PART THREE

Business and Public Policy

CHAPTER SEVEN

Business–Government Relations

Governments seek to protect and promote the public good and in these roles establish rules under which business operates in society. Therefore, a government's influence on business through public policy and regulation is a vital concern for managers. Government's relationship with business can be either cooperative or adversarial. Various economic or social assistance policies significantly affect society, in which businesses must operate. Many government regulations also impact business directly. Managers must understand the objectives and effects of government policy and regulation, both at home and abroad, in order to conduct business in an ethical and legal manner.

This Chapter Focuses on These Key Learning Objectives:

LO 7-1 Understanding why sometimes governments and business collaborate and other times work in opposition to each other.

LO 7-2 Defining public policy and the elements of the public policy process.

LO 7-3 Explaining the reasons for regulation.

LO 7-4 Knowing the major types of government regulation of business.

LO 7-5 Identifying the purpose of antitrust laws and the remedies that may be imposed.

LO 7-6 Comparing the costs and benefits of regulation for business and society.

LO 7-7 Examining the conditions that affect the regulation of business in a global context.

Uber, a U.S.-based international transportation network company founded in 2009, developed a mobile app that allowed consumers to submit a trip request, which was then routed to one of its drivers. By 2015, the service was available in 58 countries and 300 cities worldwide. But Uber encountered serious opposition when it attempted to expand into the European Union. Anti-Uber forces claimed that the firm engaged in unfair competition and its drivers did not have professional licenses, required of all taxicab drivers. Under French law, organizing a system that put paying clients in touch with drivers without professional licenses was punishable by 2 years in prison and a €300,000 ($373,540) fine. Uber's general manager for Western Europe responded, "It's up to the courts to ban Uberpop [the French version of Uber]. If we're prosecuted, then we'll respond." The company also filed complaints with European Union regulators against three European Union governments—France, Germany, and Spain—claiming that these governments had blocked their services.

In 2011, Congress passed legislation to prevent the importation of contaminated food into the United States. About 15 percent of the food that Americans ate originated abroad, more than double the amount 10 years earlier, as did nearly two-thirds of all fresh fruits and vegetables. Recent data reported that one in six Americans became ill annually from eating contaminated food; about 130,000 people were hospitalized and 3000 died each year. In 2013, the Food and Drug Administration imposed even more restrictive rules and challenged food companies to better police imported food. American food importers were required to audit foreign facilities, test foods when arriving in the United States, and review records on foreign suppliers. Most major food importers and consumer advocates praised the new rules, but some worried that they might give companies too much discretion about whether to conduct on-site inspections where the food was grown and processed.[1]

What prompted or compelled governments to become more involved in their citizens' transportation options or the assurance of food safety? How do these government's actions affect businesses and what they are permitted to do? How did these actions affect society and its safety? Did government's involvement promote or harm companies or allow other firms to maintain their competitive advantage? Were these efforts by the governments necessary and effective, or can this only be answered in time?

Governments create the conditions that make it possible for businesses to compete in the modern economy. As shown in the opening examples, governments can act in dramatic ways to provide or limit opportunities for businesses and control business activities to better ensure the public's safety. In good times and bad, government's role is to create and enforce the laws that *balance* the relationship between business and society. Governments also hold the power to grant or refuse permission for many types of business activity. Even the largest multinational companies, which operate in dozens of countries, must obey the laws and public policies of national governments.

This chapter considers the ways in which government actions impact business through the powerful twin mechanisms of public policy and regulation. The next chapter addresses the related question of actions business may take to influence the political process.

How Business and Government Relate

The relationship between business and government is dynamic and complex. Understanding the government's authority and its relationship with business is essential for managers in developing their strategies and achieving their organization's goals.

[1] "France Blocks Uber 'Ride-Sharing' Service," *The Wall Street Journal*, December 15, 2014, *www.wsj.com;* "Uber Files Complaints Against European Governments Over Bans," *The Wall Street Journal*, April 1/, 2015, *www.wsj.com;* and, "F.D.A. Says Importers Must Audit Food Safety," *The New York Times*, July 26, 2013, *www.nytimes.com*. Files Complaints Against European Governments Over Bans," *The Wall Street Journal*, April 1, 2015, *www.wsj.com;* and, "F.D.A. Says Importers Must Audit Food Safety," *The New York Times*, July 26, 2013, *www.nytimes.com*.

Seeking a Collaborative Partnership

In some situations, government may work closely with business to build a collaborative partnership and seek mutually beneficial goals. They see each other as key partners in the relationship and work openly to achieve common objectives.

The basis for this cooperation may be at the core of the nation's societal values and customs. In some Asian countries, society is viewed as a collective family that includes both government and business. Thus, working together as a family leads these two powers to seek results that benefit both society and business. In Europe, the relationship between government and business often has been collaborative. European culture includes a sense of teamwork and mutual aid. Unions, for example, are often included on administrative boards with managers to lead the organization toward mutual goals through interactive strategies. One example of government–business collaboration is shown next.

> The Export-Import Bank (an agency of the U.S. government that helped finance foreign purchases of American goods) was under pressure from its critics to provide tighter rules for aircraft sales. In response, the bank reached out to Boeing Company, the biggest beneficiary of the bank's assistance, to help write the new rules. What followed was an extraordinary level of cooperation between public officials and corporate executives. The bank and company executives exchanged e-mails, drafted new guidelines, and eventually produced a new set of rules for aircraft financing. The cooperation was mutually beneficial. During the two years after the new rules were developed, all Boeing sales were approved, including the sale of 62 wide-body Boeing aircraft to foreign airlines after the bank guaranteed more than $7 billion in loans. The Export-Import Bank also benefited, as the new rules helped it return to sound financial footing. After they went into effect, the bank was able to provide $20.5 billion in financing for U.S. exports and made $675 million in profit.[2]

The collaborative relationship between the Export–Import Bank and Boeing Corporation served both the U.S. government agency and the U.S.-based firm, but raised some question of a competitive bias against other firms, especially non-U.S. aircraft companies like Airbus.

