REGULATORY CAPTURE IN THE 21st CENTURY

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OPENING REMARKS BY

SENATOR SHELDON WHITEHOUSE

SENATOR MIKE S. LEE

SENATOR ELIZABETH WARREN

PANELISTS

GRETCHEL MORGENSON

BRANDON GARRETT

HON. RONALD CASS

HON. JED RAKOFF

DANIEL CARPENTER

SIDNEY SHAPIRO

STEVEN CROLEY

NEOMI RAO

MARK CALABRIA

Reported By: Steven Poulakos

Job No: 104401
MR. WEINER: Good morning. Are you able to hear me? I am Matt Weiner, the executive director of the Administrative Conference of the United States which is often called ACUS. I'm joined today by the ACUS staff and several members of the ACUS assembly, two members of ACUS's counsel, Ron Cass and our vice-chairman Steve Croley, both of whom will be moderating rating our panels today, and finally the second most famous former chairman of the administrative conference, Paul Verkuil, who led the rebirth of the conference in 2010.

Our most famous former chairman is the late Anthonia Scalia, and if I may, let me just pause for a second and say that we'll always be very grateful for Justice Scalia, not only while he was its chairman, but also later as the Supreme Court Justice.

I would encourage you to visit the tribute to Justice Scalia on our website where you'll find his as well as Justice Breyer's 2010 congressional testimony in support of ACUS.

Thank you for joining us for today's forum. We hope that it will not only inspire a productive bipartisan dialogue about the subject of regulatory
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capture, but also that it will inspire those of you who are unfamiliar with ACUS's work to follow us and become involved in our work.

I won't stand between you and Senator Whitehouse any longer except to thank first Senator Whitehouse's and Senator Lee's staff, in particular Lara Quint and Sara Malwalze and Will Levi for helping us get this program off the ground this morning.

And, secondly, the House and Senate judiciary committees and their staffs who were there providing support of ACUS support, and finally Senator Whitehouse himself for suggesting this forum and otherwise contributing to our work.

SENATOR WHITEHOUSE: In the course of my life I have been an advocate in state and federal regulatory proceedings. I have served as a regulator, as both RI's director of business regulation and to a degree when I was Attorney General, and I have been both United States Attorney and Attorney General in seeing the prosecuting side.

So regulatory law is an area of long and considerable interest to me, and the threat of capture of regulatory agencies has long been a concern.

So I asked Director Donovan last year how
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we might do a better job of identifying and routeing out special influence within our agencies. Director Donovan listened and took the question right to the experts. I look forward to hearing what they have to say during the course of the day.

For my part, let me dare to open with a word of gratitude for regulation. Medicines are not snake oil mysteries any longer. People are rarely burned or killed in boiler explosions.

Automobiles have seat belts and airbags. Smokestacks have pollution controls. Stock jobbers have a harder time bilking innocent investors. Most insurance policies actually pay when the insured risk occurs.

Quacks and barbers can't be doctors. We take for granted the safety and reliability that a regulated world has built.

I think we also take for granted that regulation helps further our economic progress. Regulation help channel America's competitive enterprise into strong and valuable innovations instead of new tricks and traps for consumers or new ways of cutting corners.

Confidence in our industries grows when
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consumers know they can count on the safety and reliability of the product. Ask yourselves whether or not the American pharmaceutical industry would be a world powerhouse if patent medicine hucksters were still allowed to operate?

Regulation sets a positive frame for economic growth, and where they are common goods shared, like clean air, streams and oceans and unpolluted skies, there is always a perverse economic incentive to abuse such resources, leaving us all poorer. This is the principal described in Garrett Hardin's famous Tragedy of the Commons. Regulation is what constrains this perverse incentive and protects precious common resources.

Critics of regulation often argue that regulation can be overbroad, out of date, ineffective, or unduly burdensome. Of course that is true. Error and obsolescence occur in any human endeavor.

To maximize the economic benefit of regulation, we have to keep regulations efficient and up to date.

But my political experience is this: When the deregulatory crowd shows up to put this principal into practice and to champion the notion of burdensome
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regulation, the target is usually not some obsolete or inefficient technical regulation that probably needs updating.

In my experience, the targets have been the Clean Air Act, or the ban on insurance companies denying coverage to people with preexisting conditions. These restrictions keep Wall Street from disrupting the economy again.

So we have to be careful about not confusing a concern about burdensome regulation with licensing the worst abusers to go after the common will.

On the other side, there is a threat that is as least as great as burdensome regulation, which is the threat of regulatory capture. For example, when powerful interests gain improper influence over regulatory agencies.

The consequences can be catastrophic, as we saw in the Minerals Management Service and the BP oil spill, in the mine health and safety, administration and the SAGO Mine disaster, and in a sweep of financial regulators in the runup to the global financial melt down of 2008.

In each of these cases, and in others,
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regulatory agencies overly beholden to the regulated industries failed to protect the American people, and the consequences were very, very grave.

Fundamentally, agency capture assaults our democratic American government. It is "we the people" who pass laws through a democratic and open processes. Elected representatives fight for the public's will, and regulations enforce laws to protect the public interest. All is well until industries creep in, co-opt and control those regulatory agencies. When they do, the agencies are pried out of the matrix of our government of laws to become servants of industry and the public's voice, and the democratic process is lost.

The problem of regulatory capture has long been recognized. Woodrow Wilson explained more than 100 years ago, if the government is to tell big businessmen how to run their business, then don't you see that big businessmen must capture the government in order not to be restrained too much by it.

Regulatory capture has been discussed in the research of Nobel Laureate George Stigler in innumerable textbooks and horn books in administrative law and economics, even on the opinion pages of the
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Wall Street Journal.

Although the problem of capture can at times seem intractable, while at a judicial subcommittee hearing I chaired several years ago, I found broad, bipartisan agreement on a number of propositions.

Here’s what everyone conceded. First, agency captures a real phenomenon and a threat to the integrity of government. Second, the enormous stakes involved for regulatory entities create a powerful incentive to gain over regulators influence.

Third, most regulated entities have both organizational and resource advantages in the regulatory process compared to public interest groups that represent a diffuse public interest.

Fourth, the regulatory process, not the result, the process itself, can be gained by regulated entities allowing them undue control and influence over regulation. For example, a regulated entity can overwhelm an agency with comments, delay, or perhaps even halting its regulatory process.

Fifth, regulatory capture by its nature happens in the dark, done as invisibly as possible. No capturer plants a public flag on an agency that they
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control.

Sixth, the potential damage from agency capture, as we have seen, is enormous, and finally effective Congressional oversight can keep regulators focused on the public interest and defend against capture.

Given the general agreement on these propositions and given the sense of academic history on regulatory capture, it is surprising to me how little attention has paid by Congress. My first question in preparing a hearing was: What previous hearings have there been whose record we can build on, and after due exploration the answer came back, none. There is a surprising lack of practical study of regulatory captures symptoms, its defects, and its cures, and there is virtually zero government effort to systematically identify it, prevent it, and root it out.

We respond episodically after a captured disaster, but no one in the United States government has the job of seeking to define, and locate, and prevent, and cure regulatory capture.

This weakness needs to be addressed. It is a matter of simple good government and it need not be a
partisan issue. Whether you think that agency capture is a symptom of excessive or inadequate regulation, whichever economic interest you think poses the greatest risk of capture. And however you think capture should be resolved the process of making government work well is one area in which we ought to have common cause.

I'm delighted that ACUS has provided this opportunity for a real discussion of what regulatory capture looks like and how best to confront it. I look forward to the remarks of my colleagues, Senators Lee and Warren, and to the insights of the two expert panelists on the role of capture in both rule-making and enforcement settings.

So thank you all for your interest. I hope that we are embarked on a journey that may take some time, but that will lead to a destination where there actually are results.

I thank you very much.

UNIDENTIFIED SPEAKER: Any questions for the Senator?

SENATOR WHITEHOUSE: I'm from Rhode Island. I don't just take questions, I take comments and rude remarks. (inaudible)
ATTENDEE: So as you pointed out, regulatory capture has been identified problems for several decades now, and one of the initial responses to the problem was to create new procedures in certain ways that mitigate or prevent regulatory capture, for example, something like the notice; but as you also pointed out in your comments, those processes themselves have been capture by (inaudible). And comments, so I guess procedural solution to regulatory capture is that real capture itself and what preventative steps can we take to address that problem as we seek out new solutions --

UNIDENTIFIED SPEAKER: I don't know that it's easy to find a process solution that can itself be gained. As a general proposition transparency is a good thing, but transparent comments entered by the millions can jam up the regulation and allow the status quo to be promulgated, and there transparency didn't help you. So it's not final answer.

I would like to speak to someone, perhaps at OMB or perhaps a roving inspector general for capture, who has the task of creating a matrix of warning signals of regulatory capture.

I think in this room we can agree on a
number of them off the top of our heads. How much money flows through or is affected by a particular body. How isolated the small body itself is. If there's no real public interest in what it does other than that industry and it has a huge economic effect on the industry that (inaudible) proposition, a chart of what the turnover is between industry and the leadership of the agency, continuing examination of whether there are improper benefits going back and forth.

We should have known in advance that MMS folks were being taken on shooting trips and having drug and hooker parties and being flown to the Peach Bowl on private aircraft, and examining rigs owned by companies with which they had an employment application pending before the whole damn thing blew up; but it was really nobody's job to look for that, and if you are the agency, then it's embarrassing to point that stuff out, it's bad for (inaudible). You can be isolated and squeeze that agency, and so it's got to be somebody else's job to be the bad guy.

So those are some of the thoughts that I have, but I think you can't cure it through process alone. It's got to be somebody's job to say where the
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places we need to work are, and then make a public report and listen in the same way that National Transportation Safety Board does after a plane wreck or something, like what went wrong, go back and do your report of what went wrong, those kids that got incinerated. There's a pipeline leaks was completely taken over by the pipeline companies.

It shouldn't be that hard. If we can find Osama Bin Laden, we ought to be able to find regulatory capture.

ATTENDEE: Well, I appreciate those examples of what I think are outright examples of the definition of regulatory capture. I wonder whether your conception of capture also includes areas where rules are really not as predictive in keeping up with the special intent around environmental and health and safety objectives as they might be.

In other words, capture seems everlasting, but there seems like about a spectrum.

UNIDENTIFIED SPEAKER: In that matrix we could easily have an independent review of what appeared to the independent reviewer to be Congressional intent and compare that to what the agency is doing, at least to bring to light that our
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reading of the statute is that it should be X, Y, and Z. Their reading is only A, B, and C. Is that a red flag? It's not final, but it can be added to the matrix (inaudible) of, and, yes, I agree with that.

And then look at the SEC right now. It has been captured completely, deliberately, and overtly and it's the intention of half of the commission's members to have it be, in fact (inaudible) that there's all sorts of ways it can happen.

ATTENDEE: Can I make one follow up on that?

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UNIDENTIFIED SPEAKER: Yes.

ATTENDEE: What is your view of the appropriate role of the office in the infringement regulatory affairs, because as a public interest advocate in the regulatory process, we often find their hand behind things. This weakens the rules and creates that gap seen in the MS solution and I think it's time for an examination of the executive order (inaudible).

I would be open to that. It's a recommendation that I have made. I have clearly seen, particularly in environmental rules that were taken to OMB and put on the White House and left there to die. And so a process has been capture. We have been
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advised by the political effort in the White House -- it doesn't have to be an industry that captures the agency. It's truly supposed to be in foundation and having worked and stopped one of the environmental was an actually bipartisan with the Bush Administration the Obama Administration also (inaudible) article the way they sat on some of the these environmental when they matrix my want to protect. I see Senator Lee there and I don't want to keep you.

