects of consumer products on consumers. The agency will consider prices, product safety and quality, and the truthfulness of product information provided by producers. Among its activities will be formal intervention in regulatory proceedings, judicial appeals of agency decisions, informal contact with personnel in other agencies, in the consumerist movement and even in industry, and participation in Congressional hearings and investigations related to consumer affairs. It will not have any direct regulatory or prosecutorial powers, and it will not be the advocate for other "public interest" groups, such as environmentalists, labor, small businesses, farmers, pensioners, etc. To the contrary, it would , in principle at least, oppose these interest groups should they favor policies that impose significant costs on consumers.

Admittedly, this definition of a consumer advocate does not reflect the agency described in any legislation, passed or proposed. Congress has not expressed interest in creating its own watchdog, but it has considered bogging down the agency with concern for small businessmen and farmers, both of whom already have effective bureaucratic protectors. Neither does the foregoing definition specify the details of the agency's rights and powers. The definition is offered to capture the essence of a pure consumer advocacy agency as a point of

departure for further analysis of the agency's aims, policies and effects.

THE CASE FOR A CONSUMER ADVOCATE

The principal argument that has been put forth in support of creating an advocate for consumer interests is, in essence, an appeal to the concept of procedural due process. Proponents of an advocacy agency for consumers base their case on two observations about regulation: first, agencies often make decisions that sacrifice the interests of consumers to those of other groups, notably producers, and second, producers and other well-organized special interests are far more likely to be represented in the formal proceedings of an agency than are consumers. The proponents conclude by arguing that these two observations are, plausibly, causally related, so that redressing the imbalance of representation will move regulatory decisions more in favor of consumers.

Few would disagree with either generalization upon which the case for a consumer advocate is based. The theoretical models predicting a pro-producer bias in regulatory outcomes will be discussed briefly below; suffice to say here that in the 1970s it is rare, indeed, to find an article in the popular press or the professional literature that does not chastise regulators for "crawling in bed with industry."—/

—/The most recent paper of which I am aware that extolls the performance of regulators is the enthusiastic, if Pollyannaish, offering by A. J. G. Priest, "Possible Adaption of Public Utility Concepts in the Health Care Field," Law and Contemporary Problems 35 (1970).

Like most generalizations, the meaning of this one deserves careful, explicit definition. Only Marxists contend that agencies do exactly as producers bid; most others find some truth in the claim of businessmen that regulation does alter firm behavior in ways contrary to the firm's interests. What is really being said in the accusation that regulation is pro-producer is that, on balance, regulation tends to make the life of producers somewhat more secure than it otherwise would be, particularly with respect to the threat that an established firm will be displaced by a competititve entrant into its market.

That consumers are usually unrepresented in regulatory affairs is well-documented, although the extent to which consumerist intervenors do participate is certainly on the rise. One would expect consumers, as a group, to have less representation in relation to their stake in agency decisions than do producer groups. Consumers constitute a far larger, more heterogeneous group than do firms in a regulated industry. In general, the larger the group and the more diverse the preferences of its members, then the greater is the per capita cost of organizing the group and of reaching a group decision about its collective choice among alternatives. In addition, the larger the group the less important to the success of the group is participation by any single member. Hence a member of a large group has an incentive not to pay the costs of participation since the benefit he will receive will be only slightly affected by his decision to join.

If the total stake of two groups in a decision is equal and if the effectiveness of their representation is related to expenditures incurred through participation in the decision-making process, the larger group will be less likely to be represented because: (a) its organization costs will be higher, (b) it will face a problem with free riders, and (c) it will have less chance of success -- and therefore

less reason to act -- than if the group's representation were proportional to its stake in the issue. In the case of consumers, all of these factors are essentially at work to their maximal extent. Most individuals have a tiny personal stake in any given regulatory issue; they would hardly find it worthwhile to join an organization that would represent them in the proceedings that deal with it. Nevertheless, to the extent a regulatory decision generates monopolistic practices (but not perfectly discriminatory ones) where competition would otherwise prevail, the total gains to the producers will fall short of the total costs to consumers.—/

—/ This will be true unless the rest of the economy is particularly perversely structured. Presumably the purpose of regulation is not to find an elusive second-best by eliminating the few bastions of perfect competition in an economy otherwise overflowing with concentrated markets, high transaction costs, externalities, incomplete opportunities for trading contingent claims, and the like.

The preceeding argument does not imply that only the supply side of a regulated market will be effectively represented. Some users of the output of regulated firms are members of relatively small, homogeneous interest groups. In proceedings before the Interstate Commerce Commission, for example, state and local governments have opposed route-abandonment proposals by railroads. And, of course, industry trade associations and large firms have opposed proposals that would cause them economic harm. In fact, the most effective group -- and the beneficiary of the "pro-producer bias" -- is frequently an industry that is a user of the output of the regulated firm. Their gains can come at the expense of individual

households, poorly represented industries, and the regulated firms. In the ensuing discussion, then, pro-producer bias in regulatory outcomes refers to all biases in favor of well-represented groups of firms, regardless of which side of the regulated market they find themselves. Although it does some violence to language to include, by implication, poorly represented industries in the class of consumers, as a practical matter is probably is not a misleading generalization. Their lack of representation, for reasons given above, is likely to flow from their competitiveness -- they face high organization costs because they are comprised of numerous firms. Hence, cost increases imposed on them by regulators will in the end be passed through to their customers, rather than extracted from excess profits.