Working in Opposition to Government

In other situations, government's goals and business's objectives are at odds, and these conflicts result in an adversarial relationship where business and government tend to work in opposition to each other.[3]

> A clash between the U.S. government and the coal industry came to a head in 2013. When the government announced new rules to cut greenhouse gas emissions, coal companies feared that a significant number of coal-burning power plants would be forced to shut down, and they would lose customers. The coal industry teamed up with other business groups to challenge President Obama's climate-change agenda. It coordinated lobbying efforts with manufacturers and other business groups to reach out to members of Congress, especially politicians from coal-producing states and those with coal-burning utilities. The plan was to work with sympathetic congressional representatives to modify or delay White House-supported actions that would limit the use of domestic coal and potentially drive up electricity prices.[4]

Why do businesses sometimes welcome government regulation and involvement in the private sector, and other times oppose it? Companies often prefer to operate without government

[2] "Boeing Helped Craft Own Loan Rules," *The Wall Street Journal*, March 12, 2015, *www.wsj.com*.

[3] The "collaborative partnership" and "in opposition" models for business–government relations is discussed in "Managing Regulation in a New Era," *McKinsey Quarterly*, December 2008, *www.mckinseyquarterly.com*.

[4] "Big Coal to Fight Obama Plan," *The Wall Street Journal*, June 26, 2013, *online.wsj.com*.

constraints, which can be costly or restrict innovation. But regulations can also help business, by setting minimum standards that all firms must meet, building public confidence in the safety of a product, creating a fair playing field for competition, or creating barriers to entry to maintain a business's competitive advantage. How a specific company reacts to a specific government policy often depends on their assessment of whether they would be helped or hurt by that rule.

In short, the relationship between government and business can range from one of cooperation to one of conflict, with various stages in between. Moreover, this relationship is constantly changing. A cooperative relationship on one issue does not guarantee cooperation on another issue. The stability of a particular form of government in some countries may be quite shaky, while in other countries the form of government is static but those in power can change unexpectedly or government rulers can change on a regular basis. The business–government relationship is one that requires managers to keep a careful eye trained toward significant forces that might alter this relationship or to promote forces that may encourage a positive business–government relationship.[5]

Legitimacy Issues

When dealing with a global economy, business may encounter governments whose authority or right to be in power is questioned. Political leaders may illegally assume lawmaking or legislative power, which can become economic power over business. Elections can be rigged, or military force can be used to acquire governmental control.

Business managers may be challenged with the dilemma of doing business in such a country where their business dealings would support this illegitimate power. Sometimes, they may choose to become politically active, or refuse to do business in this country until a legitimate government is installed.

Businesses can also influence the ability of a government leader or group of leaders to maintain political power. For example, companies can decide to withdraw operations from a country, as many U.S. firms did from South Africa in the 1970s to protest the practice of apartheid (institutionalized racial segregation). Some believe that the economic isolation of South Africa contributed to the eventual collapse of the apartheid regime. Governments may also order companies not to conduct business in another country because of a war, human rights violations, or lack of a legitimate government. These orders are called *economic sanctions.* As of 2015, the United States had imposed economic sanctions on Iraq, Kuwait, Lebanon, Libya, Qatar, Saudi Arabia, Syria, the United Arab Emirates, and Yemen because of political and human rights concerns.[6]

Government's Public Policy Role

Government performs a vital and important role in modern society. Although vigorous debates occur about the proper size of programs government should undertake, most people agree that a society cannot function properly without some government activities. Citizens look to government to meet important basic needs. Foremost among these are safety and protection provided by homeland security, police, and fire departments. These are collective or public goods, which are most efficiently provided by government for everyone in a community. In today's world, governments are also expected to provide economic security and essential social services, and to deal with the most pressing social problems that require collective action, or public policy.

Public policy is a plan of action undertaken by government officials to achieve some broad purpose affecting a substantial segment of a nation's citizens. Or as the late U.S.

[5] See George Lodge, *Comparative Business–Government Relations* (Englewood Cliffs, NJ: Prentice Hall, 1990).

[6] See The Federal Registry, Department of the Treasury at *www.gpo.gov.*

Senator Patrick Moynihan said, "Public policy is what a government chooses to do or not to do." In general, these ideas are consistent. Public policy, while differing in each nation, is the basic set of goals, plans, and actions that each national government follows in achieving its purposes. Governments generally do not choose to act unless a substantial segment of the public is affected and some public purpose is to be achieved. This is the essence of the concept of governments acting in the public interest.

The basic power to make public policy comes from a nation's political system. In democratic societies, citizens elect political leaders who can appoint others to fulfill defined public functions ranging from municipal services (e.g., water supplies, fire protection) to national services, such as public education or homeland security. Democratic nations typically spell out the powers of government in the country's constitution.

Another source of authority is *common law,* or past decisions of the courts, the original basis of the U.S. legal system. In nondemocratic societies, the power of government may derive from a monarchy (e.g., Saudi Arabia), a military dictatorship (e.g., Eritrea or Zimbabwe), or religious authority (e.g., the mullahs in Iran). These sources of power may interact, creating a mixture of civilian and military authority. The political systems in Russia, Libya, Tunisia, and other nations have undergone profound changes in recent times. And democratic nations can also face the pressures of regions that seek to become independent nations exercising the powers of a sovereign state, as does Canada with Quebec.

Elements of Public Policy

The actions of government in any nation can be understood in terms of several basic elements of public policy. These are inputs, goals, tools, and effects. They will be illustrated using the example of distracted driving.