UNIDENTIFIED SPEAKER: (inaudible) (no microphone used)

SENATOR WHITEHOUSE: I don't think we can stop looking at the agency. I think if we had a good model we're looking at agency capture, the parallels next to what's happening in Congress on certain issues with some sharper relief, I think that would be good for the public. Thank you all very much and I welcome Senator Lee (applause).

CHAIRMAN VERKUIL: I would just like thank Senator Whitehouse for his illuminating remarks which have given us much to consider, and I'd now like to introduce our next visiting speaker, Senator Mike Lee.

Senator Lee is a member of the judiciary committee, a chairman of the subcommittee on antitrust,
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competition policy and consumer rights as well as an accomplished appellate lawyer and public servant.

The Senator is also a friend of the administrative conference and participated in our last forum on criminal justice in the regulatory state.

Known for his rigorous focus on regulatory reform, the senator is working on a creative project to reinvigorate the Congress' role in the administrative state, and we look forward to his remarks. Thank you.

SENIOR LEE: Thank you very much, Chairman Verkuil, for hosting today's event. Thanks for all of you being here. Thanks to everyone involved in the Administrative Conference for the attention you've brought to the important issue of regulatory capture, and thanks for the invitation to let me come speak with you about this important issue.

It's not everyday that I'm invited to speak along-side my colleagues Senator Whitehouse and Senator Warren. On paper you might think that the three of us don't have very much in common, and yet here we are, to progressive democrats and one conservative republican speaking at the same venue on the same topic because we're committed to the same cause: Fighting regulatory capture in all of its pernicious forms.
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This is a testament to the emerging consensus among policy makers, scholars, and activists on both sides of the political spectrum, and everywhere in between the consensus that sees regulatory capture for what it is, one of the most pressing political, economic, and indeed moral issues of our time.

But too often, especially on Capital Hill, this consensus tends to breakdown along partisan lines with members of both parties are often guilty of railing against regulatory capture, what is politically convenient for them, and looking the other way when it's not.

For betterment observers in Washington this pattern of very selective outrage may be predictable, but it doesn't make it productive nor does it mean that we simply have to tolerate it.

As I see it, the only way to truly combat and ultimately reduce regulatory capture is to end what I describe as the conspiracy of acquiescence that has influenced Senates, Houses and Presidents of every conceivable partisan combination.

There's no legitimate reason why some regulatory agencies should fall under intense scrutiny of their cozy and collusive relationships with
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regulated industries and special interests, while others are simply given a pass.

If we oppose regulatory capture within the Securities and Exchange Commission or within the Federal Reserve we must also oppose it within the Environmental Protection Agency and the Federal Communications Commission.

Likewise if we oppose regulatory capture when it leads to the selective under-enforcement of agency rules we must also oppose it when it produces excessive regulations that distort markets and protect incumbents.

This is the approach recommended in the collection of essays that inspired today's event, preventing regulatory capture.

In this volume's introduction Senators Daniel Carpenter and David Moss provide a useful definition of this the phenomenon, one that accounts for its variety, its scope, and its many forms.

As the authors put it, regulatory capture is the result or process by which regulation in law or application, is consistently or repeatedly directed away from the public interest and towards the interest of the regulated industry by the intent and action of
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the industry itself. But it's not just private

for-profit companies that engage in regulatory capture.

Carpenter and Moss are quick to point out, it's not

just possible, but common for special interests, other

than regulated industries, to capture a regulatory

agency.

In fact, labor unions and nonprofits, no

less than wealthy corporations and Wall Street

megabanks, are capable of and interested in capturing

regulators in order to advance their own narrow focused

interests. In other words, regulatory capture,

properly understood, is a symptom of the perennial

tension between the public interest and the cacophony

clashing private interests at the heart of our

republic.

James Madison called the inevitable

conflicts that arise from this tension, "The mischiefs

of factions," and he believed, along with the other

framers, that the American constitution was uniquely

equipped to limit the power and influence of special

interests factions that would otherwise tug at and

exert an enormous amount of pressure on the fabric of

our society. At the core of the founders'
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principles.

First, the laws that govern a nation and
direct its economy should be written by people who are
elected by-and-therefore, stand accountable to the
public. That's why Article 1 of the Constitution, in
fact, Article 1, Section 1, Clause 1, the very first
operative provision of the entire document itself
grants all federal and legislative powers specifically
commerce. Why, because that's the branch of government
that the framers properly understood as the most
accountable to the people.

Today, we also have special interest
factions, and the government privilege they seek in
obscurity, whereas it's much more difficult to
understand the public interest to undermine, rather,
the public interest when policy and decision-making are
both visible and accessible to the average citizen, the
average voter.

Second, the powers of government should be
separated so that the people who write the laws are not
the same that as those who enforce the laws or
adjudicate disputes that regarding the meaning of those
laws.

When these powers are combined in a single
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entity, when we fuse these powers, the incentives and the political rewards and regulatory capture increase traumatically in a way it's manifested on the public interest.

Our constitutional system was set up to operate according to these basic principals. this is not how the federal government works today. Today, you see, the vast majority of federal laws are not passed by the House and Senate and signed by the President. They're written by unelected bureaucrats, by a decision-making process that is opaque and highly technical.

Precisely the kind of venue is susceptible to capture by concentrated interest. As creatures of the Executive Branch, these bureaucrat agencies also have the power to enforce the very rules and very regulations that they themselves write, and, in many cases executive agencies wield a quasi-judicial power through administrative law judges.

Proponents of this combination of this insularity and centralized power within the executive agencies claim that these innovations on the framers' original design are necessary in order to protect it against regulatory capture, but this is an ironic
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argument because experience has shown that precisely the opposite is true.

Concentrating the powers of the judge, the jury, and the executioner in a single government body made up of individuals who never stand for election creates an environment where there's an easy high-value target with special interest factions vying for access to the lever of power in pursuit of their own interests.

It's not that they're pursuing their own interest that's the problem. We've concentrated all of these talents in a limited, unique, and successful in a way that makes it far too easy for them, in fact, inevitable for them to manipulate those powers.

The point here is, of course, not to assign blame or to impugn the motives of any of the parties involved in regulatory capture. I know firsthand that the men and woman who run executive branch agencies as well as those employed by the industry's special interest groups affected by federal regulation, are themselves hard working, well intentioned, well educated and highly specialized.

The vast majority of the time, the parties involved in regulatory capture, are not themselves
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corrupt, dishonest, or acting in any way that we can describe as illegal; but that's precisely the problem.

The status quo arrangement of incentives and power within the modern administrative state has made regulatory capture all but inevitable. It just gives, it gives by virtue of the way that it's set up of the structure.

The American constitution was written by people who understood, as James Madison wrote in The Federalist Papers, that the latent causes of faction are so into the nature of man.

So the constitution for that very reason establishes a system that divides government and makes lawmakers dependent on the people in order to make it as difficult as possible for the mischiefs of faction to systematically direct the law away from the common good.

The modern administrative state flips this theory on its head, consolidates power, and assumes that good intentions will always overcome the latent causes affection.

This upending of our constitution quarter was not accidental and it didn't just happen overnight. Over the close of the 20th century, and accelerating
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into the 21st, Congress has steadily and voluntarily
and quite deliberately surrendered its constitutional
law-making power and its responsibilities to the
Executive Branch.

One of the unintended, but absolutely
undisputable, consequences of Congress recasting itself
as the backseat driver in American government.

It's been to move the bulk of law making
into bureaucracy where the opaque and highly technical
decision-making process facilitates regulatory capture
by concentrated interest.

This has led not only to bad policy, but in
inexorably to greater public distrust for our
government institutions. So it should come as no
surprise that the movement against regulatory capture
is gaining a whole lot of momentum at this precise
moment in our nation's history.

If there's one thing we know about American
politics today, one thing that we can all agree on is
that there is a deep and growing distrust between the
American people and our political system in Washington.
No matter where they live or which party they support,
most Americans no longer believe that we have a
government of, by, and for the people, and in many
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cases they're right.

Increasingly what we have today is a government of unelected officials with a degree of job security that would make tenured professors seem envious. A government by well-connected market incumbent and fashionable special interests, and a government for the benefit of political and economic elites.

Regulatory capture has played an important role in building today's discredited status quo, and just as importantly in insulating it from reform and insulating it from the very dynamics in our society.

So any efforts to win back the trust of the American people, as both political parties surely hope to do in years ahead, must include as a part of its agenda an effort to rain in the agencies and to regulate the regulators.

The goal of our reforms can't be to target (inaudible) or another while leaving untouched the dysfunction and culture of capture throughout the rest of the bureaucracy. We need to elevate personal over party and pursue structural reforms that make Congress once again responsible both in the sense of discharging its constitutional duties and also in the other equally
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important sense of making it directly accountable to
the people.

Two such reforms that I support and call to
your attention today are the Reins Act and the
Regulatory Accountability Act. I say Act in an
aspirational sense here.

These are bills not yet laws but, bills we
hope one day that they will become laws. Each in his
own regulatory agencies and the rules they issue under
closer Congressional supervision, which is to say, it
would make what is now a headless fourth branch of
government accountable once again to the American
people.

These are not partisan proposals and
there's no good reason why they can't achieve the
support of both political parties. Strengthening
Congress so that policymaking is more transparent and
more accountable to the public is not itself a partisan
project. It's about putting the federal government
back to work for the American people.

This is the goal that I share with Senator
Whitehouse and Senator Warren and I share in common,
even though we may not always agree on exactly how to
get there, and it's that common commitment to restoring
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a government of, by, and for the people that gives me hope for the future of the country and for the future of our collective fight against the phenomenon of regulatory capture.

Thanks to all of you for all you do in this effort. I look forward to working with you in the months and years ahead and look forward to achieving a degree of victory in this area.

Thank you very much.

UNIDENTIFIED SPEAKER: I move directly to our first panelist.

UNIDENTIFIED SPEAKER: While regulatory enforcement is usually defined in terms of the enterprises that adopt regulations, there's also a side of the capture equation that deals with the enforcement of regulation, and even though this is not thought of as commonly, it is often the part that gets criticized in public when you ask why wasn't a prosecution brought or why was it brought, why was this particular punishment handed out, or why was it not given.

Senator Whitehouse asks that we take a look at the practical sides of things. So we have assembled a panel that includes an academic, a journalist, and a judge, three people who, of course, have the most
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practical jobs you can think of. They also happen to be experts in the area. I'm going to introduce them briefly and then turn the program over to them and then we'll have a discussion among ourselves.

First you'll hear from Brandon Garrett who was Just Thurgood Marshall's professor of law at the University of Virginia. Professor Garrett is also the author of two extremely successful books, the Harvard University Press, one Convicting the Innocent, and the other called Too Big to Jail. We expect these to be made into major motion pictures at some point in the near future. You will see that he is somebody that publishes at the Harvard University Press and other university presses. You can tell a book is a success when it's bought by someone outside of the immediate family. It's very important that those of you write down the titles of the books we mention today and go out and buy them immediately after.

Our next speaker will be Gretchen Morgenson who is a book business financial editor and columnist at the New York Times. She's also a Pulitzer prize winning reporter, and her book, Reckless Endangerment deals with the role of Fannie Mae and the run up to the financial crisis.
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Our next speaker will be Judge Rakoff of the U.S. District Court, the Southern District of New York. Judge Rakoff is extremely well-known and he is often accused of being an academic masquerading as a judge because of his many writings and his deep learning. I think actually that he was persuaded that the pay in academia was too high and he thought the judgeship was a suitable alternative. You can find his writings in academic journals as well as the pages of the New York Review of Books.

