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The Potential for Reducing Inflationary Pressures by Reforming Government Regulation

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Preface

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Numerous government activities, often unwittingly, generate inflationary pressures or otherwise interfere with the attainment of important national goals unrelated to the specific activities. These unwanted side-effects occur in good measure because government policymakers frequently tend to ignore the effects of government programs on productivity, capital formation, innovation, employment, and inflation.

For example, government imposition of socially desirable requirements on business through the regulatory process appears to be an inexpensive way of achieving national objectives. It costs the government little and is no significant burden on the taxpayer. But, the public does not escape paying the cost. Every time that the Environmental Protection Agency imposes a more costly, albeit less polluting, method of production, the cost to the consumer of the resultant product will tend to rise. Similarly, each time that the Consumer Product Safety Commission sets a standard which is more costly to attain, some product costs will tend to increase.

The monetary authorities could offset the inflationary effects of regulation by attempting to maintain a lower rate of monetary growth. In practice, however, public policy makers tend to prefer the higher rate of inflation to the additional monetary restraint and the resulting decreases in employment and output. Also, to the extent that real resources are devoted to low-payoff activities, economic welfare is reduced.[1/] The loss of the potential increases in productivity from such diversion eliminates a possibility of offsetting ordinary factor cost increases and thus exacerbates the inflation problem.

It is not inevitable, of course, that every regulatory activity increase inflationary pressures. In those instances where regulation generates social benefits

Note: The author is indebted to Roland McKean and Lee Benham for numerous useful insights and helpful suggestions.

(such as a healthier and thus more productive work force) in excess of the social costs imposed by the government action, inflationary pressures should be reduced. The point being made here is that many forms of governmental intervention in the private sector involve heavy costs -- and that, with some care and concern, the regulatory process might be revised so as to achieve comparable benefits at lower costs. Indeed, the central purpose of this paper is not to propose the general elimination of regulatory programs but to indicate some of the more promising approaches to reducing their inflationary consequences.

Adverse Impacts of Government Regulation of Business

Regulation and Inflation

There are a variety of ways, direct and indirect, in which the operation of governmental regulatory programs contributes to an exacerbation of the inflation problem. In some cases, the impact is direct and visible to all. A striking case in point is the passenger automobile, where the federal government has mandated a wide array of specified safety and environmental features to be incorporated by the manufacturer. In the case of the so-called interlock system, the public outcry became so intense that the Congress overruled the regulators, eliminating the requirement.

Other types of government regulation may be indirect but equally costly. Several research efforts examining building regulations have documented repeated instances of increases in the price of housing due to building codes. A study at Rutgers University tentatively concluded that overly stringent or outdated codes increase housing costs by somewhere between 5 and 10 percent of total unit costs.[2/] Several scholars have estimated the effects of land-use controls on the cost of residential housing. Although the analyses vary in methodology and data, they generally conclude that there is a weak to moderate, but uniformly positive, relationship between single family housing costs and land use controls in developing areas.[3/]

In many other ways, government regulation increases the overhead cost of producing goods and services. The rapidly rising paperwork burden furnishes a striking case in point. One large corporation, the Standard Oil Company of Indiana, is required to file approximately 1,000 reports annually to 35 federal agencies including the Federal Power Commission, the Federal Energy Administration, the Bureau of Indian Affairs, and the Small Business Administration. Duplication inevitably occurs. The company must report its oil and gas reserves, with each report taking slightly different form, to the FEA, the FPC, the FTC, and the U.S. Geological Survey. It requires 636 miles of computer tape to store the data that the company must supply to the Federal Energy Administration. In total, Indiana Standard has 100 full-time employees whose work is centered around meeting federal regulations, at an annual cost of about $3 million.[4/]

Employee fringe benefit costs are increasing as a result of new pension regulations. Some portion of advertising costs results from the requirements imposed by affirmative action programs in the equal employment opportunity area. More indirectly, it is likely that productivity is affected by the variety of regulations that are designed to improve the quality of the work environment. To the extent that the regulations reduce accidents and absenteeism they do indeed contribute positively to output and thus economic welfare.

But in practice the emphasis has shifted to essentially "bureaucratic" concerns. More forms are now filled out. More safety rules are posted. More inspections take place. More fines are levied. But, no significant reduction in industrial accident rates has resulted. Table 1 contains the latest available data on accident rates in American industry. It can be seen that the experience for 1973 (the first year of operation of the Occupational Safety and Health Administration) was not any more favorable than for 1972, the year prior to the advent of OSHA.