Public policy inputs are external pressures that shape a government's policy decisions and strategies to address problems. Economic and foreign policy concerns, domestic political pressure from constituents and interest groups, technical information, and media attention all play a role in shaping national political decisions. For example, a growing recognition of the dangers of distracted driving has pressured many state and local governments to ban or regulate the use of various electronic devices by drivers. Distracted driving may occur when a driver's attention is diverted by personal grooming tasks, adjusting music or navigation settings, eating, reading, and assorted other activities. It has become an even greater threat to driver and passenger safety as technological advances occur at a rapid pace. More and more drivers are now able to make or receive calls, send text messages, and even browse the Internet—all while driving a car at high speeds, in heavy traffic, or during bad weather conditions.[7]

> According to an annual National Highway Traffic Safety Administration study, more than 3,000 people are killed and nearly a half million injured in distraction-related crashes. A 2014 Insurance Institute for Highway Safety study found that the risk of a crash was 17 percent higher when the driver was distracted by using a cell phone. Teens were particularly vulnerable. Nearly six out of 10 crashes involved teen drivers who were distracted immediately before the accident. In a survey sponsored by Erie Insurance, 30 percent all of drivers admitted to texting while driving and 75 percent reported that they had seen someone else do it—causing researchers to believe that the percentage of texting while driving was much higher than 30 percent. Fifteen percent of drivers admitted they had engaged in "romantic encounters" while behind the wheel and 9 percent said they had changed clothes while driving.[8]

[7] "Windshield Devices Bring Distracted Driving Debate to Eye Level," *The New York Times,* May 29, 2015, *www.nytimes.com.*

[8] "Study Asks Just How Distracted Are Motorists?" *Pittsburgh Post-Gazette,* March 30, 2015, *www.post-gazette.com.* For updated information on distracted driving, see *www.distraction.gov* and the *Insurance Institute for Highway Safety's* website at *www.iihs.org.*

The harms associated with distracted driving are alarming. A spokesperson for a major auto insurance company explained, "Distracted driving is becoming a national epidemic and it has to be controlled."[9]

Government bodies—legislatures, town councils, regulatory agencies—need to consider all relevant inputs in deciding whether or not to take action, and if so, what kind of action.

Public policy goals can be broad (e.g., full employment) and high-minded (equal opportunity for all) or narrow and self-serving. National values, such as freedom, democracy, and a fair chance for all citizens to share in economic prosperity, have led to the adoption of civil rights laws and economic assistance programs for those in need. Narrow goals that serve special interests are more apparent when nations decide how tax legislation will allocate the burden of taxes among various interests and income groups, or when public resources, such as oil exploration rights or timber cutting privileges, are given to one group or another. Whether the goals are broad or narrow, for the benefit of some or the benefit of all, most governments should ask, "What public goals are being served by this action?" For example, the rationale for a government policy to regulate distracted driving has to be based on some definition of public interest, such as preventing harm to others, including innocent drivers, passengers, and pedestrians.

> The goal of distracted driving regulation is to prevent deaths and serious injuries resulting from drivers being distracted while driving. However, some members of the public have insisted on their right to use their phones for texting and other activities in their vehicles. Traveling salespersons, for example, depend on their phones as an important tool of the job. Some regulations have addressed this by permitting drivers to use hands-free devices that permit them to keep their hands on the wheel. But some government safety experts have disagreed, saying, "When you are on a call, even if both hands are on the wheel, your head is in the call, and not your driving."

The issue of banning the use of cell phones, hand-held or hands-free, for the sake of making our roads a little safer for all, remains at the forefront, but new technology has created even greater distractions. Devices can project information and data streamed from a smartphone onto the car's windshield. Maps, speed, incoming texts, caller identification, and even social media notifications can be projected just above the dashboard of a car for the driver to read. So, the goals of saving lives, reducing injuries, and eliminating health care costs are increasingly more urgent and the demand for regulation even more critical.

Governments use different *public policy tools* to achieve policy goals. The tools of public policy involve combinations of incentives and penalties that government uses to prompt citizens, including businesses, to act in ways that achieve policy goals. Governmental regulatory powers are broad and constitute one of the most formidable instruments for accomplishing public purposes.

> Federal action limiting cell phone use in the United States stalled, so state and local governments stepped in to ban the use of cell phones by drivers while operating their vehicles. By 2015 14 states had completely banned the use of cell phones while driving without a hands-free device, 37 had banned cell phone use by novice drivers, and 20 had banned school bus drivers from using their cell phones. Forty-six states banned text messaging for all drivers. And this is not just

9 "Texting While Driving Dangerous, Study Confirms: How Dangerous?" *CBS News - Health Pop*, October 6, 2011, *www .cbsnews.com*.

a public policy issue for Americans. More than 45 nations, including Australia, China, France, Germany, India, Israel, Japan, Russia, Spain, Taiwan, and the United Kingdom, ban calling while driving.[10]

Public policy effects are the outcomes arising from government regulation. Some are intended; others are unintended. Because public policies affect many people, organizations, and other interests, it is almost inevitable that such actions will please some and displease others. Regulations may cause businesses to improve the way toxic substances are used in the workplace, thus reducing health risks to employees. Yet other goals may be obstructed as an unintended effect of compliance with such regulations. For example, when health risks to pregnant women were associated with exposure to lead in the workplace, some companies removed women from those jobs. This action was seen as a form of discrimination against women that conflicted with the goal of equal employment opportunity. The unintended effect (discrimination) of one policy action (protecting employees) conflicted head-on with the public policy goal of equal opportunity.

Different groups disagreed over the possible effects of distracted driving laws. Proponents obviously argued that the ban on cell phone use reduced accidents and saved lives. In fact, from 2012 to 2013, the number of deaths attributed to distracted driving nationwide declined nearly 7 percent, possibly due to the bans enacted by many states. Opponents pointed to numerous other distractions that were not banned, such as drivers reading the newspaper, eating, putting on makeup, or shaving. "People have been driving distracted since cars were invented. Focusing on mobile phones isn't the same as focusing on distracted driving. Distraction is what has always caused car crashes and mobile phones don't appear to be adding to that," said a spokesperson for the Insurance Institute for Highway Safety.[11]

As the distracted driving examples illustrate, managers must try to be aware of the public policy inputs, goals, tools, and effects relevant to regulation affecting their business.