Let me turn this over first to Professor Garrett and then we'll go down the line and come back with questions.

PROFESSOR GARRETT: So my name is Professor Garrett. I teach at the University of Virginia in Charlottesville. It's somewhat sobering that this illustrious group -- and thank you for inviting all of us. It's sobering that this group decided to have Judge Rakoff and I here to talk about criminal prosecutions at an event on regulatory capture.

The last agency would one hope or expect to be influenced by special interests would be federal prosecutors, who are among the most powerful enforcers of their kind in the world.
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Normal prosecutors normally follow akin to regulators enforcing policy. They enforce criminal laws and they put the bad guys in jail; but corporate prosecutions are more complex whether the target is a corporation itself or officers and employees, and they do serve regulatory roles.

I think it's a very good thing that the public is increasingly demanding greater accountability for corporate crimes. And to give an example, I'd like to briefly take the case of HSBC, particularly because that case unfolded here in the Senate in June 2002.

The soon to be former head of compliance at HSBC said this -- he was before the Senate subcommittee on investigations and he said, as I thought about the structural transformation of banks compliance (inaudible) the group that is, now is the appropriate time for me and for the bank or someone new to serve as "the head of group."

Basically his testimony began with, I quit. So the subcommittee's remarkable investigation -- he ends it, by the way, everything is going to be much better now that I'm not at HSBC.

The subcommittee turned up millions of pages of documents and produced lengthy reports, which
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are available on line, and they uncovered not just a compliance problem or a weak anti-money laundering program at the multinational bank, but billions of dollars that had been diverted to a who's who of legal activities and organizations.

Mexican drug cartels with links to terrorism, sanctioned regimes and others. The scale of the violations was shocking and it could have resulted in any number of criminal cases and not just one.

Prosecutors described concerted efforts to hide dirty money transactions with e-mails and internal notes that the subcommittee here at the Senate turned up saying things like, care sanctioned country, do not mention our name in NY, or do not mention Iran.

So it's amazing what people put in the e-mail. When HSBC compliance officers raised alarms they were disgruntled or ushered out, and all of that was in wonderful e-mails that the subcommittee turned up as well.

Now, later in that year in 2012 HSB settled this case, one case, with prosecutors. Any number of the things described in the subcommittee reports could have supported and had a large criminal investigation.

The case was settled, so the banks were not
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convicted of any crimes, and so individuals were not charged. This is criticized in editorial pages around the country, and by members of Congress, and the press.

That was the same day that prosecutors filed their case in the Eastern District of New York. They asked the judge to approve what is called a deferred prosecution agreement. Typically that is for low-level individuals, juveniles, first-time offenders. This case would be put on hold to give the bank a chance to show it's compliance.

Now, a money laundering conviction could have resulted in termination of the bank's U.S. charter. The bank was instead in charge of money laundering, it was charged with violations of the Bank Secrecy Act.

At the time Assistant Attorney General Lanny Breuer explained: Our goal here is not to bring it HSBC down, it's not to cause a systemic effect on the economy, it's not for people to lose thousands of jobs.

After the entry of this deferred prosecution settlement HSBC shares rose. Shares in the Senate on both sides of the aisle were calling it a "too big to jail" settlement.
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Senator Grassley said functionally, HAASBC has quite literally purchased a get-out-of-jail-free card for its employees for the price of $1.92 billion. Senator Jeff Merkley called it a "too big to jail" approach. Senator Elizabeth Warren stated that, evidently, if you launder nearly a billion dollars for drug cartels and violate our international sanctions, your company pays a fine and you go home and sleep in your own bed at night.

One of the most remarkable stories in all of American criminal law is the recent rise of the corporate prosecutions. I describe in my book, "Too Big to Jail", how billion dollar fines have become normal events. I assembled a vast database of corporate prosecution agreements and plea agreements from the past decade and beyond, all available online. This past year, 2015, corporations paid record sums exceeding $9 billion in penalties to federal prosecutors.

Now, those remarkable stories (inaudible) recent rise of prosecutions. Gone not seek billed fines in appropriate criminal cases, such as the HSBC case, a decade ago and it is true that companies have obtained more and more in the way of financing every
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year over the last decade.

This past year 2015 companies paid sums exceeding $9 billion for penalties to federal prosecutors.

Now, companies cannot literally be put in jail, of course. And that is why adequately holding them accountable is so important. Responsible officers and employees can be targeted. Firms can be structurally reformed, but only if compliance requirements are taken seriously. Often they are generic and need not be audited. Firms can pay deterrent fines and compensate victims.

Yet many companies pay no fine, and even the biggest payments are often greatly discounted. More companies are not being prosecuted each year; fewer and fewer are prosecuted in federal court. Speaking of individual defendants, like in the HSBC case, almost two-thirds of those corporate prosecutions were not accompanied by any charges filed against employees.

The DOJ has accounted recent changes to focus more on individual investigations, in response to criticism. Although interestingly in the HSBC it is not over. It has been several years since the deferred
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prosecution was entered, the DOJ is fighting release of the report of a monitor who has been supervising compliance.

The judge of Eastern District of New York, Judge Gleason, thought that it was in the public interest to publicly read a thousand page document describing several years of the agreement combined with (inaudible) at HSBC, and a concern that the systems are in place to prevent future crimes of the same type.

So perhaps more resources for corporate investigations, and more of a sea change in priorities is needed to end "too big to jail" once and for all.

I'll stop there, and I really look forward to discussing all of these issues and not just in the criminal areas.

UNIDENTIFIED SPEAKER: Thank you very much.

MS. MORGENSON: I'm Gretchen Morgenson. I'm reporter for the New York Times, and I discovered multiple crisis that have occurred and our financial markets since 1998. In the aftermath of the 2008 financial crisis, Congress (inaudible) into act writing on legislation that was designed to insure income that such a devastating effect would never again occur.

Some 390 new rules have been written under
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Dodd-Frank, and according to the latest poll, who's tracking on it, only 68 percent of (inaudible) by the end of 2015. The brief rules have not yet been posed at the end of last year, for the five years after Dodd-Frank.

Since writing the new rules have is complete, I know that (inaudible) hours will tackle the important issues of regulatory capture. By I do think statistics up to date illustrate a larger (inaudible).

While it's nice to believe that a rash of new rules will protect Americans from future bailouts and pricing, this is naive. Indeed one of the most evident things about our current regulatory regime, especially in the securities division, is the frequency with which regulators do not enforce the rules that are already on the books.

I'll refer to one particular instance of the (inaudible) factors of the SEC provide so-called wage earners to respondents in. By providing waivers to system regulations regularities are declining to use a powerful enforcement tool that could help.

Four years ago a former colleague of mine, (inaudible) was reporting that on the numerous cases for the SEC case (inaudible) institutions of half
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(inaudible). As of now, there are 350 instances where the SEC provided (inaudible) attorney cost to firms that were such action to enforcement action.

And (inaudible) about that or JC MorganChase in settling six fraud cases they also approved 22 (inaudible)of regulation. In granting the waivers, the SEC, has apparently bought into the bank argument of, quote, strong record of compliance.

Even worse, half of the waivers identified in the report went to repeat offenders. Wall Street firms had settled some previously fraud charges, by agreeing to never violate the laws, the SEC regulators said (inaudible).

Among those security waivers are those that allow the SEC to continue to manage clients money. Another couple of examples would be well-balanced issuers of waivers which allow firms that have violated antitrust provisions of the securities laws to continue raising money to streamline stocks and (inaudible). Thankfully such waivers have recently grabbed the attention of Kara Stein, an SEC commissioner.

Lastly she instructed her (inaudible) waivers provided to JC Morgan, CVS, Barkley, Citi Group, and RMBS in a case involving manipulation of
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foreign exchange rates.

Saying that the special treatment has, quote, effectively rendered criminal convictions of financial institutions largely symbolic, she argued that with these tools, the SEC has the responsibility to assure that those lending institutions will create meaningful changes in their culture. Yes, we (inaudible) use them she says.

Now the SEC is often outmanned, outspent, outgunned. If that argument brings solace, well, even to use the tools that have had disposal to change, the routines of the look regulatory captured. And there's only one for example.

As Senator Whitehouse said in his opening remarks, regulatory failure prove out the year leading up to the financial crisis in 2008 and (inaudible) its impact. The willful blindness of regulators to recognize the risk that was building up in the banking industry was (inaudible) and yet many of those same regulators receive greater power in the aftermath.

The regulatory capture is real and it is furnished and I applaud the response for an important program to try to address it thank you.

JUDGE RAKOFF: Thank you. My name is Jed
Rakoff. It's my privilege to be a Federal District Judge for the last 20 years, but my comments today are offered strictly in my personal capacity, although, of course, they are colored by the cases that I've seen in my court in the Southern District of New York where cases involving the financial industry are often brought.

I second Professor Garrett's comments about the shortcomings of deferred prosecutions and nonprosecution agreements and the like, that have been brought against corporate entities and financial institutions.

Every case is different. Too many cases against corporations appear chiefly to realize innocent employees and shareholders and appear to have achieved very little in the way of (inaudible) futures (inaudible).

But to use the more striking (inaudible) is that these prosecutions and the parallel regulatory proceedings have rarely been brought against the individuals who actually committed the crimes.

The individuals who actually committed the crimes should be brought to justice as a matter of simple morality. Moreover, in my experience, there's
mush more deterrence when you go after the individuals. This failure to go after the individuals is in striking contrast to practices in prior decades. For example, in the savings and loan crisis that culminated in the early years of the and loan crisis of the 1990s, no fewer than 800 executives were successfully criminally prosecuted for their fraud and for concealing the increasingly risky investments in which those institutions were (inaudible).

These prosecutions of individuals included many high-level executives, including Charles Keating Junior, who was, in the eyes of many, the originator of the fraud, by comparison, even though the Department of Justice and the Securities and Exchange Commission have in recent years successfully brought high-profile cases against financial institutions for the fraudulent practices that led to the financial crisis.

In none of these cases has any high-level executive been criminally prosecuted, and even in the civil simple regulatory cases only a very few executives have been proceeded against. As Professor Garrett just mentioned, Deputy Attorney Yates has commendably called for greater emphasis on individual prosecution, and we'll see the results.
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Now, I'm in no position to say whether the prior failure is the result in part or in total of regulatory capture or not, but I would note that historically successful prosecutions in the financial arena had been the product of joint investigations by Department of Justice and the relevant regulatory agency, whether it be the SEC or the OTS or the OCC or whatever.

You may recall that in connection with the S&L crisis, Senator Cranston of California was formally reprimanded for trying to derail the joint DOJ and regulatory investigation of Mr. Keating.

Nothing like that has been alleged in the financial crisis, but the failure to prosecute high-level individuals in connection with the financial crisis still stands (inaudible) in sharp contrast, to prior scandals where such prosecutions were common and successful.

It's really hard to escape the inference that the great recession which caused and continues to cause so much suffering was in part the result of fraudulent misconduct where in increasing risk was increasingly disguised creating a bubble.

One cannot help but ask, why have the
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individuals who inflated that bubble not been brought
to justice. Thank you.

UNIDENTIFIED SPEAKER: The questions
discussed of the relationship between the prosecution
of enterprise and individuals, and a lot of times
academic writing has speculated on which is more
effective.

And I know that you were just saying that
there ought to be a shift and more prosecuting
individuals and certainly the Ace Memo of last
September lays that out; but I want to ask both
Professor Garrett and Gretchen whether you thought that
this was something you needed to see more of, and to
the extent we haven't seen it, is explained by capture
of some sort or by other considerations without the
extent of your (inaudible).