Table 1

Recordable Occupational Injury and Illness Incidence Rates for Selected Comparable Industry Divisions, Private Nonfarm Sector, United States, 1973 and 1972

Industry	Incidence rates per 100 full-time workers[1]					
	Total recordable cases		Lost workday cases		Nonfatal cases without lost workdays	
	1973	1972	1973	1972	1973	1972
Private nonfarm sector[2]	11.0	10.9	3.4	3.3	7.6	7.6
Transportation and public utilities[3]	10.5	10.8	4.6	4.5	5.9	6.3
Wholesale and retail trade	8.6	8.4	2.7	2.8	5.9	5.6
Finance, insurance, and real estate	2.4	2.5	.8	.8	1.6	1.7
Services[4]	6.3	6.1	2.0	2.0	4.3	4.1

[1] The incidence rates represent the number of injuries and illnesses per 100 full-time workers, and were calculated as: (N/EH) x 200,000, where

N = number of injuries and illnesses

EH = total hours worked by all employees during calendar year

200,000 = base for 100 full-time equivalent workers (working 40 hours per week, 50 weeks per year)

[2] Includes oil and gas extraction which is not a component of the industry divisions listed. Other mining activities are not included.

[3] Excludes railroads (SIC 401).

[4] Includes agricultural services, forestry, and fisheries (SIC 07-09).

Source: U. S. Bureau of Labor Statistics, Department of Labor, Occupational Injuries and Illnesses by Industry, 1973, 1975, p. 2.

In the case of the job safety program, as in numerous other areas of government involvement, the important original concern of the public and the Congress has been converted to the practice of not violating the rules and regulations. "You won't get into trouble if you don't violate the safety standards," is the response, even if as many accidents occur as before. The emphasis shifts to such trivia as raising and answering these types of questions: How big is a hole? When is a roof a floor? How frequently must spittoons be cleaned? The results in terms of the safety objective are almost invariably disappointing. Yet, the reaction to this situation is virtually predictable: redouble the existing effort -- more rules, more forms, more inspections, and thus higher costs to the taxpayer and higher prices to the consumer.

Regulation and Innovation

A hidden cost of government regulation is a reduced rate of innovation. The longer that it takes for a new product to be approved by a government agency -- or the more costly the approval process -- the less likely that the change will be made. In any event, innovation will be delayed.

A recent case is the new asthma drug beclomethasome dipropionate (BD). Although this drug has been used successfully by millions of asthma patients in England, it still has not received approval of the U.S. Food and Drug Administration. BD is described as a safe and effective replacement for the drugs which are now administered to chronic asthma patients, but without the adverse side effects of the drugs in use in the United States. Unlike BD, the steroids currently prescribed in this country, such as prednisone, can stunt growth in children, worsen diabetes, increase weight through water retention, and cause bone softening. The delaying procedures of the FDA are preventing Americans from switching to the safer product, BD.[5/]

Professor Sam Peltzman of the University of Chicago estimates that the 1962 amendments to the Food and Drug Act are delaying the introduction of effective drugs

by about four years, as well as leading to higher prices for drugs.[6/] As a result in good measure of the more stringent regulation, the United States was the 30th country to approve the anti-asthma drug metaproterenol, the 32nd country to approve the anti-cancer drug adriamycin, the 51st country to approve the anti-tuberculosis drug rifampin, the 64th country to approve the anti-allergenic drug cromolyn, and the 106th country to approve the anti-bacterial drug co-trimoxazole.[7/]

The regulators really seem to have the private sector scared. In August 1975, the National Cancer Institute reported that the solvent trichlorethylene, known as TCE, may be a possible cause of cancer. TCE at the time had been used in decaffeinated coffee. It seems that the government used a rather generous dose of the chemical on the test animals. It was the equivalent of a human being drinking 50 million cups of decaffeinated coffee every day for an entire lifetime. It would seem that the consumer's bladder would give out or he or she would drown before having to worry about getting cancer. But what was the industry's reaction? To laugh at this example of governmental nonsense? Hardly. With the cyclamate episode still firmly in mind, one major producer quickly changed to another chemical.[8/]