The point of controversy in the positive case for a consumer advocate is whether the generalizations about consumer representation and pro-producer bias are causally connected. Whether a consumer advocate could significantly alter regulatory outcomes depends upon the objectives of the regulators and the relationship of inputs to outputs in the regulatory process. If the regulatory process were aptly characterized by either its description in high school civics texts or the extensive literature in economics on the behavior of the firm under regulatory constraint —/ the consumer advocacy agency would not have an effect on regulatory outcomes. According to this view of regulation, the regulatory agency is already an effective consumer

—/ Harvey Averch and Leland L. Johnson, "Behavior of the Firm Under Regulatory Constraint," American Economic Review 52 (December 1962), and W. J. Baumol and A. Klevorick, "Input Choices and Rate-of-Return Regulation: An Overview and Discussion," Bell Journal of Economics and Management Science 1 (Autumn 1970).

advocate. Its objective is to constrain the behavior of private firms in imperfect markets by setting prices and profit rates or by establishing minimum performance standards. The world in which the agency operates is one in which information about demand and costs, both now and in the future, is available with sufficient precision that regulators can determine with reasonable accuracy a socially optimal policy. The agency is established because the legislative process is too cursory, and probably too corrupt, to be expected to deal effectively with correcting market imperfections. Hence, to attain regulatory objectives, an expert independent body is created that will learn the details of the operation of an industry so that it can develop operating constraints on firm behavior that will ameliorate market imperfections while still leaving the industry economically viable.

In such a world, the consumer advocate has no role. The regulatory agency already has the information it needs on the operations of the regulated industry, and already is suffused with the desire to serve the interests of consumers. Of course, about the only people remaining who believe that this description of the regulatory process is realistic are the agencies themselves, and their comments in response to the proposal to create a consumer advocacy agency follow this same line of reasoning. For example, the Postal Rate Commission reminded Congress that it always appoints a staff member to represent the consumer in all of its rate hearings. The Atomic Energy Commission (prior to its fission) regarded the proposed agency as "unnecessarily duplicative" since it already protected consumers against unsafe nuclear reactors and accepted the Antitrust Division's advice on protecting consumers against detrimental anticompetitive effects of nuclear power facilities. The Federal Power Commission "does not recognize the need ... for protection of consumer interest insofar as our responsibilities as delegates of Congress are concerned." The FPC gives a

classic defense of its position that bears repeating:

> The task of a consumer protection agency in regulating interstate electric and natural gas utility service is, of necessity, highly specialized and demands the services of knowledgeable experts who can be depended upon to bring all facets of a particular problem to the attention of the agency. Over the years, the staff of the Federal Power Commission has accepted its legal obligation to provide forthright presentation and advocacy of the consumer viewpoint before the Commission and the Courts. In addition to staff represenation and consumer participation directly or through consumer associations, the consumer interest is also effectively represented by gas distributors, state commissions, environmental organizations in many instances, and others who participate regularly as parties or intervenors in Commission proceedings.—/

—/ The foregoing quotations and characterizations of agency positions are all from U. S. Senate, Committee on Government Operations and Committee on Commerce, To Establish an Independent Consumer Protection Agency: Joint Hearings, 93rd Congress, First Session, 1973.

In contrast to this idealistic self-image, some observers believe that regulation never was intended to protect consumers. Instead, it was designed and is operated to reduce competition among producers. Marxists see regulation as an institutional innovation of the capitalist ruling class to improve the possibility for monopoly profits.—/

—/ See Gabriel Kolko, Railroads and Regulation (Princeton: Princeton University Press), 1965.

Stigler predicts a similar result, with the main difference being that firms and professional organizations must purchase anticompetitive insitutions from a legislature that, rather like a firm,

maximizes the gains of its members from the granting of institutional favors.—/

—/George Stigler, "The Theory of Economic Regulation," Bell Journal of Economics and Management Science 2 (Spring 1971).

If either theory is roughly correct, giving consumers more representation in the regulatory process is unlikely to alter regulatory outcomes, since the mandate and procedural requirements of the agency have already been designed to enable the agency to make decisions in favor of producer groups. Procedural due process does not create an ability to influence decisions unless the decision-making body, whether a court, a legislature or a regulatory agency, either enters the process with a set of objectives that differ in some significant way from the objectives of one of the interests participating in the process, or has concrete, specific rules that require certain substantive results should interests other than producers support them. Otherwise, the agency can satisfy the procedural requirements by allowing all interests to participate, citing all the legal, economic and other evidence submitted, and then simply finding unpersuasive the arguments in opposition to the producers.

Since the decline of substantive due process, dating from Nebbia v. New York, courts have generally steered clear of reviewing agency decisions on more than procedural grounds.—/ Consequently,

—/According to the Court:

> So far as the requirement of due process is concerned, and in the absence of other constitutional restriction, a state is free to adopt whatever economic policy may reasonably be deemed to promote public welfare, and to enforce that policy by legislation adapted to its purpose. The courts are without authority either to declare such policy, or, when it is declared by the legislative arm, to override it. If the laws passed are

> seen to have a reasonable relation to a proper legislative purpose, and are neither arbitrary nor discriminatory, the requirements of due process are satisfied, and judicial determination to that effect renders a court functus officio. . . . With the wisdom of the policy adopted, with the adequacy or practicability of the law enacted to forward it, the courts are both incompetent and unauthorized to deal. . . .
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> Price control, like any other form of regulation, is unconstitutional only if arbitrary, discriminatory, or demonstrably irrelevant to the policy the legislature is free to adopt, and hence an unnecessary and unwarranted interference with individual liberty. [Nebbia v. New York, 54 S. Ct. 55 (1934)]

While the case at hand dealt with an issue of state regulation, the principles enunciated therein have generally been followed with respect to judicial review of regulatory law and agency decisions.

the agency faces no necessity to bend its decisions in the direction of consumerist intervenors as long as it accords them whatever procedural rights a court will demand.—/

—/As an aside, where in the Marxist or Stigleresque regulatory theory is there an explanation for establishing a powerless consumer advocate? One possibility is that "public interest" lawyers are intent on creating more demand for their services. Although this seems far-fetched owing to the meager number of public interest lawyers, it is interesting that the American Trial Lawyers Association supports the creation of a Consumer Protection Agency. Another possibility is that creation of a consumer advocacy agency deflects the attentions of consumerists from Congress and regulators, defusing some of the political demand for less industry-oriented policies. This latter possibility is investigated in the next section.