UNIDENTIFIED SPEAKER: Well, I want to say
two on things about that. I do think it's important
that corporations be the target of criminal
investigations. One of the things that you would
especially be able to do is figure out who did what and
to target responsible individuals.

When the organizations help the
corporations that are cooperating, the corporations
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(inaudible) to cooperate, the prosecutors and turnover documents, turn over e-mails that are privileged, and you think that that should be an enormous benefit. That should make it easier to sort out.

This is a complex organization and there are a lot of people involved in that illegal business scheme, and it's unfortunate that that power (inaudible) of cooperation hasn't been used effectively in the past; but the Yates memo changes from the Department of Justice.

It suggests that (inaudible) individuals must be prioritized individuals early on in the investigation, and the case of (inaudible) acts in the past years ago by a corporation that describe the conduct, the clock is ticking and the prosecutors decide, you know, we can't wait years worth to (inaudible) mandate who it was and to solve the case; but the experience of federal prosecutors when they have targeted individuals and other cases suggest that there's also serious resources concerned.

Many individuals are prosecuted, for example, who have been called for marketing illegal tax shelters, the prosecutors pretty readily (inaudible) for example, KPG and other corporations. The case
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against individuals, and there are a couple of them, and many of them are (inaudible).

Now, we see those cases costing millions

and millions of dollars in the prosecution, and we are beginning to have a couple of U.S. attorneys negotiate for prosecution agreements with the companies so that they have multiple employees, separately or represented by different law firms, counsel all of sudden to bring a case pending before it's complete.

Just a couple of months ago, we had a CEO prosecuted in a nasty coal mine explosion in West Virginia, and the prosecutors with the cooperation of supervisors who worked their way up the chain and that eventually decided to have evidence to prosecute the CEO. In contrast that we have other cases of prosecution agreements with other people (inaudible) where people died and individuals were wrongly convicted of (inaudible) and did those prosecutors think of it as resource question, even they (inaudible) or is it they stayed after a press conference, according to them they didn't see evidence of intent (inaudible) for people to really look into the case and weren't so quick to sign the agreement (inaudible) capture or inadequate resources or inadequate will,
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(inaudible) all that matters is resources (inaudible).

MS. MORGENSEN: I don't understand what a lawyer has to do to (inaudible) but all I know is that when I look at SEC settlements, (inaudible) settlements damaging an (inaudible) upsetting tab, I don't see anything from the individuals who perpetrated those acts, and I just can't help asking myself why.

The corporations didn't do the deed, some person or persons inside did, and shareholders end up paying, and so the consequence that (inaudible) deeply that Americans have to the regulatory system, but I don't really know what the answer is.

I do think we have to bear the impact of the revolving door where individuals leave their regulatory entities in the law firm and either represent or do not represent individuals or are pursued by that regulatory entity.

Obviously, people are entitled to be represented by the best that money can buy, but that seems to me is certainly part (inaudible) of the individual.

I think the SEC is reluctant to meet the challenge to go after individuals, and even when it does go after individuals, I think the actions taken
are passive in a way. The fact that the new century should be (inaudible) is that the (inaudible) very early on in the crisis, and there was actually accountability professionally, you know, at the time that the (inaudible) companies played out a monitor in the (inaudible) and bankruptcy on waited out chapter and versus hundreds of pages belonging to this report, gave the SEC a roadmap to how this group of executives had cooked the books and the fines and penalties that were extracted (inaudible) legal work. So in that case I looked at a large (inaudible) why the reluctance? Why not throw the book at them?

UNIDENTIFIED SPEAKER: One raises the question of the possibility of individuals and corporations, and you mentioned the change from the S&L crisis to the subprime crisis.

How many of them do you think is explained by the nature of regulation at issue? We have more complicated regulations where the actual informal regulations (inaudible) and predisposed prosecutors who want to go after individuals less and enterprises more or do you think that there's been a change in the nature of leverage with respect to particularly some of the larger players in terms of the potential public
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impact and the resulting fines that you get as a result or did you have something else in mind.

JUDGE RAKOFF: I'm inclined to think it's something else. When I was a federal prosecutor I had the good fortune to be chief of the securities and business fraud unit in the U.S. Attorney's Office in the Southern District of New York, and we considered it a defeat if we could not find the individuals who had committed the crime, who actually had done the deeds, as opposed to going after companies. We almost never went after companies. Effectively we didn't think it was fair to the shareholders and employees of those entities that I mentioned in the S&L crisis, but the same was true of the accounting crisis that led to a WorldCom and Enron, where the very highest level CEOs of both companies were successfully prosecuted. There's a long history of successful prosecution of individuals.

These are not easy cases to prosecute, but it can be done. In the future there's high regulatory capture, whether that's the (inaudible). I think another element has been certain politics of that situation.

If you're a large institution and the
government's going after you and the regulator that you have to deal with is a going after you, you're going to have to come to terms with them on some terms.

You will attempt to get the best terms possible, and if there has been some degree of regulatory capture or revolving door or whatever, you may get terms that are not that onerous that you can view as just the cost of doing business, but ultimately you're going to have to come to terms.

So these are easy pickings for the government in a certain way. They can say we have today reached an agreement with fat cats and they're going to pay a great big fine and they're going to engage in compliance measures and sometimes they're going to have the monitor, and it sounds real good.

It's much harder to make the cases against the individuals, but you can and it historically has been done. Professor Garrett made an excellent point a minute ago where he pointed out that there has been much less use of the banking institutions themselves to cooperate against the individuals within their own community that actually committed the crimes. It's not going to be easy for any bank to give up their CEO, but the pressure that would be brought by the government in
that regard is considerable and hasn't really been made
been made much use of.

Instead what has happened is that both the
regulators and the Department of Justice have announced
the settlement with the banking institution and they
have just off to another case because they've gotten
their big headline and they don't feel the need to
pursue it further.

I also worry -- and a number of
commentators have pointed this out -- that the less you
pursue cases against individuals, the less able you are
able to pursue cases against individuals. The
prosecutors who pursue these cases successfully have to
be quite specialized. It can't be your everyday line
assistant U.S. attorney. It's people who over the
years have developed expertise, and if you don't have
that kind of investigation, that expertise is lost.

So I don't think it's so much a lack of
resources. I think it's more of a lack of will,
coupled with a lack of experience in pursuing the cases
against the individuals.

Now, that is to say, because it is
political in part, I think political pressure can and
has had some effect. I applaud the Deputy Attorney
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General Yates for her announcement of individuals, but I think it was also a reaction to public sentiment, and in that sense it was politics in the best sense.

MR. CASS: Let me ask Professor Garrett. One of your colleagues, after serving at the Federal Communications Division said that he thought the form of capture that people talked least about but what was the most pervasive form of capture was captured by the staff, captured by those who worked at an institution long-term.

To what extent do you think this exists in enforcement as well and what do you think the ultimate effect of that is?

PROFESSOR GARRETT: There's a revolving door and people leave after six or seven years of being federal prosecutors. I do think that federal prosecutors are extremely aggressive, that these are often elite units that are bringing major cooperate cases.

There have been a genuine change in focus, and you sort of defer nonprosecution agreements spreads like wildfire, all of a sudden the biggest cases, the cases involving the public companies just sort of the defacto things that we do.
I suspect that many of the U.S. attorneys working on these cases is this our job to be negotiating these sort of deals. We're not civil lawyers. I thought -- we're prosecutors. I think there was really was a change in the law. Many of them may have been resisted it.

I hope that things are turning now in another direction. (inaudible) the New York Times headlines when some of the first banks had to sign deferred prosecution agreements and not nonprosecution agreements filed entirely out of court.

And in the last couple of years we've seen plea agreements with banks and more and more is that we are going to more carefully investigate the individuals and we will be targeting bankers.

So I hope that the job of a federal prosecutor turns to more like what Judge Rakoff described it being in the past. So was it capture or was it just a change in focus, was it an overreaction and Arthur Andersen and sort of a policy approach that we need to go soft. I don't know.

I do want to say one thing which is for all of the things we are doing on particularly federal prosecutors today, when you compare the enforcement
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against corporations on the criminal side in our
country to criminal enforcement against corporations in
just about any other country, there really isn't any
comparison.

When you talk to people in the UK or France
or other countries they say, well, you may complain
that these prosecution agreements in the U.S. are too
compromised, well, at least we're charging
corporations. Many countries criminal liability to
corporations doesn't exist or it's limited to certain
areas, and there are billion dollar cases being
brought. There are cases where employees are being
charged. In many other countries often with major
cooperate crimes happen. Like (inaudible) sanctions
when banks in the UK and other countries are
(inaudible) prosecutions that get brought they get
brought in the U.S.

We shouldn't -- we've become sort of the
vocal corporate (inaudible) in this country and maybe
that's a good thing. Other countries aren't stepping
up to the plate, but (inaudible) however there may be
concerns about capture as to our criminal enforcement.
It's a lot worse in other parts of the world.

UNIDENTIFIED SPEAKER: He just mentioned
the case. This is a case where ultimately prosecution failed, but it did put a company out of the business and there was a lot of debate about the prosecution whether it was well- or ill-conceived. Do you think that has an impact?

MS. MORGENSEN: Definitely. Whenever I ask prosecutors about those people are willing to talk to me are not for prosecution (inaudible) they say that just put the fear of God in people. The idea of being responsible for putting 5,000 people out of work was just -- is just a really damaging hanging over deliver heads.

To Brandon and Judge Rakoff's point about problems with not bringing these cases because we're not using our muscle and we're going to lose the muscle memory as the prosecutors.

I was struck when I would read some of these settlement cases that the Department of Justice was bringing with these major banks on mortgage issues with the statement of facts, and the facts were really nothing more than I had uncovered years earlier in my reporting.

So here I am diving into these things and I'm finally going to get to some info that I wasn't
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able to get when I was working so hard covering this five years ago, and there's nothing new in these statements of fact, nothing regulatory, in addition, of course, not identifying the perpetrators.

So I am seemly unimpressed with what has been turned up as evidence to create and come to the table in these big settlements. It's really as if they were basically reading the newspapers.

JUDGE CASS: They may have been.

UNIDENTIFIED SPEAKER: We have time for one or two questions from the audience before we wrap the panel up.

ATTENDEE: This is a broader question.

MR. CASS: We have a mic.

ATTENDEE: Food safety, but it's a larger question about mens rea the state of mind of corporate officers.

(Inaudible) it has to do with the recent hospital mens rea case, and the case I'm thinking of has been a topic of this conversation because perhaps makes a prosecutor's job easier (inaudible) mens rea rules were better to incorporate more responsible or more at risk of being irresponsibility because with the agency they have to bring their (inaudible) DOJ, and
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the DOJ makes the determination (inaudible).

So perhaps that's a take the (inaudible).

MR. CASS: Let me ask if someone on the panel wants to take this. This is sort of one side of the question that's been raised recently. There have been people arguing that there's a need to increase the ways for requirements rather than decrease, and so we receive both sides.

So who wants to take the first crack.

JUDGE RAKOFF: Yes. I think that with the watered down mens rea, what we're talking about in terms of the criminal law individuals, the sanction we're talking about is prison. I think it is frankly immoral to send anyone to prison unless they have knowingly done something wrong.

Now, there are rare exceptions. We have, for example, in some states negligent homicides, but even there it's usually a form of recklessness that borders on knowingly, and I understand, particularly in the environmental area, there's a push to hold people responsible for environmental degradations that are quite severe and I understand the motivation there, but I think if we're talking about prison, I don't see how one could ever justify prison for someone who didn't
knowingly do something wrong.

