

Why do we regulate?

Richard W. Rahn

Should government regulate business? I expect most people would answer "yes" to that question, but if you ask them why, I expect these same people will have a harder time giving an answer that makes sense.

Some may say, "in order to prevent businesses from engaging in fraud or misrepresentation." But we do not need regulation to do that; there are already many federal, state and local statutes against fraud and misrepresentation, and businesses that behave badly can be dealt with through normal civil and criminal legal means. Others who are a bit more sophisticated might argue that we need to regulate business in order to protect people from "market failures." However, the empirical evidence is that there are far fewer "market failures" than commonly imagined, and many of these so-called market failures are actually a result of misguided government policy or regulation.

For a minute, try to imagine a world without government regulation, but where all of the standard laws against theft, fraud, misrepresentation and bodily injury still exist. Under such a scenario, what do you think would happen if we had no food and drug administration to tell us what was safe to consume? No financial regulators to protect us from bank failures and financial scams? No health and safety regulators to protect us from unsafe products? Would we all die? Not likely, because the judicial system, coupled with private standard setting associations, would likely give us an equal, if not a higher, level of protection than we have now.

More than a century ago, when electrical appliances were first being developed and sold, there was a problem in that many of the new products shocked their customers and/or started fires. The electric appliance industry quickly understood this situation was dangerous and not good for business and thus started an industry sponsored organization to test products to make sure they were safe and reliable. The organization was called Underwriters Laboratories. It still exists today to ensure that electrical products bearing the UL seal are safe, and its mark has become the standard.

In the absence of regulation, virtually every industry would do the same thing, because legitimate enterprises know that being known for selling faulty products would ruin their reputation and put them out of business. Unfortunately, as a result of ceaseless propaganda from pro-government interest groups, most Americans have been brainwashed into thinking they need regulatory agencies to protect them.

A most provocative paper has just been published by the American Enterprise Institute, written by former U.S. Treasury General Counsel Peter Wallison, entitled "Why Do We Regulate Banks?" Mr. Wallison argues that "it is difficult to identify a sound policy reason for regulating banks. Most of the conventional explanations -- inherent bank instability, deposit insurance, the Federal Reserve's role as lender of last resort, or the Fed's role in the large-dollar payment system -- turn out on examination to be either unfounded or based on risks that the government need not take in order to foster growth of the economy." Mr. Wallison goes on to detail "the huge costs to the taxpayers and the economy" caused by bank and S&L failures that have been due to regulation. Finally, Mr. Wallison, who has had major regulatory responsibility, concludes as to the question, "Why do we regulate banks? That we do so because we want to, not because we must."

In an excellent paper dealing with the telecom industry by Stephan B. Pociask, titled "Wireless Substitution and Competition," published by the Competitive Enterprise Institute, the author finds "convincing evidence that wireless services are strong substitutes for wireline

services." His analysis concludes that "the nature of competition has changed, and it also means that price and service regulation is largely unneeded, since market forces are sufficient to hold prices in check."

The point of these above examples is that we have more and more evidence that much of government regulation is not only not needed but is non-productive and destructive. It is now estimated that this year our total regulatory burden will be \$913 billion, or roughly eight percent of the U.S. gross domestic product.

Unneeded and harmful regulation has very real costs to people that shows up in fewer jobs, less international competitiveness, less freedom, and a lower standard of living for most people. It is time for us to fundamentally rethink the regulatory state. Your local supermarket does not need the government to tell it to sell only safe food, because if it doesn't its customers will go elsewhere, and it will also be sued. A free market system with few barriers to entry for new competitors, coupled with a strong legal system that penalizes neglect and misbehavior, is more likely to protect the citizen with lower costs than whatever number of regulatory agencies can be developed by the government class.

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