Types of Public Policy

Public policies created by governments are of two major types: economic and social. Sometimes these types of regulation are distinct from each another and at other times they are intertwined.

Economic Policies

One important kind of public policy directly concerns the economy. The term **fiscal policy** refers to patterns of government collecting and spending funds that are intended to stimulate or support the economy. Governments spend money on many different activities. Local governments employ teachers, trash collectors, police, and firefighters. State governments typically spend large amounts of money on roads, social services, and parkland. National governments spend large sums on military defense, international relationships, and hundreds of public works projects such as road building. During the Great Depression of the 1930s, public works projects employed large numbers of people, put money in their hands,

[10] For a complete listing of states that have regulated cell phone use while driving see the *Governor's Highway Safety Association* at *www.ghsa.org*.

[11] Statistical information from the *Governor's Highway Safety Association* website at *www.ghsa.org;* and "Study: No Evidence Cell Phone Bans Reduce Crashes," *Fox News*, July 7, 2011, *www.foxnews.com*.

and stimulated consumption of goods and services. Today, fiscal policy remains a basic tool to achieve prosperity, as the following example illustrates.

> In 2015, Chinese government leaders and economists were surprised by the country's sharp economic decline and were increasingly worried about the potential risk of job losses throughout the country. The world's second largest economy grew at 7 percent in the first quarter of 2015, the lowest rate since the global financial crisis in 2008–9. The leaders turned to fiscal stimulus to revive the growth of the country. The National Development and Reform Commission, China's top planning agency, infused large amounts of funding in an attempt to speed up investment projects in several key sectors, including water conservation, environmental protection, power grids, and health care. A chief economist explained, "It's hard to boost consumption while external demand is weak, so the only thing they can do is boost investment."[12]

By contrast, the term **monetary policy** refers to policies that affect the supply, demand, and value of a nation's currency. The worth, or worthlessness, of a nation's currency has serious effects on business and society. It affects the buying power of money, the stability and value of savings, and the confidence of citizens and investors about the nation's future. This, in turn, affects the country's ability to borrow money from other nations and to attract private capital. In the United States, the Federal Reserve Bank—known as the Fed—plays the role of other nations' central banks. By raising and lowering the interest rates at which private banks borrow money from the government, the Fed influences the size of the nation's money supply and the value of the dollar. During the Great Recession, the Fed's action to lower interest rates nearly to zero—an example of a monetary policy—was intended to stimulate borrowing and help the economy get moving again.

Other forms of economic policy include *taxation policy* (raising or lowering taxes on business or individuals), *industrial policy* (directing economic resources toward the development of specific industries), and *trade policy* (encouraging or discouraging trade with other countries).

Social Assistance Policies

The last century produced many advances in the well-being of people across the globe. The advanced industrial nations have developed elaborate systems of social services for their citizens. Developing economies have improved key areas of social assistance (such as health care and education) and will continue to do so as their economies grow. International standards and best practices have supported these trends. Many of the **social assistance policies** that affect particular stakeholders are discussed in subsequent chapters of this book.

> One area often addressed by social assistance policies is housing. Many governments have programs that subsidize rent payments, guarantee home loans, or provide housing directly for low-income citizens or military veterans. For example, Brazil's *Minha Casa, Minha Vida* ("My House, My Life") program has built one million homes since 2009 for low-income families. Mortgages are provided by a government-affiliated bank and more than $1 trillion in investments had been channeled into this program by 2014. Many of the first units built by the program were intended to house families displaced by development for the World Cup and Olympic Games in Rio de Janeiro.[13]

[12] "China Looks to Fiscal Stimulus to Fight Slowdown," *Business Times*, May 7, 2015, *www.businesstimes.com.sg*.

[13] For more information on this program see *myhousemylifebrazil.com*.

One particularly important social assistance policy—health care—has been the focus for concern on the international front and for national and state lawmakers. As discussed later in this chapter, the United States government has wrestled with the need for better health care for its citizens and the challenge of how to pay for this care.

Government Regulation of Business

Societies rely on government to establish rules of conduct for citizens and organizations called *regulations*. **Regulation** is a primary way of accomplishing public policy, as described in the previous section. Because government operates at so many levels (federal, state, local), modern businesses face complex webs of regulations. Companies often require lawyers, public affairs specialists, and experts to monitor and manage the interaction with government. Why do societies turn to more regulation as a way to solve problems? Why not just let the free market allocate resources, set prices, and constrain socially irresponsible behavior by companies? There are a variety of reasons.

Market Failure

One reason is what economists call **market failure**, that is, the marketplace fails to adjust prices for the true costs of a firm's behavior. For example, a company normally has no incentive to spend money on pollution control equipment if customers do not demand it. The market fails to incorporate the cost of environmental harm into the business's economic equation, because the costs are borne by someone else. In this situation, government can use regulation to force all competitors in the industry to adopt a minimum antipollution standard. The companies will then incorporate the extra cost of compliance into the product price. Companies that want to act responsibly often welcome carefully crafted regulations, because they force competitors to bear the same costs.

> The issue of global warming, caused in part by greenhouse gas emissions, is such a big issue that no single firm or industry can afford to take the first step and try to control it in order to minimize the harm to our planet and environment. World leaders have met periodically since 1995—most recently in 2015—under the auspices of the United Nations to negotiate and update a convention (treaty) to limit countries' greenhouse gas emissions. Many hope that this international agreement will create a path for businesses to follow to improve the health of our planet. While people may disagree on how to accomplish this important goal (as the earlier example of the coal industry's opposition to regulation illustrates), the challenge is beyond what the marketplace can tackle and it requires some form of government intervention by many countries.