MR. CASS: I would say there's some areas where you have responsible (inaudible) and strictly form of liabilities. It's limited to misdemeanors, and in some areas actually you do have to show some enhanced mental state of the executive even for a misdemeanor, like in the Blankenship trial in West Virginia. There's a safety violations (inaudible) require more than negligence on behalf of the executive.

I think it raises different questions, whether it's really a good idea at all to do something that the Senate is looking at mens rea legislation (inaudible) across the board for federal crimes, but I guess the idea being that it's a technical violation, maybe the executives couldn't be expected to know that something was really a crime. It might actually backfire if it's a regulated industry where every executive should know that minors are supposed to have ventilation (inaudible) and supposed to do testing to make sure who doesn't have salmonella.

I'm not sure how effective that (inaudible) goal is as it just insulates executives from liability, but do I think it's an important conversation to have.
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I certainly agree with Judge Rakoff. It's a felony, it must be mens rea and the prosecutors would want to risk bringing a case if they couldn't have shown mens rea.

JUDGE CASS: We have time for one last question.

ATTENDEE: I wanted to ask Gretchen about the whole notion of waivers and whether when they are given by the SEC they are public documents and when they are written about, what is the -- how does the SEC justify them.

MS. MORGENSON: Good questions. The waivers are public, but it's extremely difficult to find them. You have to really look hard. The SEC doesn't make it easy on their website to determine when waivers are given they sort of put them all together so you can't see how often.

This is why this report was cited by my colleague years ago was informative and revealing, that could be changed I think as part of the idea of transparently about deals and what goes on in the making of them.

What was your other question?

ATTENDEE: Just how does the SEC --

MS. MORGENSON: They justify them as
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they're too punitive. If you were not to give JP Morgan the waiver on, for instance, the ability to have quick access to the capital markets to raise money in the bond or stock offerings.

If you were to take that ability away as too punitive (inaudible) our markets. These are typically the excuses that are given. You know, the money management waiver is especially troubling because why would you think that the SEC would want a bank that has made a fraudulent activity to be able to still manage public investor's money, and yet it's deemed as something that would hurt the markets or hurt the bank.

I think part of this whole discussion, we have -- capture involves have the idea that the regulatory regulators job, especially at the Federal Reserve, is safety and soundness of the banking system, and for many years they thought profitability meant safety and soundness, and whether they were making profits, you know, fairly or not, didn't really enter into the discussion. So I think that's he also a big piece of it as well.

MR. CROLEY: We're going to have to let the mics be captured by the next panel, but please join me in thanking this panel.
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UNIDENTIFIED SPEAKER: I think we'll give everybody two-minute break.

(There was a brief recess taken.)

UNIDENTIFIED SPEAKER: I'll ask each of our panelists to offer brief remarks. The topic is to ask some questions and then we'll open the floor. And before I call on him, first I would like to pose a few questions or I'll ask the panelists to return. I'll kind of get the juices following a little bit since this panel is about rule making. There's really two origins of every question.

One is the general form of capture, something I know these panelists thought a lot about but I think also a concept that requires continued precision.

So question number one is: What is capture, and more specifically, how are we distinguishing it from influence or even benign interaction with communications with our government. So the investigation ability of that company is what's captured in rule making, but, as I say, the term warrants some precision in general.

Second question is going to be: What's the counter factor, what's the baseline against which we
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are assessing the presence or absence of capture. To flip that question, to put it a different way, what does a uncaptured regulatory regime look like and what's uncaptured in such regime.

The third thing I think might be fun for some of us to touch on concerns medicine. So there are antidotes or metaphor or capture, what is the side effects? Where are the costs associated with solutions to capture and how can we assess the relative benefits and disadvantages of administering these metaphors.

And finally thinking (inaudible) the same sort of thing, questions our (inaudible) capture is come to some common understanding of what that is as opposed to the preventative way. I don't want to take this metaphor too far already because is it preventative or is it some kind of therapy?

And return to the first question. I'm going to turn it over to Dan. A lot of people institutions a lot of legal rules, one could argue, are designed precisely to address capture. It's just so happens we don't use that term.

So regarding judicial review you might think of sunshine laws or FOIA laws. We have offices and programs in government that are designed, one could
argue, to address capture, although again we don't use that term.

The IGs, the GAOs, and the Department of Justice are institutions that are captured, that are capture-finding institutions. So let me frame our conversation with those four themes, and I'll invite panelists to term them as they see it. (inaudible).

MR. CARPENTER: Thank you very much. It's an honor to be here. I'll answer some of those questions now and some later. Harvard Business School Professor David Moss and I looked at capture in a 2013 book, here it is, Preventing Regulatory Capture, and to paraphrase, we find capture as the result or process by which regulation is consistently directed away from the public interest and towards the interest of the industry. There are other special interests that we also talk about. So it's not always industry-base capture, but that's at the focus here today.

The public interest is also hard to define, but for today's purposes I want to focus on where the public interest is represented in statutes passed by Congress and signed by the President, upheld by the courts, and the statutory regime, that is, and where capture happens where special interest draw policy away
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from statutory intent for industry (inaudible).

Four brief points. By the way, that last point fits rather well with Senator Lee's concern about the way in which Congressional intent (inaudible) regulatory capture.

So capture is the (inaudible) we can argue in this book can be weak or strong. Capture is not, in other words, like pregnancy (inaudible). It's not a binary situation where it just consists or does not.

There are lots of cases of intermediate capture you agree with policies push in (inaudible) in a friendly direction is smaller compared, for instance, to the very plausible cases of capture at the OCC before the financial crisis. The case of medical device regulation at the FDA maybe the case of weak capture, and we can talk that, and for that reason number two the degree to which there is a continuum means that capture is at least in part preventable, which is, we shouldn't congratulate our political institutions entirely if we agree that not all agencies have been fully captured then we ought to be looking at that variation.

If that's true, if we see some evidence of capture in an agency, then full scale dismantling or
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overhaul of the regime or full scale deregulation of
the capture alone is where (inaudible) and those may be
good policy to pursue for other reasons, but pursuing
them for capture alone, I think, misses the fact there
are often (inaudible).

Third, and these are really the two major
points I have to offer today. Capture is really hard
to measure. It's not because it's a sticky thing.
Capture is hard to measure in part -- this is where I
completely agree with Senator Whitehouse -- because we
as a society have failed to produce (inaudible) the red
flags, the warning signs.

We have institutions that are
systematically set up to assess the adherence of
administrative decision for legislative intent, and to
assess the quantifiable costs and benefits of
regulation.

Yet as Senator Whitehouse noted in his
preface today in his introduction, we don't have
anything like that for capture agency. It's far from
clear to me, by the way, to the extent that you appoint
a guardian or camazar to kind of capture analysis, or
set of camazars in that respect, the courts are in a
good position to do this or at least are in a good
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position to do this alone.

I also think that statisticians and economists, or social scientists like myself, if their training is primarily in cost benefit analysis without being attune to legislative intent, meaning politics, for that matter, especially quantitative and statistical test analysis, are also poorly equipped to measure it unless they're trained (inaudible) program evaluation alone.

Now, senator Whitehouse's proposal to have inspectors general to look at the issue is a good start, but I do worry that inspectors general are usually already busy with other things.

Executive order or some degree of Congressional intention for the issue would help. When agencies have their decisions reviewed according to certain criteria, such as rationale feasibility, fairness of administrative procedure or cost benefit calculus, you tend to respond and then to care about those things.

We systematically scrutinize agency decisions. For capture we might get agencies to think about those things generally. Since we're on a panel study rule making I would highly recommend the work of
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the Susan Yaki of the University of Wisconsin Madison who is doing really the best quantitative work on rule making.

Her ideas to use data (inaudible) techniques -- this goes back over ten years -- comments to rules that relate to exchanges between a proposed and final stage. It's not airtight proof. There are a lot of different reasons the correlation between sometimes comments and (inaudible) reasons other than capture shouldn't miss that or see her work as she thinks about this very generally; but she's done it, and it largely has not been done for financial agencies.

Where it has been done, by the way, and in a recent study by CFTC, it was found that (inaudible) future trader commission rules were four to ten times more responsive to regulated financial firms comments than it was to financial professionals and other commentators. Four to ten times.

Is that proof positive alone of capture? We don't know, but if that would persist over a long time you'd certainly want to investigate further. She is a collaborator on a grant funded project that we currently have right now at Harvard at detecting
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industry influencing and financially rule making and we hope to be reporting some results in 12 to 18 months.

Finally at the risk of making myself unwelcome back in Cambridge -- by the way, for Steve Croley's question, what would uncaptured rule making look like? It's hard to get a perfect example of what it would look like, but the absence, or at least the diminution of those kinds of persistent industry-based advantages would probably be one test.

If you're finding consistently greater attention to industry comments across the range of agencies, at least we ought to be asking why and where those are -- where those differentials are smaller.

I'm not saying we ought to be automatically more pleased, but we probably don't need to work as hard for capture.

Finally at the risk of making myself unwelcomed back at Cambridge, let me conclude that agencies reliance on university expertise is without caution of ever less of a fix for capture. In part that's because corporate partnerships, which are fine in and of themselves, make universities ever less independent in judging policy.

The example I think that is probably
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clearest to me is the area of medical technology.

There's a plausible revolving door right now between the industry funded Clinical Research Institute in the FDA. The new commissioner of the FDA comes from that institute. And Duke, by the way, just hired as kind of head of the policy center, the commissioner who set up a major program funded by industry at Duke.

Consider the 21st century Cures Act recently supported by the University of Pennsylvania president Amy Guttmann. She's entitled to her opinion. I knew her as an academic at Princeton, but it was a poorly written piece.

I highly doubt that Amy Guttmann political philosopher or democratic education would have written it, but Amy Guttmann, the president of the university which stands to benefit greatly from a billion dollar increase in NIH funding and which stands to benefit greatly from the more rapid commercialization of ideas developed at Penn, is more likely to have written it.

Of course, if you see the documentary inside job you may think there's a reason to believe that my own university's economics department played an outside role in thinking the appointments and the decision-making that went into the financial crisis.
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One chapter in the (inaudible) I highly recommend it, produces evidence that economists themselves show some systematic evidence of capture. Their conclusions and studies of executive compensation -- their conclusions and studies of executive compensation, for instance, depending upon their funding and their proximity to executive education sources. These are really big statistically significant differences.

I don't want to suggest any one profession or professional school should be singled out. I know many political scientists are, for that matter, including some of my colleagues, conflicts of interests, but these biases should be examined across the board.

To sum up. Capture can be weak or strong. It's preventable and not necessarily a death trap for agencies. We should look at the variation. We need to measure it systematically. That is the one thing I think we need institutional action on, and we need to be carefully about trusting universities as sources of expertise. Sometimes they're as much the problem as the solution. Thanks.

UNIDENTIFIED SPEAKER: I would like to try
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to do two things in my brief time up here. First say
something about the definition of capture, and then go
to some process and other solutions which I would like
to briefly suggest to you.

Capture is easy to diagnose in the case of
MMS where we have lots of industry influence and
objectively a failure to regulate (inaudible) from
blowing up, but there's a more subtle kind, which Dan
spoke about, which is the persistent tilting of policy
away from the public interest. The difficulty, of
course, is defining the public interest, because if
you're talking about whether regulatory policy should
be more stringent or less stringent, that's a
contestable matter, and people obviously have points of
view about that and put in different kinds of evidence.

Nevertheless, I do think capture occurs
when you see a regulatory agency persistently adopting
the policies favored by regulated entities. And I say
that because most of the statutes, particularly in the
health safety and environmental area, are aspirational,
where Congress is asking the agency, in effect, to do
the best it can, the most affordable thing we can, to
protect the environment. And when agencies
persistently fail to do that, I think that raises, at
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least, and inference of Capture.