In order for a consumer advocacy agency to have an effect on regulatory outcomes, a somewhat more complicated conceptual model

of the regulatory proccss is required. If the decisions of the regulatory agency are somewhat more pro-producer than were intended by the legislature in giving an agency its mandates, the agency's decisions may be successfully appealed to the courts by nonproducer participants in the regulatory process. For example, environmentalist groups have provided numerous examples of the use of the court system to force recalcitrant agencies to consider environmental consequences of their decisions. In fact, most federal regulatory agencies refused to consider environmental issues in their cases until instructed to do so by the courts upon appeal of agency decisions by environmentalists. Although each agency has its precedental environmental case, the classic example is the Calvert Cliffs case in which three intervening groups -- the Sierra Club, Friends of the Earth, and the Committee for a Sane Nuclear Policy -- successfully appealed a license for a nuclear power facility that was granted by the Atomic Energy Commission. The claim of the intervenors, which was accepted by the courts, was that the AEC had failed to consider the environmental consequences of the construction of the nuclear power facility, contrary to the dictates of existing legislation and executive orders.

The decision by most agencies to avoid environmental issues until forced to do so by the courts was certainly consistent with the interests of producers, and even of consumers qua consumers. Requiring that agencies consider environmental issues may increase the likelihood that a particular proposed action by a firm will not be approved (although this is, in practice, not common). It always increases the cost of obtaining regulatory approval of a proposed action, however, and often leads to the producer incurring greater design costs in the investments or products for which it seeks regulatory approval. And some of these costs will be passed on to consumers.

One must conclude that intervention in regulatory proceedings by environmentalists has paid some dividends to the environmentalist movement. At the very least, intervention has reduced the likelihood that a firm will obtain timely approval of actions (by increasing the cost) that are contrary to the environmentalists' perception of their interests.

This, of course, does not establish that consumer advocates will have a similar effect, for regulatory agencies, with few exceptions, have never regarded themselves as protectors of the environment, although they all proclaim a self-image as a consumer protector. Furthermore, the victories of the environmentalists have been obtained by private groups, not a federal environmental advocacy agency. In order to claim that the consumer advocacy agency would be effective one must develop a theory of the regulatory process that predicts a systematic pro-poducer bias in agency decisions that is not the legislative intent and that results from inadequate consumerist representatation in the process. In other words, one must show that the systemic features of regulation which lead to a producer bias in outcomes are the direct consequence of the identity and strength of the groups intervening in agency decisions.

Numerous theoretical models of the regulatory process do produce such a prediction. —/ Suppose that whatever the objective of

—/ No attempt to survey theories of regulation will be made here. Elsewhere I have made such an attempt: see Roger G. Noll, "Government Administrative Behavior and Technological Innovation," Social Science Working Paper #62, California Institute of Technology, November 1974.

the agency, its performance is either crudely measured or determined

by the following class of agency indicators: budget, fate of legislative program, number of rules promulgated and cases decided, economic health of regulated firms, ability to avoid appeals of decisions -- particularly successful appeals -- and the tone of press reviews of the agency's activities. Of course, depending upon the particular theoretical model, these various indices can be systematically related in complicated ways. For example, reversals of agency decisions by the courts may be undesirable because (a) they cause the Congress and the Office of Management and Budget to grant the agency a smaller budget; (b) they reflect upon the competence of the highest agency officials, thereby reducing their future employment possibilities in the private sector; or (c) they simply provide a signal to the agency that it is not adequately serving the ephemeral public interest that it likes to think of itself as maximizing.

In principle, of course, a direct measure of the agency's net economic impact would be preferable to this class of indirect measures as an indicator of the agency's performance. But the agency may not see itself as maximizing economic welfare, or may regard these indicators as so closely related to its effects on economic welfare that it need look no farther, or may regard the measurement of economic welfare so difficult that it settles for measures of its standing among those with whom it has the greatest contact -- the courts, the Congress and, most of all, regulated firms and other interests that are well-represented in its proceedings. The point here is simply that agencies, for whatever reason, may rely on these other, less direct success indicators in evaluating themselves. As long as this is the case, agencies will have an incentive to decide uncontested issues in favor of whatever interests are represented in their proceedings. This minimizes the resources committed to the case, makes appeal of the decision unlikely (normally only

participants in the process can appeal, and there is little incentive to appeal a decision that grants a group most of what it wants), and, if the producer group is rational, contributes to the economic health of the regulated industry. Intervention by a consumer group -- or any other nonproducer interest -- according to this point of view, will eliminate whatever incentive the agency would have to go beyond the legislative intent in favoring the producer group by introducing the penalty of a successful appeal should such decisions be promulgated.

Of course, decisions by regulatory agencies presumably depend on more than the fact of representation -- the process is more than a politico-legal tug-of-war. The agencies are, by design, "expert" bodies, which is to say the regulatory process is, in part, a mechanism for gathering, analyzing and evaluating technical information. Observers of the interactions between agencies and the budgeteers in Congress and the Executive Office regard the expertise of the agency as one of its most potent weapons in attaining its budgetary objectives.[1] In addition, to the extent an agency accords any weight to the economic consequences of its decisions, it will pay some attention to the information that it is supplied about regulated activities.

[1] For example, see Aaron Wildavsky, The Politics of the Budgetary Process (Boston: Little, Brown & Co., 1964).