Negative Externalities

Governments also may act to regulate business to prevent unintended adverse effects on others. **Negative externalities**, or spillover effects, result when the manufacture or distribution of a product gives rise to unplanned or unintended costs (economic, physical, or psychological) borne by workers, consumers, competitors, neighboring communities, or other business stakeholders. To control or reverse these costs, government may step in to regulate business action.

> In 2014 U.S. government regulators announced new rules to fight an increase in black lung disease, caused by breathing coal dust. These new regulations were the first major efforts since the 1969 Coal Mine Health and Safety Act, which

established modern health and safety requirements in mines nationwide. Government health officials attributed increasing rates of the disease to new machinery that generated more dust, longer shifts for younger workers, and an increase in silica dust churned up when thinner coal seams were tapped after many years of mining at the same location.[14]

Natural Monopolies

In some industries, **natural monopolies** occur. The electric utility industry provides an example. Once one company has built a system of poles and wires or laid miles of underground cable to supply local customers with electricity, it would be inefficient for a second company to build another system alongside the first. But once the first company has established its natural monopoly, it can then raise prices as much as it wishes because there is no competition. In such a situation, government often comes in and regulates prices and access. Other industries that sometimes develop natural monopolies include cable TV, broadband Internet service, software, and railroads.

Ethical Arguments

There is often an ethical rationale for regulation as well. As discussed in Chapter 5, for example, there is a utilitarian ethical argument in support of safe working conditions: It is costly to train and educate employees only to lose their services because of preventable accidents. There are also fairness and justice arguments for government to set standards and develop regulations to protect employees, consumers, and other stakeholders. In debates about regulation, advocates for and against regulatory proposals often use both economic and ethical arguments to support their views. Sometimes firms will agree to self-regulate their actions to head off more costly government-imposed regulatory reform, as shown in the following example.

> The National Highway Traffic Safety Administration (NHTSA) decided to launch an investigation after two Tesla Motors cars hit debris on the road, leading to a battery fire in 2013. The first incident occurred when the car struck a metal object on the highway; the second one, when the car hit a tow hitch lying on the road. Immediately after the NHTSA's announcement, Tesla Motors announced that it was conducting its own investigation and would implement certain safety measures aimed at creating more ground clearance in their cars and would extend its warranty policy to cover vehicles damaged by fire.[15]

Whether the actions are self-imposed by a company or forced on businesses by the government, the protection of the public is often the motivation for regulatory action.

Types of Regulation

Government regulations come in different forms. Some are directly imposed; others are more indirect. Some are aimed at a specific industry (e.g., banking); others, such as those dealing with job discrimination or pollution, apply to all industries. Some have been in existence for a long time—for example, the Food and Drug Act was passed in 1906—whereas others, such as the Wall Street Reform and Consumer Protection (or Dodd-Frank) Act of 2010, are of much more recent vintage. Just as public policy can be classified as either economic or social, so regulations can be classified in the same fashion.

[14] "Black Lung Disease Spurs New Coal-Mine Rules," *The Wall Street Journal*, April 23, 2014, *online.wsj.com*.

[15] "U.S. Safety Agency Opens Inquiry into Tesla Fires," *The New York Times*, November 19, 2013, *www.nytimes.com*.

Economic Regulations

The oldest form of regulation is primarily economic in nature. **Economic regulations** aim to modify the normal operation of the free market and the forces of supply and demand. Such modification may come about because the free market is distorted by the size or monopoly power of companies, or because the consequences of actions in the marketplace are thought to be undesirable. Economic regulations include those that control prices or wages, allocate public resources, establish service territories, set the number of participants, and ration resources. The decisions by the Federal Trade Commission (FTC) to prevent anticompetitive business practices illustrate one kind of economic regulation. The U.S. Congress responded to the global recession, in part, by passing the **Dodd-Frank Act**, as discussed next.

> The passage of the Dodd-Frank Act in 2011, heralded as the most comprehensive financial regulatory reform measure since the Great Depression, revolutionized many business activities. Among other things, the Dodd-Frank Act affected the oversight and supervision of financial institutions, provided for a new resolution procedure for large financial companies, created a new agency responsible for implementing and enforcing compliance with consumer financial laws, introduced more stringent regulatory capital requirements, effected significant changes in the regulation of over-the-counter derivatives, reformed the regulation of credit rating agencies, implemented changes to corporate governance and executive compensation practices, required registration of advisers to certain private funds, and effected significant changes in the securities markets.[16]

Yet, some businesses generally resisted many of the changes intended by the Dodd-Frank Act and fought back, as discussed in Exhibit 7.A. These efforts caused many to wonder if the Dodd-Frank Act had failed or was much weaker than lawmakers had intended.

Antitrust: A Special Kind of Economic Regulation

One important kind of economic regulation occurs when government acts to preserve competition in the marketplace, thereby protecting consumers. **Antitrust laws** prohibit unfair, anticompetitive practices by business. (The term *antitrust law* is used in the United States; most other countries use the term *competition law*.) For example, if a group of companies agreed among themselves to set prices at a particular level, this would generally be an antitrust violation. In addition, a firm may not engage in **predatory pricing**, the practice of selling below cost to drive rivals out of business. If a company uses its market dominance to restrain commerce, compete unfairly, or hurt consumers, then it may be found guilty of violating antitrust laws.

> For example, in 2015 a federal appeals court upheld a decision that found Apple liable for conspiring with book publishers to raise the price of e-books. The conspiracy, concluded the judge, had unreasonably restrained trade in violation of federal antitrust law. Apple's actions were in response to Amazon's aggressive discounts for e-books and its growing command of the e-book market. Apple entered into an industrywide agreement with five major book publishers to switch to a different pricing model that allowed the publishers rather than retailers to set e-book prices and e-book price began to rise. After the court decision, Apple was expected to have to pay $450 million, mostly to e-book consumers.[17]

[16] "The Dodd-Frank Act: A Cheat Sheet," Morrison & Foerster, n.d., *www.mofo.com*. Also see Kelly Richmond Pope and Chin-Chen Lee, "Could the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 be Helpful in Reforming Corporate America?" *Journal of Business Ethics*, February 2014, pp. 597–607.