Examples of obvious inefficiencies or trivia in regulation of business are not hard to come by.[9/] Capable, intelligent and well-meaning administrators delegating decisions to capable, intelligent and well-meaning subordinates cannot specify in advance all of the correct or desirable exceptions to general rules. Upon examination, the reported examples of regulatory nonsense often do not turn out to be mere flukes. They are almost an inevitable result of the rapid expansion of the scope and variety of regulatory functions that has occurred in the United States in recent years.[10/]

The adverse effect of regulation on innovation may be felt more strongly by smaller firms and thus have an anti-competitive impact. According to Dr. Mitchell

Zavon, president of the American Association of Poison Control Centers:

> "We've got to the point in regulatory action where it's become so costly and risky to bring out products that only the very largest firms can afford to engage in these risky ventures. To bring out a new pesticide you have to figure a cost of $7,000,000 and seven years of time."11/

Regulation and Capital Formation

Federal regulation also affects the prospects for economic growth and productivity by levying a claim for a rising share of new capital formation. This is most evident in the environmental and safety areas and its importance can be observed quite readily.

An examination of the flow of capital spending by American manufacturing companies just prior to the recent recession is quite revealing. In 1969, the total new investment in plant and equipment in the entire manufacturing sector of the American economy came to $26 billion. The annual totals rose in the following years. But when the effect of inflation is eliminated, it can be seen that four years later, in 1973, total capital spending by U.S. manufacturing companies was no higher. In "real terms," it was approximately $26 billion in both years.

That is not the end of the story, however. In 1973, a much larger proportion of capital outlays was devoted to meeting government regulatory requirements in the pollution and safety area -- $3 billion more, to be specific.12/ Hence, although the economy and its needs had been growing substantially in those four years, the real annual investment in modernization and new capital had actually been declining. The situation was worsened by the accelerated rate at which existing manufacturing facilities were being closed down because the rapidly rising costs of meeting government regulations meant that they were no longer economically viable. About 350 foundries in the United States have been closed down during 1971-1974 because they could not meet requirements such as those imposed by the Environmental Protection Agency and the Occupational Safety and Health Administration.13/ This may help to

explain why the American economy, for a substantial part of 1973, appeared to lack needed productive capacity, despite what had been large nominal annual investments in new plant and equipment in recent years.

The governmental decision-making process can have other adverse effects on capital formation by introducing uncertainty about the future of regulations governing the introduction of new processes and products. An example is furnished in a November 1975 report of a task force of the President's Energy Resources Council dealing with the possibility of developing a new synthetic fuel industry. In evaluating the impact of the Federal Water Pollution Control Act Amendments of 1972, the task force reported, "It would be next to impossible at this time to predict the impact of these requirements on synthetic fuels production."14/

With reference to the National Environmental Policy Act of 1969, the task force stated that the major uncertainty was not whether a project would be allowed to proceed, but rather the length of time that it would be delayed pending the issuance of an environmental impact statement that would stand up in court. The task force pointed out, "The cost of such delays (construction financing and inflated raw materials and labor costs) is an obvious potential hazard to any synfuels project."15/

In evaluating the overall impact of government regulatory activity, the task force concluded, "In summary, some of these requirements could easily hold up or permanently postpone any attempt to build and operate a synthetic fuels plant."16/

Regulation and Employment

Government regulation, albeit unintentionally, can have strongly adverse effects on employment. This has been demonstrated in the minimum wage area where teenagers have increasingly been priced out of labor markets. One recent study has shown that

the 1966 increase in the statutory minimum wage resulted by 1972 in teenage employment in the United States being 320,000 lower than it otherwise would have been. As a result of that one increase in the compulsory minimum wage, the youth unemployment rate in 1972 was 3.8 percentage points higher than otherwise would have been the case.[17/]

In the construction labor area -- where unemployment rates are substantially above the national average -- government regulation also acts to price some segment of the work force out of competitive labor markets. Under the Davis-Bacon legislation, the Secretary of Labor promulgates "prevailing" wages to be paid on federal and federally-supported construction projects. A variety of studies has shown that these federally-mandated wage rates are often above those that actually prevail in the labor market where the work is to be done.[18/]

Perhaps although only to a minor degree, the equal employment opportunity program may tend to increase unemployment by delaying the filling of job vacancies. To the extent that employers must undergo protracted job searches prior to hiring employees, the average length of unemployment is likely to be longer. It is not uncommon for a position to remain unfilled despite the presence of an adequate labor supply at market prices because the governmental regulatory requirements have not been met.

