**Buyer Beware: With Mandated Disclosure, You Get What You Pay For**

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One of the most pervasive beliefs about the regulatory state is that information disclosure is cheap and efficient. With little cost, Energy Star ratings encourage firms to compete on energy efficiency, restaurant grades cause restaurateurs to improve food handling practices and calorie counts reduce overeating. With such simple market-mimicking cues, we get something for nearly nothing and avoid contentious issues associated with conventional regulation.

Yet this view is misconceived. Designing a good disclosure regime can be far from cheap.

There are of course the obvious costs for regulated parties. Each year, for instance, physician practices spend on average 785 hours per physician and more than $15.4 billion on reporting quality measures. Publicly traded firms can incur average costs of $2.2 million to comply with Sarbanes Oxley's disclosure requirement for internal controls on financial reporting.

But far less appreciated is the fact that many disclosure regimes can have prohibitive costs on the regulators themselves. Implementing disclosure can shift agency resources in unanticipated and often pernicious ways, distorting the regulatory agenda. Consider what was once deemed a poster child for information disclosure, restaurant grading. In New York, due to a little known political compromise, grading shifted inspectors' time away from the worst offenders to resolving grade disputes. Administrative appeals of grades spiked, flooding the dockets of administrative judges.

Part of the problem was that disclosure of restaurant grades was mismatched with the design of the restaurant inspection system. The inspection system is geared principally to identify major public health hazards and to ensure that minimum standards are met. It was not designed with the goal of drawing fine distinctions among restaurants deemed safe enough to operate. Caseloads are high and substantial discretion exists in applying the health code, leading to dramatic differences in stringency across inspectors. In New York, the result was that grades had little predictive power over how a restaurant would fare when a different inspector would visit. Other jurisdictions resolve this regulatory mismatch by simply engaging in grade inflation. In St. Louis, 96% of restaurants receive A grades, even with as many as four critical violations.

Over the past three years, I've worked with Public Health - Seattle & King County to design and implement a grading system to address such challenges. To do so required extensive statistical analysis of inspection records to develop a more reliable grading methodology and a peer review system to improve the process. And for the better part of a year, these decisions consumed senior staff. While a more reliable grading system can be designed, naïve calls for grading are oblivious to these first-order issues of the quality and consistency of inspections.

Disclosure policies are often passed without providing additional resources for implementation. But demanding more without funding more comes with tradeoffs, often undercutting the agency's core mission. Take calorie disclosure. It may seem cheap on its face, but concrete regulatory implementation can soak up valuable agency resources. How, for instance, should an agency verify caloric claims? Serious testing would require a new administrative scheme: one study found that while claims were generally accurate, nearly 20 percent of food labels understated caloric content by at least 100 kcal per portion. Private enforcement might offload detection costs to the public, but would require an administrative tribunal to adjudicate. In King County, which adopted calorie disclosure in 2007, implementation questions alone commanded the attention of senior food safety staff for the better part of a year. And the hidden cost was the abandonment of efforts to "standardize" food safety inspectors according to a demanding FDA protocol (essentially a series of joint inspections with a senior staff). Disclosure can distract from the core mission.

Often there is a pretense that costs barely exist. A review in a leading public health journal concluded that calorie labeling is a "low-cost education strategy," even when finding little evidence that calorie disclosure reduces consumption. King County's efforts were ultimately preempted by a 100+ page FDA rule, promulgated in a contentious six-year long process. Implementation is now subject to an appropriations threat, which is itself evidence that the disclosure isn't exactly cheap. The Energy Star sticker, administered by the Environmental Protection Agency (EPA) and Department of Energy, also illustrates the low-cost pretense. With over 40,000 products, the agencies cannot engage in serious testing to verify whether products meet Energy Star performance standards, relying instead on company self-certification. The EPA's watchdog inspector general concluded that the system failed in identifying the most energy-efficient products and reducing greenhouse gas emissions, with little oversight of how the label was actually used. The Government Accountability Office (GAO) found the system vulnerable to fraud and abuse. The GAO even secured an Energy Star sticker for a bogus gas-powered alarm clock. (Yes, gas-powered.) To do Energy Star right would take extensive independent testing, applied to products ranging from cellulose insulation materials to computer tablets to new homes, meaning this disclosure regime may turn out to be far from simple and cheap.

Last, consider the Freedom of Information Act (FOIA) itself. Then-Professor Scalia lambasted Congress for amending the FOIA without serious consideration of resource costs (agency personnel, adjudicatory costs) to meet information requests. The FDA in 2015, for instance, employed 138 full-time staff members to respond to FOIA requests, with processing and litigation costs topping $35M. Because FOIA administration is typically subsumed in general administrative activities as a budgetary line item, this creates internal competition for agency resources. (By contrast, FDA does not have sufficient staff to step up inspections as required under the Food Safety Modernization Act.) The failure to recognize tradeoffs has also had pernicious effects on FOIA's usage. One study showed that FOIA is disproportionately used by private companies, crowding out the use by journalists. A journalist described a FOIA request as "the single most disillusioning experience of my life." If information is open to all parties alike, FOIA must be funded, or Congress must grapple with tough tradeoffs.

So what is to be done? First, policymakers should borrow from Silicon Valley's playbook and mandate "A/B testing" of any disclosure initiative. No established technology company would deploy a new user interface without such testing. In the public sector, scholars can defray research cost, just as my research team did in designing a randomized controlled trial for King County. Rigorous testing of such pilot programs would illuminate the benefits, costs, and tradeoffs of well-meaning initiatives. It would also insulate policies from judicial review. Rigorous pilot testing at the outset, for instance, would have strengthened the FDA's position in the D.C. Circuit, which invalidated FDA's graphic cigarette warning rule in part for lack of evidence.

Second, because meaningful disclosure is often predicated on effective regulation to produce high quality information, conventional regulatory reform begins to look a lot more appealing. Consider vehicle fuel economy and greenhouse gas ratings, another favorite for consumers. Volkswagen's diesel emissions scandal shows how private companies can game ratings in the absence of serious testing and oversight. It was non-governmental researchers who first discovered evidence of Volkswagen's "defeat device" that activated emissions controls only during laboratory testing (which EPA uses to verify emissions). Defeat devices are banned under U.S. law, but a ban must be enforced. In the 1990s, an EPA engineer actually invented a method to measure emissions in real driving conditions, which might have detected Volkswagen's cheating, but this EPA program was shut down in 2001. Disclosure cannot make a silk purse out of a sow's ear.

Third, policymakers should not equate simple signals with simple implementation. While the Obama administration initially aimed to rank and grade colleges based on student outcomes, it rightly recognized the complexity of this task, ultimately abandoning the grading attempt. Ask any law school dean about U.S. News rankings. Simple signals — the Energy Star, an A grade, a USDA mark — may be desired by consumers, but require serious data collection, measurement, and analysis to develop and test.

Last, just as federal law bars unfunded mandates from the federal to state government, policymakers should put their budgets where their mouths are: funding the costs of new disclosure initiatives, rather than allowing disclosure to crowd out existing agency responsibilities.

When it comes to disclosure, you get what you pay for.

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