[17] "Apple Loses Federal Appeal in E-Books Case," *The Wall Street Journal*, June 30, 2015, *www.wsj.com*.

Exhibit 7.A

Business Pushes Back on the Dodd-Frank Act

Three years after the Dodd-Frank Act was passed, only 40 percent of the regulations had been written. President Obama, an advocate of the act, wanted to know why, so he called in those responsible for writing the act's regulations. Nine different agencies were summoned, reflecting one of the major problems with the act—too many agencies were involved. The U.S. Treasury, the Federal Reserve Board, the Office of the Comptroller of the Currency, the Consumer Financial Protection Bureau, the Federal Housing Finance Agency, the Commodity Futures Trading Commission, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Securities and Exchange Commission all had oversight of parts of the law.

In addition, businesses launched a political attack targeting these agencies and Congress. By 2012, more than 3000 lobbyists swarmed Capitol Hill, nearly six for every member of Congress, to influence or delay the full impact of the Dodd-Frank Act. The financial services industry spent more than $1 billion targeting the weakening of the Dodd-Frank Act. As one consumer advocate pointed out, "The lobbyists are just the point of the spear. There are also the regulatory lawyers, the research staffs, the public relations people and all those loyal think tank supporters shilling for the banks."

From 2013 to 2015, Congress voted to roll back major elements of the Dodd-Frank Act, such as repealing the requirement that big banks "push out" some derivatives trading into separate units that are not backed by the government's insurance funds, delaying by two years the mandate that financial firms sell off bundled debt, exempting some private equity firms from registering with the SEC, and allowing some small, publicly traded companies to omit historical financial data from their financial filings.

Sources: "The Red Tape That's Choking Financial Reform," *Bloomberg Businessweek*, August 26–September 1, 2013, p. 14; "How Wall Street Defanged Dodd-Frank," *The Nation*, April 30, 2013, *www.thenation.com*; "House Votes to Repeal Dodd-Frank Provision," *The New York Times*, October 30, 2013, *dealbook.nytimes.com*; and, "House Passes Measure to Ease Some Dodd-Frank Rules," *The New York Times*, January 14, 2015, *www.nytimes.com*.

The two main antitrust enforcement agencies are the Antitrust Division of the U.S. Department of Justice and the Federal Trade Commission. Both agencies may bring suits against companies they believe to be guilty of violating antitrust laws. They also may investigate possible violations, issue guidelines and advisory opinions for firms planning mergers or acquisitions, identify specific practices considered to be illegal, and negotiate informal settlements out of court. Antitrust regulators have been active in prosecuting price fixing, blocking anticompetitive mergers, and dealing with foreign companies that have violated U.S. laws on fair competition. In Europe, the European Commission enforces antitrust regulation, as seen in the Microsoft example that follows.

> In 2013 Microsoft was fined €561 million ($732.2 million) by the European Commission (EC) after it broke its voluntary promise to offer more than 15 million Windows users a choice of rival web browsers. The fine was the latest altercation between the EC and Microsoft. A decade earlier, the EC fined Microsoft €1.6 billion ($2.08 billion) for failing to provide rivals with information at fair prices and for tying its media player to its operating system. According to EC's competition chief, "such a breach is of course very serious, irrespective of whether it was intentional or not and it calls for sanctions. I hope this decision makes companies think twice before they ever think of internationally breaching their obligations or even neglecting their duty to ensure strict compliance."[18]

If a company is found guilty of antitrust violations, what are the penalties? The government may levy a fine—sometimes a large one, as the EC did against Microsoft. In another example, Berkshire Hathaway agreed to pay $896,000 to settle U.S. allegations that the

[18] "EU Fines Microsoft $732 Million," *The Wall Street Journal*, March 6, 2013, *online.wsj.com*.

firm violated antitrust laws by failing to report the acquisition of an equity stake in USG Corporation, a gypsum wallboard-maker based in Chicago. "We made a mistake when we overlooked the filing requirement," explained Berkshire's chief executive, Warren Buffet.[19] In the case of private lawsuits, companies may also be required to pay damages to firms or individuals they have harmed. In addition, regulators may impose other, nonmonetary remedies. A *structural remedy* may require the breakup of a monopolistic firm; this occurred when AT&T was broken up by government order in 1984. A *conduct remedy*, more commonly used, involves an agreement that the offending firm will change its conduct, often under government supervision. For example, a company might agree to stop certain anticompetitive practices. Finally, an *intellectual property remedy* is used in some kinds of high-technology businesses; it involves disclosure of information to competitors. All these are part of the regulator's arsenal.

Antitrust regulations cut across industry lines and apply generally to all enterprises. Other economic regulations, such as those governing stock exchanges, may be confined to specific industries and companies.

Social Regulations

Social regulations are aimed at such important social goals as protecting consumers and the environment and providing workers with safe and healthy working conditions. Equal employment opportunity, protection of pension benefits, and health care for citizens are other important areas of social regulation. Unlike the economic regulations mentioned above, social regulations are not limited to one type of business or industry. Laws concerning pollution, safety and health, health care, and job discrimination apply to all businesses; consumer protection laws apply to all relevant businesses producing and selling consumer goods.

An example of a social regulation is federal rules for automobile and truck emissions and mileage standards. Beginning in 2011, the federal government rolled out new standards to be applied to automobiles made between 2011 and 2025. By 2025, all new cars and trucks sold in the United States must have a performance equivalency of 54.5 miles per gallon while reducing greenhouse emission gases to 163 grams per mile. These new requirements could save families an estimated $8,200 in fuel costs over the lifetime of the vehicle, relative to a 2010 standard. In 2015, new standards were proposed to improve fuel efficiency and cut carbon pollution for trucks. The new standards were expected to lower CO^2 emissions by approximately 1 billion metric tons, cut fuel costs by about $170 billion, and reduce oil consumption by up to 1.8 billion barrels over the lifetime of the vehicle. In addition to cost-savings and environmental benefits, this social regulation also would help the country achieve its goal of less dependence on foreign oil.[20]

The most significant social regulation in the United States since the 1960s was the comprehensive reform of health care coverage passed by Congress in 2009. It is described in Exhibit 7.B.