Regulation and Entrepreneurial Functions

One of the immeasurable impacts of government regulation relates to the basic entrepreneurial nature of the private enterprise system. To the extent that management attention is diverted from traditional product development, production, and marketing concerns to meeting governmentally-imposed social requirements a significant but subtle socialization of corporate activity may result.

In the employee pension area, for example, the recently-enacted pension regulation has shifted much of the concern of the management of the pension funds from maximizing the return on the contributions to following a more cautious approach of minimizing the likelihood that the fund managers will be criticized for their investment decisions. It thus becomes safer -- although not necessarily more desirable to the employees covered -- for the pension managers to keep more detailed records of their deliberations, to hire more outside experts (so that the responsibility can be diluted), and to avoid innovative investments.19/

It may be difficult to appreciate the extent of the detail and minutia of the government regulation which is imposed on private sector activities. It is instructive to examine the Federal Register, the official publication which contains the rules and regulations promulgated by federal agencies. The January 16, 1976 issue is dominated by the 94 pages of tables which contain the minimum wage rates for federal and federally-assisted construction established by the Secretary of Labor under the Davis-Bacon Act.

Of the remainder of the January 16 Register, a major item relates to the orange juice standards of the Food and Drug Administration. This section ranges from the types of equipment which are deemed acceptable to measure the color of orange juice to the number of points required (36 to 40) for canned orange juice to qualify as being of "good color." This fascinating portion of the Register is followed by lemon regulation 22, which restricts the number of lemons which may be shipped from California and Arizona during the period January 18-24. Another FDA regulation then describes the handling of dried prunes.

Several of the other items in the January 16 Register may be of somewhat greater importance. They deal with standards on school bus brakes, procedures for making rural housing loans, advertising for eye glasses, subsidies for local railroad service, and the amount of notice that must be given if a drawbridge is required to

be open. Not all of the items in the January 16 Register necessarily impress the casual reader as being those matters of high national policy which the Founding Fathers presumably had in mind in forming a more perfect union.

Approaches to Regulatory Reform

A new way of looking at the microeconomic effects of government programs is needed. A parallel can be drawn to macroeconomic policymaking, where important and at times conflicting objectives are recognized. Attempts at reconciliation or trade-off are made, such as among economic growth, employment, income distribution, and price stability.

At the programmatic or microeconomic level, it is also necessary to reconcile the goals of specific government programs with other important national objectives, which are not now in practice the concern of many of those agencies. Healthy working conditions are an important national objective, but surely not the only one. And society has no stake in selecting the most costly and disruptive methods of achieving a higher degree of job safety. A similar situation occurs in relating environmental protection, product safety, and other regulatory efforts with such important practical concerns as the cost to the consumer, the availability of new products, and the efficiency of productive activity.

One method of broadening the horizons of government policymakers and administrators is through the device of the economic impact statement. The requirement that they consider the costs and other adverse effects of their actions as well as the benefits should be imposed on the economic regulatory commissions as well as on the regulatory activities of the other departments and agencies. Economic impact statements also should be required of procurement and subsidy programs which contain regulatory features.

This is not a plea for the elimination of government regulation, but rather for reducing where possible the inflationary and other undesirable consequences. The theoretical rationale for this moderate approach was provided by Professor F. A. Hayek in his Constitution of Liberty:

> "...a free market system does not exclude on principle... all regulations governing the techniques of production... They will normally raise the cost of production, or what amounts to the same thing, reduce overall productivity. But if this effect on cost is fully taken into account and it is still thought worthwhile to incur the cost to achieve a given end, there is little more to be said about it. The appropriateness of such measures must be judged by comparing the overall costs with the gain; it cannot be conclusively determined by appeal to a general principle."20/

In a more specific way, the same point was made by a leading liberal legislator. Senator Hubert Humphrey has provided a very cogent example of the shortcomings of the existing regulatory approach:

> "The government goes around willy-nilly making decisions of consequence. There was no estimate of the economic impact of the Occupational Safety Act, for example. I happen to be for the occupational safety program, but what were its economic implications? Did anyone think that through? No."21/

The policy formation process needs to proceed beyond merely another set of so-called inflation impact statements. First of all the costs and the benefits need to be more than examined; they should be weighed one against the other. In the process the actual or proposed regulations that generate excessive costs should be modified or eliminated. But we need to go beyond the direct impact on price, and include the relationship to productivity, capital formation, and innovation.