The importance of information in the regulatory process gives represented groups still another advantage in influencing decisions. If information is expensive and difficult to comprehend, a participant in the process can use information strategically to direct the policies of the agency. The adversary process is, in part, an embodiment of the recognition that strategic use of information is

possible. The procedural right to representation in a decision-making process affecting one's welfare has substantive importance because it accords one the opportunity to present counter-evidence to show that the information presented by the opposition was incomplete, inaccurate, irrelevant or incorrectly analyzed.

While a consumer representative might be expected to be effective in counteracting the most egregious examples of strategic use of information, it would still face some exacting problems. The source of information on costs and demand, present and future, is primarily the regulated industry. While some analysis can be successfully accomplished with the information supplied by firms to regulators, the underlying quality of the data -- and the data that are either never collected or never made available -- are imperfectly known at best. Thus, the consumer advocate, like the agency, is vulnerable to strategic use of information, particularly if it is not endowed with analytical resources on a par with those of the regulated industry. Furthermore, the unevenness between the consumer advocate and the producer groups in the amount and relevance of data that they possess will give the advocate less opportunity than the industry for using information strategically.

This does not mean that the consumer advocate is doomed to reach the same conclusions as the agency staff, as has been suggested.[1] The agency will have some independent sources of

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[1] Statement of Ralph K. Winter, Jr., in Joint Hearings.

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information -- particularly alternative methods and models for analyzing the data provided by other sources. In addition, the agency is likely to face different incentives, if not to have different motives, than the regulatory body. The advocacy agency will, for example,

engage in a wider variety of policy activities affecting a broader spectrum of interests than is typical of regulatory bodies. A regulatory agency normally deals with at most a handful of industries, and deals with each numerous times on different aspects of its regulatory mandate. Antagonizing one of its regulated industries can have repercussions on many other cases before the agency by making the industry less cooperative in supplying information or by causing the industry to wage political war on the agency by appealing its policies to Congress. An advocacy agency will have a lower proportion of its activity devoted to dealing with any given industry. Hence it will be less dependent on future cooperation from the industry, and less vulnerable should the industry attack its actions politically. Furthermore, as long as the advocacy agency is not extremely large compared to regulatory agencies, any given producer group will deal with the consumer advocate less frequently than with the agency that regulates it. As a result, it will have less incentive to capture the advocate than it has to control the regulators.

Another difference between the advocate and the regulator is that the former has less stake in procedural measures of the success of the regulatory process. It will be less concerned than are regulators with the fact that a decision was reached or that the decision-maker gave the appearance of being neutral, objective and just -- in fact, in some cases the advocate will try to establish the opposite. The advocate will, presumably, achieve its objectives to the extent it changes regulatory outcomes, whereas producing an outcome of any form -- as long as it is legally unassailable -- has value to the regulator.

A final factor that will influence the consumer advocate to behave differently than the regulator is that it will be far more likely to develop a political constituency among consumerist groups, if not

consumers directly. The agency will be a natural point of contact between governmental policy and consumer groups since the advocate presumably will be monitoring activities in numerous agencies. In order to be effective within the governmental hierarchy, an agency must develop constituencies -- groups that will defend the agency before Congress and in the media.[1] Constituencies develop in

[1] See Wildavsky, The Politics of the Budgetary Process.

part by the granting of favors and in part through frequent, informal contact with the agency. The latter can be especially important in the regulatory process since a relatively small proportion of the population pays much attention to it. Not only are consumerist groups the natural allies of the advocacy agency, they are the ones most likely to have a powerful incentive to develop a continuing informal relationship with it. As with regulators and regulated, it would be natural for the advocacy agency and consumer groups each to be a source of employment for the other, and for each to share information about its current activities to capture scale economies in information collection and dissemination.

For all of these reasons the consumer advocate can be expected to have different objectives and to face a different set of incentives than the regulatory agency. In fact, the opposition of the established agencies to the creation of a consumer advocate is consistent with this theoretical conclusion. If agencies were pure consumer advocates, as their self-image suggests, they should welcome a consumer advocacy agency as a possible resource to marshall in especially tough, important cases. Or, if agencies were, in their formal decision-making mode, the neutral, judicial institutions that is also a part of their self-image, they would hardly fear

participation of representatives from a group whose welfare is dependent upon their decisions, much as a court of law would not be opposed to the existence of a public defender's office.

More likely, existing agencies oppose the establishment of an advocacy agency because it will, in fact, express a different point of view than that taken by the staff of the regulatory agency that has the task of presenting the consumers' stake in the matter. The causes for the differences can be many: either of the two may be mistaken, either may, in fact, be representing some interest other than that of consumers, or the information about the consequences of alternative policies may be sufficiently uncertain that it cannot support a choice among several policy conclusions (which, by implication, indicates that the decision carries more risk for consumers than one would infer if only one position were stated and defended in the proceedings).[1]

[1] This last point is the heart of an insightful criticism of the use of benefit-cost analysis in nuclear safety regulation. See Paul L. Joskow, "Approving Nuclear Power Plants: Scientific Decision-making or Administrative Charade," Bell Journal of Economics, Vol. 5 #1 (Spring 1974).

If an agency does not want to be wrong, to be "exposed," or to emphasize the uncertainties connected with its decision (thereby undermining its illusion of expertise), it will find life more comfortable if it can monopolize representation of a general public interest.

The main conclusion to be derived from the preceeding analysis is that a consumer advocacy agency will change the incentives of regulatory agencies and thereby affect their decisions. This does not mean that the agency will generate net social benefits; to reach that conclusion requires further analysis of the kinds of changes in

decisions the advocacy agency is likely to produce and the costs associated with producing those changes. Since the proponents of the advocacy agency have not addressed either of these issues in great detail, they will be explored in the discussion of the case against the advocacy agency.