Now, the possibly exists both in a neutral definition, such as that offered by Professor Carpenter or in the remarks of Senator Lee, that capture can go both ways. But I think the empirical evidence, in fact, leads us mostly to conclude that it goes in the direction of regulated entities. The reason for that is simple. Most forms of capture, subtle and more overt, depend on the resources. As the vice president of the Center for Progressive Reform, I would love to have the resources of a capturing agency. We can't seem to raise that kind of money. I'm sure that's true of all my colleagues in the room in the public interest community.

Well, what to do? First, I would study the impact of decreases in funding. Funding of regulatory agencies is as well as (inaudible) in decades. The high point was in the 1970s. That is, have lots of (inaudible) effects of deteriorating regulatory policy, and I think, and I can talk more about this in remarks, has made agencies much more subjective, much more capable of being captured by regulated entities.

In that regard (inaudible) and I propose that we three agencies (inaudible). I think we ought
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to ask agencies what amount of resources do they reasonably need to carry out their (inaudible) more effectively. And by the way, I would put decrease funding in the definition of "capture." The amount of money we save by underfunding regulatory agencies is minute in a federal budget and wouldn't make one bit of difference to the federal deficit. We could double or triple funding of every agency tomorrow, and no one would notice the difference in the overall federal budget.

On the grounds of transparency suggested by Senator Whitehouse, I would start by better calendaring. Agency officials, higher officials keep up with calendars, and you can't learn much from them, and it's somewhat inconsistent. I think there should be more detail about what happens into those meetings, maybe a brief summary, so you can trace meetings, who's meeting and what is occurring in those meetings.

I would require regulatory agencies to do summary statistics of who comes to meetings, and how often they meet so at the end of the year, you could go to one source of data, find out how many meetings they hold, and who they held them with. The agencies themselves would do the statistics. I would do the
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same for rule-making comments. I realize there are thousands of them, but they can be coded when they come in, because they're not all electronic, and sorted; and you can find out that industry-related entities have many comments, and public interest groups have far fewer.

To the extent those studies have been done, they're very difficult to do and very time consuming. Industry meetings and comments exceed those filed by public interest groups five or ten to one, almost without exception. They're (inaudible) rule-makings in which there are no public interest comments.

Finally -- and I'll end with this -- Rina (phonetic) and I have suggested what we call regulatory metrics, going on Professor Carpenter's suggestion. We would do a sort of a meta statistics. So, for example, and to oversimplify, we would have the EPA report on how clean the water is. And if we're stuck with 62 percent clean water for a decade as -- and I think we are, by the way, then I think we could start to ask questions, why are we stuck there? It may not be captured. It may be lack of funding. It could be lots of things. But we ought to be able in a more straightforward and visible fashion to chart the
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progress of agencies towards the statutory (inaudible), which are to protect the public and the environment.

MS. RAO: Thanks to the administrative conference for inviting me to speak on these important issues. I was asked to say a little bit about the role of Congress in regulatory fashion, which I'll do in my brief time up here.

So I guess I wanted to start by saying I think one part, at least one part, of the traditional story of capture is correct, which is that it's much easier to regulate than to legislate. As you can see, the dynamic begins in Congress, which often delegates significant amounts of authority to administrative agencies, and that authority is often given to various open-ended (inaudible) terms. And in these agencies, there are often a very significant zone of discretion, and the accumulation of these delegations, I think particularly over time, has shifted most major policy-making decisions to agencies, and away from the legislative process. And in the regulatory process, there is much less visibility, and there's much less accountability.

I know that lawmakers delegate for a variety of reasons. Sometimes they can't reach a
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compromise. They may simply want to rely on the expertise of agencies, or they may just want to push off certain hard questions. But I think another important reason that we see so many delegations of authorities is that members are often able to get more work done working with agencies than by passing legislation. And I think this tendency has only become more pronounced in an area of party polarization and gridlock in Congress.

So how do we accomplish our objectives. I think there are both formal and informal mechanisms for that. The informal mechanisms are all the things that we see publicly, like there are things like oversight hearings. There are, you know, open letters to agencies asking for information. There is the appropriations process. You know, all of these things are legitimate ways in which Congress interacts with the administrative state.

But first, there are lots of informal mechanisms, and that includes all of the various informal types of contacts between members of Congress and their staff and agency staff.

Now, (inaudible), this type of influence is very difficult to measure. I think that Professor
Shapiro's idea that we should be documenting the (inaudible) agency should probably also apply to people on the Hill. And, you know, I think we might get a better sense, then, of what the magnitude of this influence is. But I think anyone -- and I've worked both in the executive branch and in Congress, and I think this is -- most people understand that this is the an ordinary way that things get done.

And so I think it's -- the shift is -- the (inaudible) focus on this administration made them surprising, because it really is where -- where policy-making is done. In some ways it's problematic because members of Congress don't have any executive power, and they don't have any administrative power. They're exclusively given legislative power. And I think that Steve raises a great point that, you know, what -- what is the (inaudible) for entity. And I think it's partly because the baseline is so difficult to know, right, what is the public interest, that the process becomes so much more important, right. Our constitution creates a process. (Inaudible) defining what the public interest is, and that is our law-making process. Now, whatever happens with the (inaudible) administrative agencies.
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Now, Congress, of course, has the power to oversee agencies and to ensure that they are compliant with the mandates of the law, which presumably reflects the public industry. But it's often the case that statutes are so open-ended that it's very hard to figure out whether the agency is meeting the requirements of the law. It's no easy task to do that. And so fatefulness to law, in many instances, may well become fatefulness to the interest of a particular member of Congress.

I think it's this -- I think really the problem is that there's so much discretion in agencies. And so that allows the private interest groups and members of Congress to try to influence that discretion.

You can call that "capture." I'm not sure that the label necessarily matters, but the problem is that there's an influence that may be pressing against the public interest as defined by our public laws.

And I want to also say that I think this dynamic, the dynamic that law makers focus on administration rather than law-making has really undermined Congress as an institution. I mean, the Constitution already has stacked the deck against the
(inaudible). It's really hard to do. You have to go through (inaudible) feature, not a bug of our constitutional system. But if (inaudible) members can accomplish a lot of their goals by working through the administrative state this (inaudible) Congress as an institution because it reduces the incentive to actually pass laws.

So what we see happening in these instances is that lawmakers are (inaudible) the most significant power, really the first power of our federal government, the legislative power, that they exercise together, for little bits of the administration that they can exercise separately.

And I think ultimately this (inaudible) in Congress, and we have also seen that it allows the executive branch to accumulate ever more power, which further upsets the separation of powers. And, of course, those separation of powers were designed to secure liberty and accountability.

And that's what under my file. Thanks.

MR. CALABRIA: Well, first of all, let me say I'm honored to be invited by such a great panel, and it's nice to come back to work here (inaudible) to the banking committee which is not (inaudible).
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The one thing I learned early enough is

(inaudible) let me say as an economist it's nice to say it's nice to be invited with lawyers. My dissertation work, about 20 years ago, was on the topic of (inaudible) and it's something I've given a lot of thought to. That you have academics in the room. I (inaudible) let me also say.

(CAN'T HEAR A WORD HE'S SAYING)

The video is online if you'd like to learn more about it, then you should by the book and read it.

All that said, let me -- first make a point in my mind that there is, in my view, a number of regulatory systems that are, if not a hundred percent, maybe 90, 95 percent pure (inaudible) is not to pick on anyone at the federal level (inaudible) I think about licensing of lawyers and hair dressers. It's pure capture.

You know, I think the public benefits from those sorts of things are pretty close to nil. And so those are the easy cases, and the answer is don't do it.

But let's turn to the hard cases. I just wanted to make that point, because there are some pretty easy cases, and we should basically consider
that all regulations have the distribution of cost and benefits, and that capture increases the cost and potentially reduces the benefits. But that means, in some instances, that otherwise capture on the expense of trying to reduce capture and make some regulations; otherwise, the benefits concede cost to not be the case.

And unfortunately of those cases, the (inaudible) gets to spend the rest of my time on the more difficult case of very clear public benefits. Some potential for capture. And, of course, we don't all just want to have the benefits exceed cost relative to cost. So let me talk about a couple of ways that I think we can try to structurally reduce some of the cost of capture in a way that hopefully reduces gravely the benefits.

So let me first say that maybe because I'm an economist, I like simplicity. So me, in my experience -- and I also spent a little bit of time running a regulatory bureau. Complexity is a friend of the industry. The (inaudible) regulation is the easier it is for industry to influence the outcome. I'll mention some experience. In my role at the finance, over time, as big capital regulation has become more
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(inaudible) the industry itself. It's one reason, for instance, that the (inaudible) I favor things like (inaudible). It's not because they don't have costs. They're easier to monitor. They're easy for the public to figure out what's going on, and it's a lot harder to gain. So, again, simplicity really is a very big issue.

Let me also say that I spent a number of years on the banking committee working on regulatory structures, and one of the painful things that should have been obvious is, don't have an agency highly dependent on a small number of entities. So the office of (inaudible) about 25 percent of its budget is derived from WaMu.

If you think that's bad, (inaudible) regulator only recipe for capture. So one of the suggestions is certainly we try to do this. And in 2008, where we created a new regulator (inaudible). And, again, I would say that is a regulatory agency. The number of timeframe agency that is now 60. That is still pretty damn small for a regulator and easier to capture in that way. So I do emphasize, the broader the base of funding, the broader the base of repping attendees, it's much less likely that anyone is likely
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to capture an institution.

I do want to say without going into too much detail, I think it's important to keep in mind that we often talk about the industry. There is no "the industry". There's members of the industry?

My experience is both a Hill staffer regulators, that's the majority of time. It's one (inaudible) It's one sector of the industry segment to another sector of the industry, and it's important to keep in mind that having this balance between different sectors of the industry is actually a to kind of reduce capture.

When one part of the industry is small things (inaudible) that's a balance of the process that I think is very helpful. Here's what I'm suggesting where I can get myself into trouble.

The regulatory and legislative process should become less dependent on lawyers. Let me kind of tell you why. I have repeatedly seen in my experience when the regulatory process has been tilted in favor of industry quite frankly because the lawyers didn't understand the economics.

I'll be the first to say that economists don't understand law. I'm not demanding that we have
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economists run the process, because but I think that
would turn out really badly. What I am demanding and
suggesting is that we have more multidisciplinary
approach where economists at the table and economics
(inaudible) only lawyers were involved, but oddly
enough, a financial regulation really is predominantly
lawyers.

You know my opinion the failure, for
instance, of cost benefit analysis many of the time has
been the economists have not been involved. Why do I
say this is important? Partly, my background as an
economist is (inaudible) market structure down.

I think about (inaudible) do they
regulatory interventions impact concentration, impact
competition, and, again, I think you have to look a how
that affects it because often I have seen industry come
in and suggest something that sounds quite reasonable,
(inaudible) but it tilts the playing field?

So I really do think that you have to have
an economist at the process. I will say there's a
wonderful book out about 20 years ago called The
President and the Counsel of Economic Advisors. It's a
series (inaudible) of interviews of economic advisors.
You really couldn't tell the partisanship if you didn't
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know it because the constant (inaudible) the chairs of the economic (inaudible) complain about all the agencies essentially (inaudible) by their clients.

In fact, the CEA constantly pushing back against agent decisions that they thought benefited one industry over another, and I would say I think in the regulator process in the Executive Branch (inaudible) would be the Counsel of Economic Advisors having to do a greater role is important.