Relating Costs to Benefits

In November 1974, President Gerald Ford did instruct the federal agencies under his jurisdiction to examine the effects of the major regulatory actions that they would be taking on costs, productivity, employment, and other economic factors

(Executive Order 11821). Although a useful step forward, there are severe shortcomings in this effort. First of all, many of the key regulatory agencies -- ranging from the Consumer Product Safety Commission to the Federal Trade Commission -- are so-called "independent agencies," which are beyond the President's purview.

Even in the case of the regulatory activities which come within the President's jurisdiction, the new policy is limited to the regulations which, in the issuing agency's own estimation, are "major." In any event, the agencies covered by the Executive Order are only required to examine the economic aspects of their actions.[22/] A broader approach seems to be warranted, in the fashion of the current environmental impact statements.

The society is now supposed to examine the impact on the environment of the various major actions that it takes. Would it not also be appropriate to require each federal, state, and local environmental agency to assess the impacts of its actions on the society as a whole, and particularly on the economy? Surely a cleaner environment is an important national objective. But it is not the only national objective. Certainly the nation has no stake in selecting the most expensive or most disruptive ways of achieving its environmental goals.

Much would depend on the "teeth" that would be put into the required economic impact statement. Merely legislating the performance of some economic analysis by an unsympathetic regulator would primarily delay the regulatory process and make it more costly. But limiting government regulation to those instances where the total benefits to society exceed the cost would be a major departure. It could significantly slow down if not reverse the current rising trend of federal regulation of business.

To an economist, government regulation should be carried to the point where the incremental benefits equal the incremental costs, and no further. (Indeed, this is

the basic criterion which is generally used to screen proposed government investments in physical resources.) Overregulation -- which can be defined a situation where the costs exceed the benefits -- should be avoided. But if policymakers tend to ignore or downplay the costs, we are bound to operate in the zone of overregulation, which is likely where we are today.

In making decisions on which regulations to adopt, the governmental decisionmaking body should pay particular attention to several "overhead" types of areas that are often neglected -- the monitoring costs by the government itself, the information costs imposed on both the public and private sectors, and the related private costs of compliance and/or avoidance. It is hardly coincidental that, simultaneous with the recent expansion of governmental regulatory activity, the cost of legal departments and of legal services has been one of the most rapidly growing segments of company budgets.

It is also important to build into the governmental processes those incentives which would encourage government officials to give greater weight to the costs and other side-effects generated by the actions that they take. Limiting new regulations to those instances where it can be demonstrated that net benefits accrue to society as a whole is one such device. At the operational level, attention might be given to the use of the budget process as an added tool of management of regulation. In those cases where the cost-benefit analyses produced by an agency did not turn out to be an accurate representation of the effects of a regulation -- i.e., where an agency's regulations in practice generate more costs than benefits -- its budget for the coming year would be reduced, and vice versa.

The wide dissemination of the data on the economic impacts of government regulation might serve to alter the balance of interest group forces now exerted on the decisionmaking process. At the present time, it often appears that the interest groups which would benefit from the regulation are well aware of those positive con-

tributions and thus mobilize their forces in favor of greater regulation. But the information on the adverse consequences of regulation, if widely distributed, might generate countervailing interest group pressures.[23/]

Reorganization of Regulation

The effort, however, needs to proceed beyond mere statistical analysis. It should also cover the question of reorganizing the wide variety of regulatory agencies that has been established. During the past decade there has been a rapid expansion of federal regulatory agencies. Newcomers to the federal bureaucracy include the Consumer Product Safety Commission, the Environmental Protection Administration, the Federal Energy Administration, the National Transportation Safety Board, and the Occupational Safety and Health Administration.

As shown in Table 2, the expenditures of the major federal regulatory agencies came to almost $2.8 billion in the fiscal year 1976. This is a 48 percent increase over the costs of these regulatory activities in fiscal 1974. It is apparent that the biggest regulatory budgets are not those for the traditional industry-specific regulatory commissions, such as the ICC ($50 million) or the CAB ($85 million). Rather, the largest proportion of the funds is devoted to the broader, industry-wide regulatory activities of the Department of Labor ($397 million, mainly for wage and hour standards and job safety), Agriculture ($381 million, largely for food inspection), and the Federal Energy Administration ($208 million).

A consolidation of the numerous federal regulatory agencies may now be desirable. Each of these regulatory agencies was created at a different time and usually to further one specific objective -- a cleaner environment, healthier working conditions, safer products, etc. Legislative mandate in hand, each agency pursues its individual tasks, as it sees them. Yet increasingly achieving one agency's objective may frustrate if not negate the performance of another. The Environmental Protection

Table 2

Types of Federal Regulatory Activities
Fiscal year 1976. In millions of dollars.