THE CASE AGAINST THE CONSUMER ADVOCATE

The arguments against the consumer advocacy agency fall into three classes. First, creation of the agency, it is argued, will increase the costs of regulation. Second, the agency will generate some indirect costs through its effects on government policy and private enterprise. Third, the agency is unlikely to take positions that really serve an identifiable consumer interest, in part because its connection to consumers is minimal and in part because the interests of consumers are too diverse to be represented by a single advocate.

This section will not deal with several analyses of the weaknesses of certain optional details of the agency's structure, power or operations. Much of the debate in Congress has focused on the merits of alternative structures and mandates of the agency, rather than on the general issue of whether the agency should be created.[1] The only issue that could be classified as a detail that is

[1] For an excellent discussion of the details see the statement of Roger C. Cramton in Consumer Protection Legislation, Hearings Before a Subcommittee of the Committee on Government Operations, House of Representatives, 92nd Congress, 1971; and the statement of Antonin Scalia and the memorandum of Ernest Gellhorn in Joint Hearings, 1973.

considered here is whether the agency should be allowed to participate in informal processes within regulatory bodies. The following discussion assumes that the agency will participate in informal processes if it so chooses.

Direct Costs of the Regulatory Process

Creation of a consumer advocacy agency will increase the costs of the regulatory process in three ways. First, if the existence of the agency increases the frequency of intervention before regulators, the proceedings will undoubtedly take more time. The additional intervenor will consume some time presenting its case, the other parties will devote additional time to responding to the intervenors, and the agency will spend more time extracting a policy or decision from the more complex proceedings (especially since the presence of an intervenor increases the likelihood of appeal).

The rough correlation between intervention and the duration of the process is illustrated by some data that were compiled by my colleague Margaret Rouse Bates in connection with a study we are undertaking of the licensing of nuclear power facilities. Her data show the extent of intervention and duration of the eight construction permit license cases decided by the Atomic Energy Commission in 1973. Two cases in which no one attempted to intervene each took six months to decide; four cases in which intervention was attempted but was either unsuccessful or required to be limited in scope took approximately one year to decide; the final two cases in which full intervention was granted took twenty and thirty-eitht months, respectively. In none of the cases, however, did the intervenors succeed in blocking the facility or obtaining major changes in its design.

The second manner in which a consumer advocacy agency increases the direct costs of regulation is through the strategic

response of regulated firms to the presence of another force in the process. They will have to make better presentations before regulators, judges and congressmen if their arguments are to be more carefully scrutinized. In addition, they will be likely to respond to the creation of the agency by increasing their informal lobbying efforts -- at least to the extent that the consumer advocacy agency itself must be given some lobbying attention.—/

—/ The last point was made by Ralph K. Winter, Jr., in Joint Hearings, 1973, in connection with his argument that the advocacy agency eventually would be captured in the same fashion as were regulatory agencies.

The third way in which the advocate will increase regulatory costs is by forcing more proceedings to become formal. A substantial amount of the decision-making process in all regulatory agencies consists of informal contacts at the staff level between the agency and the regulated industry. In some agencies, this process is so thorough that formal cases are either rarely heard or perfunctory. For example, for over three decades the Federal Communications Commission regulated the American Telephone and Telegraph Company by "continuous surveillance" -- which is to say a formal rate hearing was never held. At the Atomic Energy Commission, the staff was intimately involved with the design of proposed reactors during the period in which the agency licensed power facilities, from 1954 to 1974. By the time a license application reached the formal hearing stage, the staff had already redesigned those features that it thought were unsatisfactory; rarely were changes made in reactor design during the formal hearing, appeal and full Commission review, even when intervenors participated in the process.

In many agencies the decision whether to open a case is made through informal discussion. The Federal Trade Commission and the agencies dealing with product safety, environmental protection and other standard-setting policies investigate far more cases than they bring to a formal process. Presumably a consumer advocate would increase the chance that a decision would have to be made to continue a case to the formal stages, since the decision not to act is, in principle, of potentially as much importance as the decision to make new policy or to impose different constraints on the regulated firm.—/

—/ Statement of Robert Pitofsky, Joint Hearings, 1973.

While converting more cases to formal processes imposes additional costs on both regulated firms and the regulatory agency,—/

—/ Avoidance of these costs may be the motivation of regulators to avoid formal proceedings. See Paul L. Joskow, "Inflation and Environmental Concern: Structural Change in the Process of Public Utility Price Regulation," Journal of Law and Economics, Vol 17 (October 1974).

this could be an important source of benefits from an advocacy agency as well. The refusal to undertake a formal process is sometimes based upon a desire by the agency to keep its actions secret, because the agency is either making unwarranted concessions to the industry or covering up a past decision that turned out to be mistaken.—/

—/ For some examples of the use of informal agreements to hide

decisions that were either proven to be wrong or excessively pro-industry, see the statement of Reuben B. Robertson, Joint Hearings.

In any case, the consumer advocate is likely to reduce the extent of informal decision-making. The courts have been willing to chastise agencies for excessive reliance on informal processes, —/

—/ For example, Moss v. CAB, 430 Fed. 981 (U.S. District Court for the District of Columbia, 1970).

so it is reasonable to suppose that the agency can find receptive judicial ears should it attack what it regards as an undesirable informal process or decision.

The critics of the advocacy agency are surely correct that the agency will increase the costs of regulation by more than the budget of the agency. And surely these costs should be weighed against the benefits in deciding whether its creation is socially desirable. But by itself, this argument does not support a definitive judgment about the agency. While the procedural costs generated by the agency are likely to be large -- conceivably several times the agency's budget -- these costs are still small compared to the estimates of the economic costs of regulation arising from inefficient operation of regulated industries. If the advocacy agency could succeed in changing just one of several nonsensical regulatory policies -- for example, the irrational route structure of the trucking industry or the rate structure of railroads -- it would recapture the costs it generates by several times over.