OMB tries to play this role, and I think they've largely been okay at it, but, again, (inaudible) and the theme I would say is more checks and balances to try to bring some light.

I think it's also important that one of the chapters talks about cognitive capture, and I think this is a really important unit to keep in mind. We all walk around in the baggage of biases (inaudible) situation and none of us is purely objective. The way that we all try to be purely objective is we sit around the room and deliberate and we try to question each other's priors. We don't see enough of that in my opinion in the regulatory process where there's a challenge. And I do think that having more of that -- again, to me the best way to do that is to make sure
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you have a process and make sure your viewpoints are
heard and make sure it's challenge to that.

Let me just say, I do have some faith in

the process and example would be really makes a lot of
sense is you go back and you look at the dates and the
range of the Administrative Procedures Act and it was
claimed when this act was put in place (inaudible) I
think it's fair to say government is a lot bigger today
than it was in 1946 even accounting for World War II.

The Administration Procedures Act was a
reaction to process of thirties and forties where there
were often cartel creations by the regulators, where
the big-industry players came in behind the scenes.

And so that notice-and-comment process, to
me, has been almost a complete value in terms of
bringing some light in the process. Has it been
enough? No. But I do think that having this process
and bringing more scrutiny is very important.

So, again, I'm saying, part of my concern
is I often here the claim of evenly (inaudible) always
ends up benefiting the industry. I'd rather take twice
as long to do something right than half the time to do
it wrong. Again I worry that the speed of conversation
(inaudible). Then we have a few things that we can
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talk about.

MR. CROLEY: Keith, thanks. Please join me in thanking our panelists for their remarks. There are several topics that we're going to have to (inaudible). Let's postpone that for some Q and A, but let me introduce our next speaker Senator Elizabeth Warren.

UNIDENTIFIED SPEAKER: It's a great pleasure to introduce for Senator Warren, but actually Professor Warren, and I think we should also, the many academics in the room, respect the fact a few academics got to create their own federal agency with what could be called the problem of capture, which I think you would say, and we haven't talked yet about structure of the agencies, but to CFPB similar financial section of the bureau is indeed structured so as to solve a problem maybe other agencies (inaudible).

It's a great pleasure to have you here, Senator.

SENATOR WARREN: Thank you. Nice to see you-all. So thank you for having me here. I appreciate the introduction. I appreciate the invitation to be here today. I actually wish I could have been with you throughout this conference. I got to catch the tail end of your remarks.
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We had two other hearings going on this morning, so I couldn't do it, but I wish I could have been with you because I (inaudible) the regulatory capture is a very big deal. It is one more way in which powerful corporations (inaudible) the system to work for themselves, and the rest of America pays the price.

One aspect of this problem is that law enforcement treats powerful corporations with kid gloves. I recently put out a report called "Rigged Justice," that list 20 examples from just 2015 alone of weekly enforcement against big corporations and their senior executives. We essentially have a two-tier legal system now. One for giant corporations and one for everyone else, and the message is clear: For the wealthy and the powerful, following the law is merely optional.

In a country that has etched equal justice under law above the doors to the United States Supreme Court, this is an ugly truth. But today I want to focus on another aspect of regulatory capture. The capture of agencies as they like the rules, because here, too, the game in Washington tilts sharply in favor of big companies.
So let's start with the obvious. It is really, really hard to pass a law through Congress that benefits working families. We have plenty of lobbyists in Washington, but they don't want laboring on behalf of working families. The tilt in Congress is pretty much out there for everyone to see. Lots of concern about preserving (inaudible) tax breaks for big companies, but not much help for seniors who are trying to scrape by on social security. Lots of concern for (inaudible) who want looser regulations and oversight, but not much help for people paying a high interest rate on student loans. It is disgraceful, but at least it's visible. Corporate influence works even better in the shadows, and that's where the rule-making occurs. That corporate influence rule-making process becomes a place where strong, clear laws goes to die.

Considering the plight of financial reform, following the worst financial crisis in three generations, one that resulted in taxpayers spending hundreds of billions of dollars to bail out banks. Congress passed the Dodd-Frank Act to make sure that this type of crisis never happened again.

Main Street went toe to toe with Wall Street, and we lost some battles, but we also won some
major victories. But passing the law wasn't the end; it was just the beginning.

To implement the law, Dodd-Frank required several regulators to write literally hundreds of different rules. The big banks and their friends knew that each one of those rules presented a golden opportunity undermine, pervert, or simply undue the work of Congress. One lobbyist referred to the day that Dodd Frank was passed as halftime, and the big banks have been lobbying agencies aggressively ever since.

Wall Street understands what the public too often forgets. The public battle is in Congress, but even if the industry loses, there are more chances to weaken or overturn the law in the agencies and in the courts. Giant corporations and their lobbyists devote their influence agency rule-making, and I have to say it pays off handsomely.

My message for today is pretty simple. When it comes to undue industry influence, our rule-making process is broken from start to finish. At every stage, from months before a rule is proposed to the final decision of a court hearing to challenge that rule, the existing process is loaded with opportunities
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for powerful industry groups to tilt the scales in their favor. The tilt starts early.

For example, a 2011 study of EPA records from 1994 to 2009 found that industry groups held a virtual monopoly of informal communications with the EPA that occurred before proposed rules on hazardous air pollutants were made publicly available. On average, industry groups engage in 170 times more informal communications with the EPA than public interest groups. Communications that occurred before any proposed rules were ever written. Similarly, Dodd-Frank has a provision called the Vulker Rule, and the idea was to stop banks from engaging in certain kinds of risky behavior.

Before that rule could be written, groups engaged, who had Wall Street interests, met with federal regulators 419 times, accounting for over 93 percent of meetings between the federal regulators and external parties about the Volcker Rule. Think about that.

Less than 7 percent of the meetings were with individuals and groups representing the public interest.

As rules wind their way through process,
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prolonging just intensifies. (Inaudible) formal

opportunity to weigh in, their views are quickly buried
in an avalanche of detailed, well-funded,
well-credentialed comment where industry insiders and
their highly paid allies.

You know, those EPA rules that I just
mentioned on dangerous air pollutants, industry groups
submitted 81 percent of the comments during the notice
and comments, period. Public interest groups submitted
less than 4 percent of the comments. Some observers
argue that this resource mismatch has a smaller impact
with agencies than it does with Congress.

Unlike Congressional action, agency rules
are constrained by well-established judicial review
standards that seek to determine whether the agency's
action is supported by the evidentiary record and the
authority delegated to it by Congress. The rules must
be supported by "substantial evidence," and agency
actions must not be arbitrary and capricious.

But corporate players are savvy. They get
it. They have learned that those same judicial review
standards can be used to suffocate new rules.
Companies don't simply photocopy the same comments and
jam up an agency's inbox with identical assertions.
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They play a much more sophisticated game levering their own expertise and paying outside experts with purportedly independent credentials to produce long and detailed comments filled with data and analyses, all selectively produced to serve their own interest.

This push buried the agency in detailed self-serving comments, slows the process massively. And their overall dominance of the notes-and-comment process results in rules that are longer, more complicated, and more the liking of major players in the industry.

Over the last few decades, additional barriers to rule-making have popped up. Requirements include cost-benefit analysis and evaluating the impact of the rule on small businesses and the environment.

Sometimes these processes result in better rules, but often they are just more obstacles that result in even longer, more complex rules, and even more opportunities for (inaudible) industry players to slow things down and build exceptions for themselves.

Consider the Office of Information and Regulatory Affairs, or as we all know it around here, OIRA. This is the tiny, obscure, and incredibly powerful agency that reviews significant regulatory
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proposals developed in other parts of government before they can become law.

A study of interest groups meeting with OIRA showed that between October 1st, 2001, to June 1st, 2011, OIRA met with five times as many representatives of industry as with people representing public interest groups.

And just last year, two professors at the University of Wisconsin, Madison, released a report showing a strong correlation between interest groups lobbying OIRA and changes in OIRA rules that then helped those industry groups.

These procedures tie agencies in bureaucratic knots and bleed much-needed resources. Often, agencies have to give up entirely on writing new rules. It's possible to see this happening in instances where Congress or the Court has directed an agency to issue a specific rule by a specific time.

A recent study with such deadlines, between 1996 and 2014, show that over 50 percent of final rules were not finished on or before their mandated deadlines. That's right. More than half the time, federal agencies did not meet their legally mandated deadlines.
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So there's an example. Dodd-Frank was passed almost six years ago, but as of today, agencies still haven't finalized nearly one-quarter of the required rules. By the way, these delays can actually put lives at risk.

Five years ago, Congress passed the FDA Food Safety Modernization Act to revamp food safety laws. Anyone in here who eats food should care about this law.

Now, those regulations were due in 2012, many weren't published until 2015, and then only after a court ordered the FDA to publish the regulations.

Meanwhile, every year, 3,000 Americans were dying from a food-borne illnesses, and 48 million Americans, that's one in six, was getting sick from contaminated food.

In 2008, a dam at the Tennessee Valley Authority Power Plant broke, dumping 1.1 billion gallons of coal ash sludge into a nearby community, damaging over 100 homes and contaminating a river and several streams. Within a year, the EPA sent OIRA a proposed rule regulating disposal of hazardous coal ash waste, but a vigorous lobbying campaign by the coal industry froze the proposal, and it took five more
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years for a rule to emerge from OIRA. Even if an agency manages to jump through all of the hoops and withstands all of the pressure and actually issues a final rule, companies sue.

In theory, the threat of a lawsuit of a corporate lawsuit over a rule that's too strong should be counterbalanced by the threat of a public interest lawsuit over a rule that's too weak or a rule that never gets issued at all. But, here again, the rules governing judicial review favor those who would stop the agency from acting in the public interest.

Under the law, it is easier for business groups to challenge a rule for being too strong or for being too restrictive or riddled with loopholes. And it's nearly impossible to successfully challenge an agency for not acting at all.

And, boy, does this take a toll over time. I talk with agency heads who are like beaten dogs. They just want to keep their heads down. This is even more true for agency attorneys general. It is hard to go up against a well-financed machine who will use every tool at its disposal to destroy years of work.

And it is a lot easier just to give in and write a softer rule or to write no rule at all.
Over time, the lobbyists' work gets done by the agency's own lawyers who are so risk averse, that they kill off agency action before it ever gets off the ground.

Now, to be clear, engaging in informal dialogue, participating in notice-and-comment, and going to court when agencies stop out of line are not bad things. But over time, bludgeoning agencies into submission undercuts the public interest. The goal should be to have a system where influence over new rules is measured not by the size of the bankroll, but by the strength of the argument.

And here are a few principals that would help balance the scales. First, increase transparency. The more sunlight that shines on the agency's process and on industry efforts to influence them, the more likely it is that an agency's final product will reflect the public interest.

A good start will be to disclose all of the meetings between agencies and interested parties, but before and during the rule-making process. Another would be to help agency support distinguish between legitimate high-quality data and research, on one hand, and bought-and-paid-for studies, on the other, that
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would require disclosure of financial arrangements and editorial relationships associated with regulatory comments. And anyone who wants to cite their own data should have to publish the data set online. Sure, (inaudible) amenity, for example, but get the data out there where other people can test drive it.

Second, level the playing field between public and private interests. The net fact of the notice-and-comment process that’s dominated by business advocates is that severely under-resource public interest advocates are just simply outdone. States who experiment with systems to build a public advocate (inaudible) regulatory process or compensate public interest advocates who invest resources to produce meaningful feedback on the rules. In summary, judicial review of agencies needs to be reformed to give the public a fighting chance, to challenge these rules, (inaudible) and agency capture.