Area and Agency	Amount
Consumer Safety and Health	
Department of Agriculture	$ 381
Department of Health, Education, and Welfare	189
Department of Justice	171
Department of Transportation	234
Department of the Treasury	320
Consumer Product Safety Commission	37
National Transportation Safety Board	10
Subtotal	1,342
Job Safety and Other Working Conditions	
Department of the Interior	79
Department of Labor	397
Equal Employment Opportunity Commission	60
National Labor Relations Board	70
Occupational Safety and Health Review Commission	6
Subtotal	612
Environment and Energy	
Environmental Protection Agency	54
Federal Energy Administration	208
Subtotal	262
Financial Reporting, etc.	
Cost Accounting Standard Board	2
Council on Wage and Price Stability	2
Securities and Exchange Commission	49
Subtotal	53

Table 2 (continued)

Industry-Specific Regulation	
Civil Aeronautics Board	85
Commodity Futures Trading Commission	11
Federal Communications Commission	50
Federal Maritime Commission	8
Federal Power Commission	36
Federal Trade Commission	45
International Trade Commission	10
Interstate Commerce Commission	50
Nuclear Regulatory Commission	198
Renegotiation Board	5
Subtotal	498
Grand Total	2,767

Source: Budget of the U.S. Government for the Fiscal Year 1976.

Agency encourages the conversion of powerplants from coal to less polluting fuels such as natural gas and then the Federal Energy Administration urges the shift back to coal, which is the relatively more plentiful fuel. Examples abound of overlapping jurisdictions and cross-cutting objectives -- job safety versus elimination of discrimination, a quieter workplace versus a cleaner workplace, clean air versus clean water, etc.

For example, the desulfurization of coal -- to reduce air pollution -- requires a combination with lime. But doing that generates large quantities of solid waste calcium sulfate. Disposing of calcium sulfate in turn creates water pollution problems. Another example relates to federal food standards which require meat-packing plants to be kept clean and sanitary. Surfaces that are easiest to clean are usually tile or stainless steel. But tile and stainless steel are highly reflective of noise. They may not always meet the standards set for occupational safety and health.

Perhaps an organizational structure can be developed which encourages better communication among the regulators and, especially, the reconciliation of conflicting objectives within the governmental mechanism. Such action might permit a greater degree of "internalizing" the benefits and costs that arise from the regulatory process. Moreover, such attempt at reconciliation would be performed in the government itself, and hopefully prior to the issuance of regulations. That could help to reduce the situations where business firms and individuals are caught in the crossfire of conflicting government regulations.

General Attitudes Toward Regulation

More basically, however, it is attitudes that need to be changed. The experience under the job safety program provides a striking point. Although the government's safety rules, regulations, and requirements have resulted in literally billions of

dollars in public and private outlays, the basic goal of a safer work environment has not been achieved.

A more satisfying answer requires a basic change in approach to regulation, and one that is not limited to the job safety program. Indeed, that program is used here merely as an illustration. If the objective of public policy is to reduce accidents, it should focus directly on the reduction of accidents. Excessively detailed regulations often are merely a substitute for hard policy decisions. Rather than issuing citations to employers who fail to fill out the forms correctly or who do not post the correct notices, the emphasis ought to be placed on those employers with high and rising accident rates, perhaps levying fines on those with the worst safety records. (Variable insurance rates may perform a similar function). As the accident rates decline toward some sensible average standard, the fines could be reduced or eliminated.

But the government should not be concerned with how a specific company achieves the objective of a safer working environment. Some may find it more efficient to change work rules, others to buy new equipment, and still others to retrain workers. But that is precisely the kind of operational business decisionmaking that government should avoid, but which now dominates so many of these regulatory programs. Without diminishing the responsibility of the employers, the sanctions under the federal occupational safety and health law should be extended to employees, especially those whose negligence endangers other employees. The purpose here is not to be harsh, but to set up effective incentives to achieve society's objectives. This can be a preferred alternative to government specifying the details of what it considers to be "acceptable" private action.

Any realistic appraisal must acknowledge that important and positive benefits have resulted from many of the government's regulatory activities -- in terms of less

pollution, fewer product hazards, ending job discrimination, and achieving other socially desirable objectives of our society.