Spillover Damages

The debate over the consumer advocacy agency includes several issues that emphasize certain gestalt-like consequences of the creation of the agency. Two of these have been repeated often enough that they must be accorded some attention in a recitation of the case against the advocacy agency. They will be but briefly treated here, owing to my judgment that they have very little merit. —/

—/ Still other arguments will be totally ignored except to characterize them in the following partial list: (a) the real aim of the proponents of the advocacy agency is to undermine the American economic system (statement of John A. Stuart, Consumer Protection Legislation, 1971); (b) the consumer advocate will do severe damage to businesses by releasing trade secrets (statement by J. Edward Day, Joint Hearings, 1973); and (c) the threat of possible intervention gives the agency a lever over business to force it to do all sorts of things outside of the regulatory process, or, in the words of one apparently frightened soul, the agency will have "unlimited power to search and destroy by implication and half-truths" (statement of Herbert Liebenson, Consumer Protection Legislation, 1971).

The first such argument is that deregulation is a better policy than adding to the complexities of regulation. —/ The difficulty

—/ Statement of Ralph K. Winter, Jr., Joint Hearings.

with this statement is, of course, the implicit presumption that the consumer advocacy agency should be regarded as an alternative to deregulation in the instances when a good case can be made for the latter. If the advocacy agency truly represents the consumers'

interests, it will add another voice to the chorus calling for deregulation in the cases in which regulators generate substantial costs to consumers. If it is not a consumer advocate, then it will not make serious inroads on the cost of regulation -- and will not, therefore, reduce the political pressure for deregulation. It is instructive that the proponents of the advocacy agency do not even intimate that deregulation is an alternative to the advocacy agency; most support some deregulation, although they express skepticism that deregulation will actually occur.—/

—/ For example, see the statement of Peter Schuck, Joint Hearings.

In any event, should extensive deregulation take place, a substantial regulatory empire will still remain, especially the standard-setting activities. There is no compelling reason to believe that the desirability of deregulation in one regulatory arena reduces whatever desirability is attached to the creation of a consumer advocacy agency for the regulatory activities that will not be eliminated.

The second spillover argument is that the advocacy agency will destroy the incentive of voluntary trade associations to establish industry performance standards.—/ Presumably the prevailing

—/ Statement of John A. Stuart, Consumer Protection Legislation Hearings, 1971.

attitude will be to let the government do it since the consumer advocate is unlikely to be pleased with anything industry would do.

If the resources of the advocacy agency and standard-setting regulators were unlimited, this argument would make some sense. The advocacy agency probably would then want to have a role in all standard-setting activities, and the industry would no longer have an incentive to perform a function that the government was willing to perform for free. But agency resources are limited; the advocacy agency will not be able to intervene in more than a tiny fraction of cases. As a result, the advocacy agency will be interested in deploying its resources where payoffs are high -- which is not towards redoing reasonable standards promulgated by industry groups.

In fact, the presence of a small advocacy agency may increase the incentives of an industry to do an effective job of self-regulation. Apparently the home appliance industry established self-regulation with respect to such matters as uniform measures of the performance of an appliance (e.g., cooling capacity of air conditioners, storage capacity of refrigerators) largely because it feared that if it did not do so, the federal government would regulate the industry.—/ Creation of a consumer advocacy agency presumably

—/ Michael S. Hunt, "Trade Associations and Self-Regulation: Major Home Appliances," in Richard E. Caves and Marc Roberts, Regulating the Product: Quality and Variety (Cambridge: Ballinger, 1975). Incidentally, Hunt finds no evidence of anticompetitive effects of appliance self-regulation, concluding that it was "non-controversially desirable."

raises the costs of federal regulation to an industry, thereby increasing the incentive to avoid regulation through an effective self-regulatory scheme.

Unrepresentativeness

The most serious challenge to the consumer advocacy proposal is the argument that no federal consumerist agency can represent consumers. The reasons for the claim are: (a) the agency is too removed from consumers in that they do not elect its leaders or support it voluntarily, so that it is unlikely to face much incentive -- or even to gain enough information to determine how -- to benefit its natural constituency; and (b) the consumer interest is nonexistent in that differences in taste, income, age, residence and numerous other demographic characteristics make consumers too diverse a group to be well represented by a single advocate.

The truth of these contentions, as theoretical matters, cannot be contested. The economics literature on impossibility theorems, compensation principles and second-best problems should give anyone pause before claiming that any action -- or inaction -- clearly produces net social benefits, particularly when implementation of a policy requires the deployment of a characteristically unresponsive bureaucratic institution.

In fact, the problem may be even somewhat worse than has been suggested in the debate over the consumer advocacy agency. Regulation is, in principle at least, socially desirable when information costs are so large that the consumer has insufficient incentive to make himself informed enough to engage in optimal consumption decisions. As Tullock has pointed out, exactly the same phenomenon occurs when the voter must determine which candidate -- and, implicitly, public policies -- to vote for.[1] As long as the unanticipated

[1] Gordon Tullock, "The Social Costs of Reducing Social Costs," mimeographed, 1972.

consequences of consumption are, in expected value, less than the costs of information, a case may be made for standards regulation; however, a voter has little chance of actually affecting an election, and hence he has little incentive to learn which of the competing candidates will adopt the best regulatory policy. To make the circle complete, as argued above he also has little incentive to join a voluntary consumer group that will lobby politicians and regulators for him.

