

When economists perform a benefit-cost analysis (BCA) of a public project or policy, they think of it as summarizing the real effects of the decision on public welfare: the well-being of real people, measured according to people's own preferences. The methods they use are specifically designed to look past the familiar aggregate statistics of economic activity—the national income, gross domestic product (GDP), and so forth—to isolate net changes in economic surplus, a dollar-denominated aggregate estimate of how much better or worse off individual consumers can be expected to feel. After all, economic activity itself has no intrinsic value; it exists only to satisfy human wants. And that is how public decisions should be evaluated, too: not by how much activity they generate, but by how well they satisfy human desires, including those—like caring about whether there are whales in the ocean—that may not correspond to much observable economic activity at all.

My chapter in a new book published this week, [Does Regulation Kill Jobs?](#), explores some of the reasons why the human welfare metric, as it is typically calculated in a BCA, appears to be insensitive to the employment effects that loom so large in the perceptions of the public and its elected representatives. It argues that, to a first approximation, employment effects are already counted in a BCA as a component of compliance costs. Of course, no BCA is ever complete, so it is always possible that some job-related welfare effects are omitted, just as it is likely that some other welfare effects unrelated to employment are also omitted. Any attempt to include additional categories of welfare effects must, however, confront the problem of potentially counting these effects more than once. The chapter concludes that, in most cases, employment effects should be treated as they traditionally have been treated—implicitly part of the calculation of compliance costs—and that some proposed alternatives to the status quo would result in double counting. It would be helpful, however, if economists could do a better job of educating the public about what, exactly, compliance costs represent. If people understood that these are not simply a “cost of doing business” but real welfare changes experienced by the public, then benefit–cost analysis would be a far more informative tool than it is today.

Although an explicit treatment of employment effects is rarely found in a typical BCA, it is not accurate to say that BCA ignores employment effects; rather, it treats employment as a voluntary transaction, which takes place at a price mutually agreeable to the employer and the employee. As such, a job is neither a cost nor a benefit—both parties to the transaction experience both costs and benefits that, at the margin, are expected to be in balance. Hence small changes in the level of employment would be expected to generate zero net benefits. At the same time, the level

¹ This commentary is excerpted from Chapter 10 of [“Does Regulation Kill Jobs?”](#)



of employment quickly finds its equilibrium level, as any jobs lost or gained in consequence of a policy decision will likely be offset elsewhere in the economy.

When a regulation affects the employment transaction directly, this *ceteris paribus* equilibrium assumption would not apply: different options may produce very different effects. A minimum wage, for example, will change the level of employment as well as the level of wages; empirical studies can help determine what the effects are, and a BCA could not realistically assume that regulated wages were in equilibrium. More broadly, it may be the case that taxes on employment (especially payroll taxes) or some regulatory requirements (such as pension and health care provisions) alter wages in a way that produces systemic distortions significant enough to warrant an adjustment in routine BCAs.

When a BCA has been done properly, it accounts for the lost output that results from directing resources away from consumer goods and services to, say, pollution control. The reduced output of market goods represents a welfare loss to somebody; we just do not know to whom. For better or for worse, the BCA metric is indifferent to who experiences gains and losses; it is interested only in the sum.

Too often, people fail to realize that in a BCA, both benefits and costs are cut from the same cloth. This illustrates a major weakness of BCA as a communication tool. By using compliance costs as a proxy for downstream welfare effects, it allows people—including government decision makers—to believe the fiction that compliance costs somehow will be “absorbed by business.” The truth is, when it comes to welfare changes, business does not absorb anything. The costs of regulation fall on real people, and these costs can be painful and even deadly.

Join us on [February 13](#) for a discussion of the new book.