And third, boy, do I agree with you on this one: Simplify. Complex rules take longer to finalize and are harder for the public to understand, and inevitably contain more special interest (inaudible) that favor business interest of small business and individuals.
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Complex rules are also more aligned on industry that provide additional detail and expertise. And that means more opportunities for capture. Simple works better.

And forth, limit the opportunities for cultural capture. Regulators should be beholden to the American people, not to corporate benefactors. Two ideas: Crack down on the revolving door, and (inaudible) parachutes for executives who enter government.

In 2013, the project of (inaudible) released a report showing that major corporations routinely offered their executives financial incentives to the tunes of hundreds of thousands, even at millions of dollars, for accepting (inaudible) positions. The Financial Services Conflict of Interest Act, a bill introduced by Senator Baldwin and by Congressman Cummings, would make these payments illegal by removing government employees from decisions, and they would help target conflicts of interest by removing government employees from decisions that financially benefit their former employers. Now, that is at least a good start in this area.

And finally, give the agencies the money
they need to do their jobs. Writing rules, responding
to thousands of comments, separating valuable data from
self-serving nonsense takes capable people who have
adequate resources. Starving the regulators is the
quickest way possible to ensure that this work is
essentially outsourced to the regulated industries
themselves. Those are some ideas for how it is that we
could begin to shift the system.

But I want to make one more point about
regulatory reform before we leave. I think the idea of
regulatory reform has become politically very popular,
but too many of the proposals that go under the title
of "Regulatory Reform" are actually supported by the
industry, precisely because those proposals would
create even more opportunities for them to block
regulations they don't like. Regulatory reform is
badly needed, but the reforms must address the central
problem, a tilted playing field that benefits the rich
and the powerful. This won't be easy. These folks
won't willingly give up power and influence, but this
is about building our government that works not just
for those at the top, but that works for all of us.
And that's why I'm glad you are here today.

I appreciate your holding this conference.
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We have to make some changes. Thank you. Thank you very much.

MR. CROLEY: Well, those remarks make a perfect segue to go open the floor for a couple of questions. I'm sensitive to folks' time, and I ran over both. We can take a couple of questions.

UNIDENTIFIED SPEAKER: The administrative conference originated and has long-championed techniques for rule making, such as negotiating rule making. Some agencies, particularly the EPA, as an example, (inaudible) a variety of collaborative techniques. My question is: Do you see this kind of activity more as opening a new forum for regulatory capture, or is it more in the other direction, that it contends we're producing an openness and a balance?

MR. CALABRIA: Having been involved from the regulatory side, at least one issue in rule making, (inaudible) safe from the regulator side, was a painful process. I could see why agencies don't actually want to do it.

In the one instance that (inaudible) involved, Congress was very specific about the range of interest that would be represented. So it was very clear that X number seats would go to consumer interest
and X number of seats would go to industry interest. And I found the process to be generally pretty helpful, because there was a very wide range of interest at the table. And so I do think it would be helpful, but I have to say (inaudible) negotiating rule making nominated.

And, again, I want to emphasize, Congress has the ability to require (inaudible) in rule making every single member of the negotiating committee if they wanted. So, again, it starts at where Congress puts the (inaudible) oversight in. So it could be bad or it could be good. It really depends on how it's done at the beginning.

UNIDENTIFIED SPEAKER: I would like to address -- my fellow economists have said that -- my fellow economists said that the lawyers are now in the process. I think that's something we have to live with, the regulatory structures around laws and regs, and that's what lawyers write.

I think the thing that the economists have to learn is they've got to learn the law. And most economists come to Washington, and they spend all of their time reading a newspaper and the American Economic Review, and I think they ought to start...
MR. CALABRIA: I couldn't agree more, as an economist who likes to read statutes and regulations. My point was really to have that, you know, at the table. And I remember (inaudible) I was involved in where certainly on a number of occasions, economists suggested things that simply weren't within the law. And you didn't work there to correct them on it, but, again, I wouldn't suggest that we would ever let economists rule the world or rule the regulatory process. I just think that if we're at the table with the lawyers on the front end, I think it would be the most favorable decision.

I'll also emphasize as well -- again, sounds partly self-serving -- the fact that I was doing (inaudible) on the entire staff of the committee during my time there, and this is a (inaudible) committee that oversees the Federal Reserve, that oversees the bank regulators. I think congressmen do a lot better job. We might need an equivalent of the joint economic committee (inaudible), but they're looking at the economy. I think adding the process in where committees are much more engaged in having that side of
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(inaudible). Again, I'm not trying to insult the lawyers in the room. They bring in expertise at the table, but I think that's your only role (inaudible) and are making bad decisions.

UNIDENTIFIED SPEAKER: That was my -- the point I want to make is that if economists want to get in the game, then they got to pay the price. And the price is learning administrative law, and if they don't do it, they're not going to get in the game. And the fact is -- the other point I want to make is, if you see the difference between two disciplines of the day on what is captured, it's a mess.

What do the lawyers say? The lawyers say it's how many comments you write, how many meetings (inaudible). Well, what does an economist say? The economists say, we have to look at (inaudible). And that's a completely -- two different approaches to a big conference, and that's why I think the only way the economists are going to get in the game, they have got to pay the price. (Inaudible).

MR. SHAPIRO: Just really quick, and this is an important point. I'm actually sympathetic to Mark's point of how the influence of lawyers -- I would just say, you know, there's more than two species on
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the planet. There's more than lawyers and economists. There's a variety of other social scientists that I think should also be in the game.

Actually, since the Obama administration's credit -- not just the Obama administration -- a lot of policy has become more (inaudible) were better informed in recent years, and I think that's a huge improvement.

They can also, I think, do a much better job incorporating people studying political institution, social networks, and things like that. I think it also raises the worry -- and I'll just point you to (inaudible) Gonzales, an economist at University of Chicago, a Chicago-school economist, who writes in our book about how -- the fact that there's pretty good evidence (inaudible) that congressmen themselves maybe captured.

It's not to say that lawyers aren't also subject to capture, but I think, you know, bringing in these different views is a good idea, but making very sure that at least we are aware of different biases and different sponsorships or subsidies that they receive from regulated interests or from nonregulated special interests.

If I might, I'd like to say a word about
expertise as well, because I actually think it's yet another protection against capture. But one of the consequences of the defunding of agencies is we gradually thinned out the expertise, mainly because people with experience in the agencies are retiring and we're not replacing them at all or replacing them with people with much less experience. And the reason I said that, I just wrote an article, published an article about expertise, and I define "expertise" both as professional training and experience.

And the best agency practices, you have a (inaudible) of people from different disciplines who engage in the very robust process within the agency. And picking up on Jim's point, after a while, the more experienced economists do learn the law, or science, and they're able to comment on it. And the lawyers in the agency then become more familiar with the economics and the science of the agency, and they can comment on it. So it's just not that you're looking to one profession to bring that kind of input into the experience; you have the opportunity to create an atmosphere, an environment, where all of your professionals learn enough about each other's class that they can debate what their hearing from the
outside, and throwing their own independent judgment to it. And that really is, and/or could be, an effective deterrent of capturing, I think.

MR. CARPENTER: And just a quick other point, Sid's point about agency defunding, and this was made by other people as well. I think the experience of term limits (inaudible) in legislative is an instructive one here. If you go into any legislative capital and ask people what happened after the -- on the states that passed term limits and their quantitative studies to back up this point, the effect was not to return representations of the people. The effect was to increase the power of state bureaucrats in those capitals, because even the new, fresh, unexperienced legislators turn to for advice the government agencies or, in some cases, interest groups. The quantitative study that backs this up is a really great study of where is power to the American legislative (inaudible).

It turns out there are legislative professionals, and which is to say the amount of resources given to committees is lower. Right. Reliance on (inaudible) model legislation is higher, which you might agree with his claims, but keep in mind
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that that's an (inaudible) is our federal system
designed by the founders of (inaudible) of a democracy.
To the extent that these states are all adopting the
same kinds of legislation, written by the same single
interest group, it's undermining federalist diversity.

And, again, I think that points to not
just, you know, a case against agency defunding, but a
case (inaudible) legislative investments.

UNIDENTIFIED SPEAKER: We'll take two more
questions, and I'm sure the panel will be happy to hang
about if people have follow-ups.

ATTENDEE: Hi. I'm Kevin (inaudible). The
conversation about regulatory capture and expertise is
fascinating, because I think there is a relationship.
Those in the industries that are regulated, those were
(inaudible) regulations tend to be the most expert in
the subject matter, so there's a natural tendency
towards imbalance. We have a congressional budget
office. We have a government accountability office.
Shouldn't we have a congressional regulatory office,
someplace that supplies expertise, from the right
source? Not just attorneys, not just economists;
subject matter experts who could help Congress oversee
our regulatory system, a double-check cost benefit
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analysis (inaudible).

MR. CALABRIA: It's certainly worth recognizing the GNA, and CRS will do some of that as well. I don't want some self-serving economist to say I've worked on this, because that's not always the answer; but I do think that there could be more -- I've certainly done this as a staffer. There are lots of resources people who we weren't aware of, but you can always use more as a staffer.

Congress used to have the Office of Technology Assessment; and despite the name, "Technology" has actually performed that broader regulatory role for Congress.

MS. RAO: I would just say I think it's helpful so long as it's being used for legislative purposes and not to try to interfere with the executive power, because once those agencies are operating, they're part of the executive branch, not Congress.

UNIDENTIFIED SPEAKER: I thank you-all for being here. I was wondering what you thought of the strategy of insulating regulators from the industries that they regulate, mainly through ethics safeguards and, of course, by the Office of Independence.

MR. CALABRIA: So let me give you a kind of
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mixed view. I'm very sympathetic to having restraints on revolving doors. I certainly am very sympathetic, and to me it says a lot that large training institutions will give you a very large bonus if you leave a financial institution to work for government. Even if there's not corruption, that certainly is the appearance of it, if nothing else, but I think there is contention.

I don't think you want people at agencies who have never worked in the industry, because, you know, the real problem here is (inaudible) the really important thing to keep in mind is, there's no requirements for anything to ever be (inaudible) is the regulation. Congress can make those decisions. They can make some of them.

So I would argue, and I can say I've had lots of arguments with people as a staffer when I suggested that maybe we, as congressmen, should be a legislator, rather than tell you.

And I think there are way too many instances where Congress just kicks the can down the road. It's ridiculous (Inaudible) rule making under Dodd-Frank. (Inaudible) I can write on two pages. That said, you know, it's a real tension,
because when you have this complexity, the people who
know are in the industry, and so you have to have this
bylaw. And, again, I think the more the dialogue is in
the sunlight, all the better; but I certainly think
reasonable restrictions on when you go to work for the
industry.

There certainly should be restrictions on, you know, if you're a bank examiner, it's one thing to
say, you've got two years where you can't work for a
bank. It should probably be a little longer for you to
actually work for the bank you might have examined. So
there should be some distinguishing characteristics
there, but I certainly think that that's something we
should work at. But I do agree that we build morale.

The objective shouldn't be, how do we make
sure that an agency never hears from anyone in the
industry. And the objective should be more sources of
information.

MR. CROLEY: Okay. We're 20 minutes over
our time. Please help me to thank our guests.

(Forum concluded at 12:20 p.m.)
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I, Steven Poulakos, registered Professional Reporter, the officer before whom the foregoing proceedings were taken, do hereby certify that said proceedings were taken by me stenographically and thereafter reduced to typewriting under my supervision; and that I am neither counsel for, related to, nor employed by any of the parties to this case and have no interest, financial or otherwise, in its outcome.

IN WITNESS WHEREOF, I have hereunto set my hand this 3rd day of March, 2016.

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Steven Poulakos, RPR

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