Unit 4 – What Regulatory Roles Does Government Play in Our Economy?

Before you read:

1. The video used the term "healthy competition." Why is competition important in a free market system?

2. Why did the government need to step in and regulate businesses?

3. Can there be overregulation? Explain.

What Regulatory Roles Does Government Play in Our Economy?

Government's Role in Maintaining Competition

Like property rights, competition is essential if markets are going to work the way they are supposed to work. The pressures of competition force producers to use resources efficiently, to develop new or better products, and to keep products and services affordable. Because competition is vital to the economy, the government acts to maintain competition when markets fail to do so.

The government's main guardian of competition is the Justice Department. This cabinet-level department, through its Antitrust Division, enforces the antitrust laws that Congress has enacted over the years. It often works closely with the Federal Trade Commission. The FTC is a **regulatory agency**—a unit of government that makes and enforces standards for an industry or area of economic activity.

As modern-day trustbusters, the Justice Department and the FTC prohibit practices that restrict competition. When they uncover such practices, they take the offending companies to court. Successful prosecution can lead to fines and jail sentences for the guilty parties. These illegal practices include the following:

Price fixing. The illegal practice of **price fixing** occurs when competitors agree on a price for a good or service. Price fixing can take many forms, from adopting a formula for computing prices to setting a minimum fee for services.

Market division. The tactic known as **market division** occurs when competitors agree to divide a market among themselves. In one type of scheme, each competitor sells to only certain customers. In another, each competitor sells in only certain geographic areas.

Government's Role in Protecting Consumers, Savers, and Investors

Caveat emptor. This long-standing rule of the marketplace is Latin for "Let the buyer beware." It serves as a warning to buyers that they purchase goods and services at their own risk. But in today's complex market, buyers may not have all the information they need to make sound judgments about products. Instead, they have come to rely on regulatory agencies to provide such information. Consumers, savers, and investors also look to such agencies to ensure that products are safe and dependable.

Protecting consumers. Regulation to protect consumers began in the early 1900s. One of the first targets of government regulators was the meatpacking industry. Upton Sinclair, in his novel *The Jungle*, described what went on in meatpacking plants:

There would be meat that had tumbled out on the floor, in the dirt and sawdust, where the workers had tramped and spit . . . meat stored in great piles in rooms; and the water from leaky roofs would drip over it, and thousands of rats would race about on it . . . These rats were nuisances, and the packers would put poisoned bread out for them; they would die, and then rats, bread, and meat would go into the hoppers together.
—Upton Sinclair, *The Jungle*, 1906

Thanks in part to Sinclair's stomach-turning prose, Congress passed both the Meat Inspection Act and the Pure Food and Drug Act in 1906. This legislation paved the way for a new regulatory agency, now known as the Food and Drug Administration. The FDA oversees the testing and approval of drugs before they go on the market.

Another wave of consumer regulation began in 1965, triggered by Ralph Nader's book *Unsafe at Any Speed*. Nader claimed that automobiles were unsafe and that the auto industry resisted making cars safer because of the added cost. The next year, Congress passed legislation requiring automakers to install seat belts in all cars. This law led to the creation of an agency to set safety standards for automobiles, the National Highway Traffic Safety Administration.

Protecting savers and investors. Of the many banking-related agencies, the Federal Deposit Insurance Corporation may have the most direct role in protecting savers. The FDIC insures nearly all bank deposits for up to $100,000 per depositor.

The Securities and Exchange Commission protects investors by making sure they have the information they need to judge whether to buy, sell, or hold a particular security. The SEC establishes and enforces rules to ensure that companies provide that information in a timely and accurate manner.

Such regulatory agencies allow Americans to feel confident when transacting business with total strangers. As the president of a Federal Reserve Bank once observed,

It seems remarkable, when you think about it, that we often take substantial amounts of money to our bank and hand it over to people we have never met before. . . . We trust that . . . the person at the bank who takes our money doesn't just pocket it. Or that when we use our credit cards to buy a new CD or tennis racquet over the Internet, from a business that is located in some other state or country, we are confident we will get our merchandise, and they are confident they will get paid.
—Jerry Jordan, 2000

Government's Role in Protecting Workers

The federal government safeguards the interests of workers through the Department of Labor. One of DOL's primary aims is to protect workers' economic rights. It does this by making sure workers get the wages due to them, fostering workplaces that are free of discrimination, and providing unemployment insurance.

Another goal of DOL is protecting workers' physical well-being. To ensure safe and secure workplaces, DOL relies mainly on the Occupational Safety and Health Administration. OSHA sets safety and health standards for industries. When you see construction workers wearing hard hats or highway workers wearing reflective vests, you can be sure OSHA standards are involved. Since OSHA was established in 1971, workplace fatalities have decreased by more than 60 percent and injury rates by 40 percent.

Problems with Overregulation. Regulation can be very expensive, both for the regulatory agencies and for the businesses that must comply with the rulings of those agencies. Sometimes regulations are so detailed and complex that they actually discourage economic activity. For example, consider this requirement from an early OSHA standard on ladder safety:

The general slope of grain in flat steps of minimum dimension shall not be steeper than 1 in 12, except that for ladders under 10 feet in length the slope shall not be steeper than 1 in 10 . . . Local deviations of grain associated with otherwise permissible irregularities are permitted.
A building contractor faced with page after page of such regulations might well decide to simply abandon jobs that require ladders.

After you read:

1. Think of an example of some kind of government regulation you saw or experienced recently. What was it? Was it necessary?