This dilemma, however, is not just a trait of regulatory policy -- and is not the one that motivated the title of this paper. Lacking the magical world of Lindahl pricing organized by an all-knowing philosopher-king, public good provision must always diverge from the optimum optimorum, whether the public good be national defense, a television program, information about a product or a safety standard.[1] To say that bureaucracy is unresponsive and the

[1] A "Lindahl system" is one in which each person is taxed exactly in proportion to the value he places on governmental activity. Its impracticality is legend. See, for example, Paul A. Samuelson, "Pure Theory of Public Expenditures and Taxation," in J. Margolis and H. Guitton, Public Economics, New York: St. Martin's Press, 1969.

political process incapable of finding a unique optimum set of policies is, then, to say very little while saying very much. The argument is no more destructive of the proposal for an advocacy agency than it is supportive, since the agencies with which the advocate must deal will also be unresponsive and unrepresentative for the same set of reasons. Nor is it even an argument for anarchy: in a sense, a social arrangement that provides no public goods, no matter how valuable, is remarkably unresponsive and unrepresentative!

The relevant representation issues for policy purposes are (1) whether in some important instances a widespread consumer interest can be identified and (2) whether, assuming a homogeneous consumer interest does exist, an advocacy agency is likely to pursue it. The second issue depends upon the motives, incentives and powers of the agency, and will be taken up in the next session. The answer to the former seems trivially to be yes. Few consumers stand to gain if an industry is able to convince a standard-setting agency that it should adopt performance standards that reduce competition within the industry but that make little or no contribution to the safety and quality of the product. Few consumers stand to gain from cartelization of industry pricing, such as takes place in transportation regulation, or from false information about product costs and performance. The main potential problem is whether the agency will focus its efforts on these types of issues, or will, instead, degenerate into a representative of a few additional narrow interests.

Conclusions About the Opponents

Like the proponents, the opponents of the consumer advocacy agency have relied on a set of theoretical arguments that, in the main, reduce to truisms. What the opponents have succeeded in showing is that a consumer advocate will increase the resources committed to the regulatory process but will not perfectly represent what is intrinsically unrepresentable.

Heading into the home stretch of the paper, neither side of the debate has left us with very much. The proponents have a good case that regulation often works to the detriment of the interests of consumers and that the advocate will change outcomes, but they really avoid the issue of whether the outcomes will be better.

Meanwhile the opponents have shown us that the change will have a cost and will not produce perfection.

What is lacking are some details on what the change will be like, so that at least individually we can judge for ourselves whether there ought to be an agency for consumer advocacy.

PREDICTING THE EFFECTS OF THE ADVOCATE

The consumer advocacy agency will be an unusual agency. In some ways it will resemble a regulated firm, in that its success will be dependent upon how it fares before regulatory agencies. Yet, like the regulators, its budget and authority will flow from Congress.

Let us assume that Congress is not completely insincere in setting up a consumer advocacy agency. In part, Congressmen expect the agency to have some effect on regulatory outcomes. Hence the agency will be rewarded according to the changes it can take credit for, the reviews of its performance in the media, and, of course, the favors it can do for the Congress. With respect to the last, the advocate might be able to deliver two types of favors: support from the constituency of the agency, and relief from complaints by the constituents of the Congressmen. Furthermore, to the extent that the agency, like the adjudicatory branches of the Department of Justice, becomes in large measure a training ground for young lawyers on their way to partnerships in Washington law firms, the desire to win cases will become a greater feature of the agency's behavior.

Like the regulated firm, the success of the advocate will depend upon its ability to develop a cordial relationship with the regulatory agencies. Friendly relations will benefit the advocate by easing its problems of collecting information, by leading the regulatory agency to consider its arguments more seriously, and simply by

enabling it to avoid unpleasant personal relations among individuals who must maintain relatively frequent contact.

This behavior stands in contrast to that of the voluntary activist organization. For the same reasons that consumers are generally less well represented in the regulatory process, those that are represented tend to be the ones who feel most passionately about the issues and whose tastes lead them to prefer an atypically great degree of government intervention into market transactions. They are likely to have above average income (the voluntary contribution to the activist organization means less to them), and above average sophistication about products (they care more about consumer issues, and therefore have more incentive to learn about product costs, quality, safety, etc.). Finally, since even for an activist the direct economic payoff to members of the voluntary association is unlikely to be large compared to its expenditures, activism is likely itself to be in part a consumption activity -- that is, hopeless fights against egregious but unchallengeable decisions may be enjoyable.

The preceeding argument suggests that the consumer advocacy agency will behave somewhat differently than the voluntary consumerist. The advocacy agency, with its greater incentive to produce concrete results attributable to its actions, will allocate its resources more toward issues that it can actually influence. That is to say that it will deal with agencies that are more flexible in their policies or that are vulnerable to appeals based upon the claim that their policies are illegal. The agency is also more likely than the voluntary activist organization to compromise with a regulatory agency and its regulated industry.

An illustrative example of the kind of interventions the agency is likely to undertake, according to this argument, is provided by

the intervention of the planning office of the Department of Transportation in the Domestic Passenger Fare Investigation of the Civil Aeronautics Board in the early 1970s.[1] In the proceedings DOT adopted

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[1] A first-hand account of DOT's role in the process can be found in George W. Douglas and James C. Miller III, Economic Regulation of Domestic Air Transport: Theory and Policy, Brookings Institution, Washington, D. C., 1974, Chapter 8.