Who regulates? Normally, for both economic and social regulation, specific rules are set by agencies of government and by the executive branch, and may be further interpreted by the courts. Many kinds of business behavior are also regulated at the state level.

[19] "Warren Buffet's Berkshire Hathaway to Pay $896,000 Civil Penalty on Antitrust Issue," *The Wall Street Journal*, August 20, 2014, *online.wsj.com*.

[20] "President Obama Announced New Fuel Economy Standards," *The White House Blog*, July 29, 2011, *www.whitehouse.gov/blog*; and, "EPA and DOT Propose Greenhouse Gas and Fuel Efficiency Standards for Heavy-duty Trucks," *National Highway and Traffic Safety Administration*, June 19, 2015, *www.nhtsa.gov*.

Exhibit 7.B The Affordable Care Act: Health Care Coverage Mandated for Americans

In 2010, led by President Obama, Congress passed the Affordable Care Act, often referred to as "Obamacare." The basic purpose of the law was to hold insurance companies accountable for their costs and services to their customers, lower the rising health care costs, provide Americans with greater freedom and control over their health care choices, and ultimately improve the quality of health care in America. Its provisions would be rolled out over 10 years. In 2010, the government began giving subsidies to small businesses that offered health coverage to employees, insurance companies were barred from denying coverage to children with preexisting illnesses, and children were permitted to stay on their parents' insurance policies until age 26.

The health care reform law aroused strong passions on both sides. Proponents of the law argued that the more than 5.1 million people on Medicare would save over $3 billion in prescription drugs costs, 105 million Americans would no longer have lifetime dollar limits on their health care coverage, and approximately 54 million Americans would receive greater preventative medical coverage. Health care fraud would decline by $4.1 billion annually due to new fraud detection measures, and 2.5 million young adults would retain health care coverage under their parents' plan. Most importantly, most Americans would now have health insurance coverage.

But, opponents challenged the new law as filled with myths, untruths, and harmful consequences. Some believed that the act would do nothing to bring down the cost of health care. Business leaders worried that the burden of providing their employees with health care insurance would result in bankruptcy or cause employers to reduce the level of health care coverage for their employees. Many worried that the mandate infringed on individual rights—including the right to go without health insurance if they chose. Several states sued, saying the law violated the constitution.

By 2015, nearly 11.7 million Americans had selected marketplace plans or been automatically enrolled under the act. Twenty-eight states and the District of Columbia had expanded their Medicaid coverage, with more than 10 million more Americans enrolled in Medicaid or the Children's Health Insurance Program. Under the act, millions more Americans received preventive services, such as vaccines, cancer screenings, and annual wellness visits at no out-of-pocket cost, than ever before. In addition, Americans could no longer be denied or dropped from coverage because of pre-existing conditions or because they hit an annual or lifetime cap in benefits.

Sources: "What's in the Bill," *The Wall Street Journal*, March 22, 2010, *online.wsj.com*; "Get the Facts Straight on Health Reform—A More Secure Future," *The White House*, n.d., *www.whitehouse.gov*; and "The Affordable Care Act Is Working," *Department of Health and Human Services*, *www.hhs.gov*.

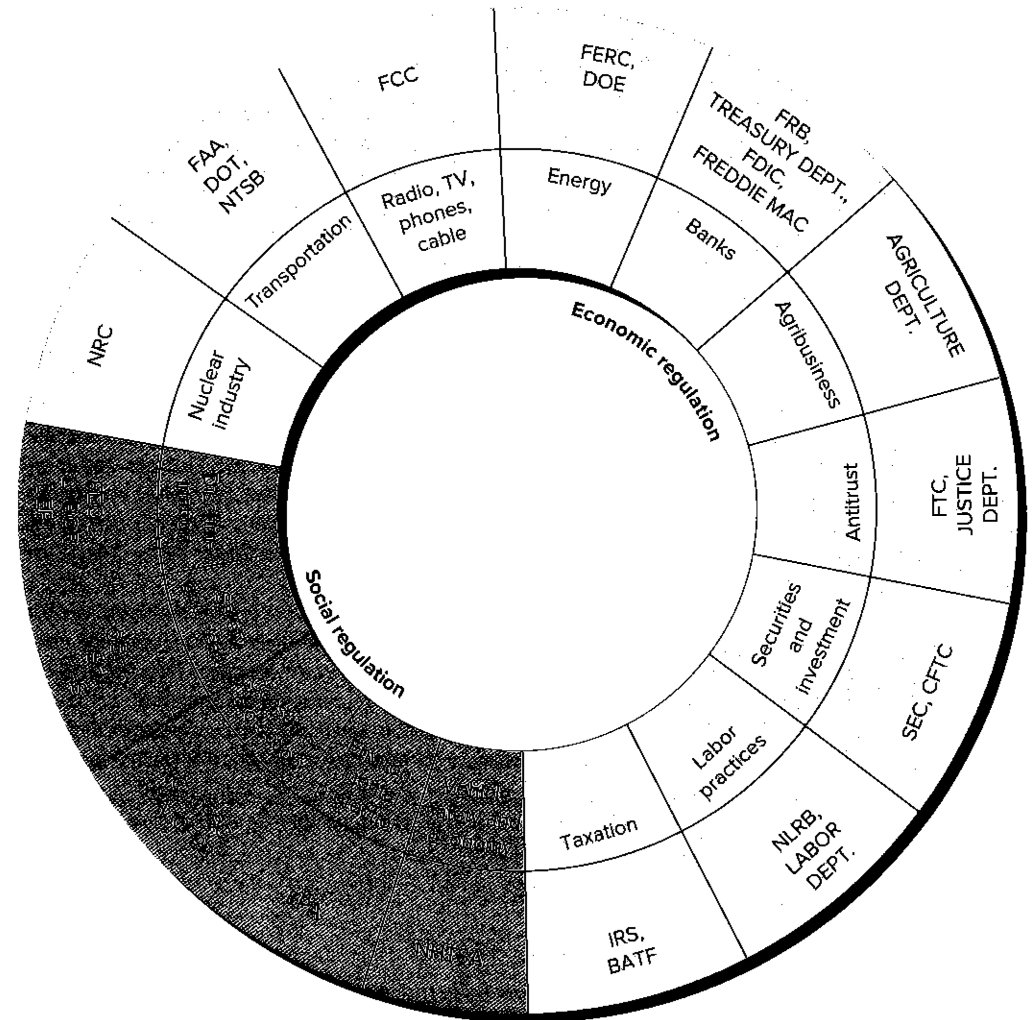
Government regulators and the courts have the challenging job of applying the broad mandates of public policy.