It should also be realized that these federal programs were established by the Congress in response to a surge of rising public expectations about corporate performance. Although business executives rarely talk or write in terms of the costs and benefits of their actions to society as a whole, they often are aware of that basic justification for governmental intervention. The president of Chrysler furnished a cogent example in justifying governmental automobile pollution controls:

> "...a large part of the public will not voluntarily spend extra money to install emission control systems which will help clean the air. Any manufacturer who installs and charges for such equipment while his competition doesn't soon finds he is losing sales and customers. In cases like this, a Government standard requiring everyone to have such equipment is the only way to protect both the public and the manufacturer."[24/]

But the "externalities" generated by federal regulation need not justify government's attempt to closely regulate every facet of private behavior.

Alternatives to Regulation

The promulgation by government of rules and regulations restricting or prescribing private activity is not the only means of accomplishing public objectives. As Roland McKean has pointed out, codes of behavior which are adhered to on a voluntary basis may often be effective.[25/] That approach may have special application at the present time. The recent revelations concerning misdeeds by corporate executives in their dealings with various government officials are leading to pleas for tighter regulation of such business behavior. But given the almost universal public outrage which has resulted, it is most likely that the prevailing norms of corporate behavior are being changed substantially -- and voluntarily -- so as to avoid repeating the episodes which have proven so damaging both to the individuals and to their organizations.

Government itself has available to it numerous powers other than regulation. Through its taxing authority the government can provide strong signals to the market. For example, rather than promulgating detailed regulations governing allowable discharges into the nation's waterways, the government could levy substantial taxes on those discharges. Such sumptuary taxation could be "progressive", to the extent that the tax rates rise faster than the amount of pollution emitted by an individual polluter. Thus, there would be an incentive to concentrate on removing or reducing the more serious instances of pollution rather than dissipating environmental clean-up efforts as is often the case at the present time.

Using taxation is not meant to punish polluters, or even to give them a "license" to pollute. Rather it would be an effort to utilize the price system by encouraging producers and consumers to shift to less polluting and thus more economical ways of producing and consuming goods and services. The basic concept is simple: most people do not pollute because they get positive pleasure from dirtying the environment. Rather they pollute because it often is easier or cheaper than not polluting. By changing basic incentives through the tax-price mechanism, individuals and organizations (both public and private) would be encouraged voluntarily to alter their economic behavior in a manner which is more conducive to the goals of the society. Perhaps most important would be the shift in public-private relationships from the current adversary position to a more neutral and efficient mode of conduct.

Footnotes

1/ For a more extensive discussion, see Murray L. Weidenbaum, Government-Mandated Price Increases (Washington, D. C.: American Enterprise Institute, 1975).

2/ See George Sternlieb and David Listokin, Building Codes, State Art of the Art, Strategies for the Future, Report submitted to the HUD Housing Review Task Force, June 1973 (processed).

3/ See George Sternlieb et al, The Private Sector's Role In the Provision of Reasonably Priced Housing, Prepared for the San Francisco Federal Home Loan Bank Board, December 11, 1975, p. 22; James G. Coke and Charles S. Liebman, "Political Values and Population Density Control," Land Economics, Vol. 38, November 1961, pp. 347-361; Richard F. Muth and Elliot Wetzler, Effects of Constraints on Single-Unit Housing Costs (Arlington: Institute for Defense Analyses, 1968); Lynn Sagalyn and George Sternlieb, Zoning and Housing Costs: The Impact of Land Use Controls on Housing Prices (New Brunswick: Center for Urban Policy Research, Rutgers University, 1973).

4/ James Carberry, "Red Tape Entangles Big Petroleum Firms In Complying With Federal Regulation," Wall Street Journal, September 3, 1975, p. 30.

5/ William Franklin and Francis Lowell, "Unapproved Drugs in the Practice of Medicine," New England Journal of Medicine, May 15, 1975, pp. 1075-1077.

6/ Sam Peltzman, "An Evaluation of Consumer Protection Legislation: The 1972 Drug Amendments," Journal of Political Economy, September/October 1973, p. 1090; Sam Peltzman, Regulation of Pharmaceutical Innovation (Washington, D. C.: American Enterprise Institute, 1974).

7/ Testimony by Dr. William Wardell, University of Rochester School of Medicine and Dentistry, before the Senate Committee on Labor and Public Welfare, Subcommittee on Health, Washington, D. C., September 27, 1974.

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