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a subdued posture that aimed for objectives that were moderate in comparison with, say, those of the general run of academic economists who have studied the agency and called for substantial deregulation. DOT did not question the desirability of CAB regulation and did not attempt to influence all aspects of the DPFI. Rather, it had three aims: (1) to make the agency consider explicitly the tradeoff between price and service quality in its pricing decisions; (2) to obtain adoption of cost-based, rather than value-of-service, pricing; and (3) to introduce some "fare flexibility" -- that is, to make the maximum allowable fare differ from the minimum. If fact, the CAB's ultimate decision adopted most of DOT's ideas with respect to the first and the second aims, and the DOT participants with justification made a modest claim to having influenced matters.

The primary point of this example is to describe the style and methods that one government agency adopted in intervening on behalf of consumers in the proceedings of another agency. In contrast to the interventions of consumerist and environmentalist voluntary groups, the DOT presentation was highly specific in content, moderate in objectives, and cooperative with the agency. In return for this behavior, the CAB reciprocated by frequently referencing the submissions of DOT in laudatory terms.

Of course, the gains achieved by DOT have been assessed by even the participants as something less than revolutionary. The CAB decided to set fares on the basis of the costs associated with "target" load factors of planes. The decision probably will benefit consumers, but not nearly so much as would trunk line deregulation. And DOT did fail to achieve what was probably the objective that would have been most beneficial -- the adoption of flexible fares -- since that proposal offered the prospect of destablizing the cartel arrangements of the industry. The lesson of the DOT intervention at the CAB is probably that modest objectives beget modest results -- but results nonetheless.

While the consumer advocacy agency will be more closely connected to consumerists than was DOT, the incentives for moderation will nevertheless operate upon it. As a result, it is unlikely to engage in extreme, highly controversial consumerist activities, as has been the fear of some of its opponents, particularly as long as its budget prevents it from entering more than a small proportion of regulatory issues. In particular, it is unlikely to seek regulatory policies that limit the legal range of consumer products to those deemed most desirable by the activist, middle-class consumer since its incentives will differ from those of the private activist organizations. A more likely result is that the agency will be too timid, settling for small but clear-cut victories rather than running a high risk of a major gain.

One other danger arises from the result-orientation of the agency. The nature of the adversary process is such that a participant in it, when having the choice of issues in which to intervene, has a greater likelihood of success against relatively poorly represented groups. Consumerists, of course, do not constitute the only group that is vulnerable to a steamroller fueled by a wealthy interest group. The advocacy agency, too could take on steamroller proportions against

groups less well-represented than consumers. All other things being equal, an agency can expect to have greater success in affecting changes by picking on disorganized groups, individuals and small businesses. In fact, a Machiavellian purpose is even served by really laying into a few defenseless "violators" of the consumers' interests: occasionally hitting mules and/or businessmen with a plank is useful in getting their attention. Of course, it is not likely that Congress would reward an agency that devoted most of its resources to lambasting individuals; at the same time, the temptation to engage in a few such activities will surely be present.

An example of how this would happen is for the consumer advocate to press for expensive retroactive compensatory actions by a firm or industry in connection with a regulatory decision to upgrade the safety standards of its product. The early decisions of the Consumer Product Safety Commission exhibit some tendency to engage in severe punishment of small firms producing products the CPSC determines to be unsafe. For example, preliminary decisions in a case against a small manufacturer of an arc-welder not only forced the firm to adopt a safer design, but also required actions with respect to past customers that will probably bankrupt the company -- even though there is no record that the arc-welder ever injured anyone.[1] Meanwhile, the

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[1] Consumer Product Safety Commission Docket 74-4, Interim Initial Decision and Order, April 29, 1975.

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proceedings to establish industry standards for lawnmowers -- which are among the leaders in preventable deaths and injuries -- indicate that the agency will adopt standards that will significantly reduce the hazard of the product, but will not require retrofitting, replacement

or refunds for past purchases.[1] Aside from the Machiavellian benefits of arbitrariness, it is difficult to understand why law and agency policy should permit these unequal treatments which appear to be based on the resources of the regulated entity rather than on justice and merit.

Herein lies the dilemma of consumer advocacy. The agency must be small enough so that it does not intervene everywhere, but it must be large enough to intervene effectively against well-represented producer groups, such as the trade associations in transportation, the major firms affecting energy and environmental policies, and even Ma Bell. Yet to make it a potentially effective opponent of these groups requires that it have sufficeint resources to overwhelm the insignificant firm or individual finding himself before a regulatory agency -- or even having his fate decided by a regulator without his knowledge. The dilemma is compounded by the expectation expressed above that the agency is likely to be more moderate in its aims when dealing with the more potent firms and more inflexible agencies. Although this is not exactly synonymous with a tendency to score big victories in tiny battles while winning tiny incremental changes in the wars that really count, there is certainly a tendency in that direction.[2]

[1] Consumer Product Safety Commission, Power Lawn Equipment Proceeding for the Development of Safety Standard. (Notice: Federal Register V. 39, No. 141 (July 22, 1974).)

[2] This conclusion probably is amenable to empirical testing. Several states have established consumer protection agencies, but to my knowledge their behavior has never been the object of scholarly study.

As with most problems of the institutional design of public policy implementation, the foremost conclusion that one can reach is that no unqualified conclusion is justified. If one generally favors most of the standard-setting regulatory activities of the federal government and some of the price and profit regulation, one probably must conclude that a consumer advocacy agency is worth trying. This conclusion is based in part on self-interest: the more one likes these kinds of regulation, the less likely it is that one is threatened by the possibility of suffering an unjustifiable loss to the agency by being overmatched by it. But the conclusion is also partly based on the observation that the instances where regulation is most justified -- namely, the control of externalities, severe information problems, and monopolistic practices by giant natural monopolies -- are the very ones in which regulators are ripest for capture through a firm's strategic use of information and the inability of the political system to make an informed judgment on the performance of the regulatory agency. Threat though it may be, a consumer advocacy agency is probably the only mechanism yet devised that holds some promise of dealing with this problem.