Figure 7.1 depicts these two types of regulation—economic and social—along with the major regulatory agencies responsible for enforcing the rules at the federal level in the United States. Only the most prominent federal agencies are included in the chart. Individual states, some cities, and other national governments have their own array of agencies to implement regulatory policy. There is a legitimate need for government regulation in modern economies, but regulation also has problems. Businesses feel these problems firsthand, often because the regulations directly affect the cost of products and the freedom of managers to design their business operations. In the modern economy, the costs and effectiveness of regulation, as well as its unintended consequences, are serious issues that cannot be overlooked. Each is discussed below.

The Effects of Regulation

Regulation affects many societal stakeholders, including business. Sometimes the consequences are known and intended, but at other times unintended or accidental consequences emerge from regulatory actions. In general, government hopes that the benefits arising from regulation outweigh the costs.

FIGURE 7.1 Types of Regulation and Regulatory Agencies



Economic regulatory agencies

NRC	Nuclear Regulatory Commission	FTC	Federal Trade Commission
FAA	Federal Aviation Administration	SEC	Securities and Exchange Commission
FCC	Federal Communications Commission	NLRB	National Labor Relations Board
FERC	Federal Energy Regulatory Commission	IRS	Internal Revenue Service
FRB	Federal Reserve Board	BATF	Bureau of Alcohol, Tobacco, Firearms and Explosives
CFTC	Commodity Futures Trading Commission	FDIC	Federal Deposit Insurance Corporation
FREDDIE MAC	Federal Home Loan Mortgage Corporation	DOE	Department of Energy
DOT	Department of Transportation	NTSB	National Transportation Safety Board

Social regulatory agencies

EEOC	Equal Employment Opportunity Commission	CPSC	Consumer Product Safety Commission
OSHA	Occupational Safety and Health Administration	FDA	Food and Drug Administration
MSHA	Mine Safety and Health Administration	EPA	Environmental Protection Agency
FTC	Federal Trade Commission	NHTSA	National Highway Traffic Safety Administration
HHS	Department of Health and Human Services	CFPB	Consumer Financial Protection Bureau

The Costs and Benefits of Regulation

The call for regulation may seem irresistible to government leaders and officials given the benefits they seek, but there are always costs to regulation. An old economic adage says, "There is no free lunch." Eventually, someone has to pay for the benefits created.

An industrial society such as the United States can afford almost anything, including social regulations, if it is willing to pay the price. Sometimes the benefits are worth the costs; sometimes the costs exceed the benefits. The test of **cost–benefit analysis** helps the public understand what is at stake when new regulation is sought.

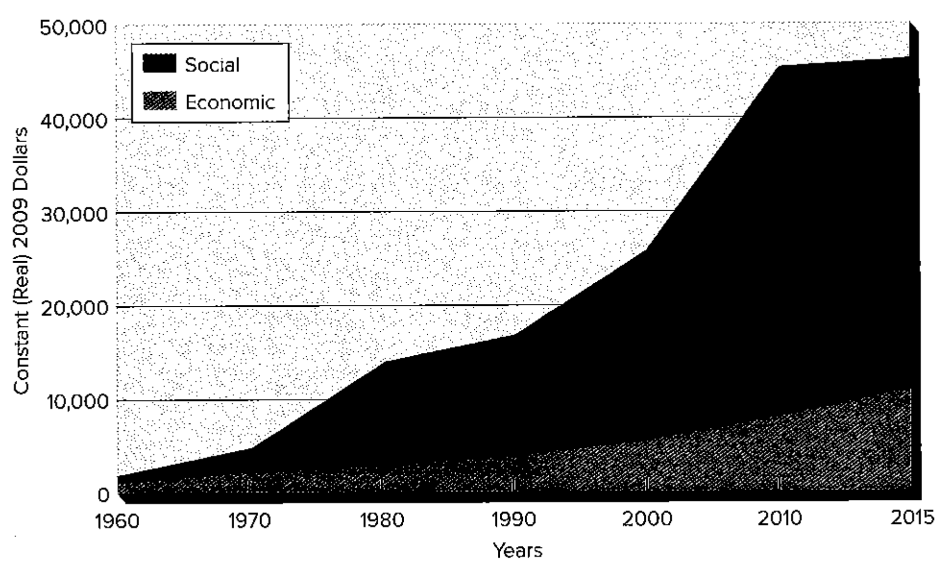
Figure 7.2 illustrates the increase in costs of federal regulation in the United States since 1960. Economic regulation has existed for many decades, and its cost has grown more slowly than that of social regulation. Social regulation spending reflects growth in such areas as environmental health, occupational safety, and consumer protection. A rapid growth of social regulation spending occurred in the 1960s and again in the 2000s, but has slowed somewhat recently. The cost of regulation has its critics, especially when the costs to small businesses or manufacturing firms are considered.

> Economists Nicole Crain and Mark Crain reported that complying with federal regulations cost U.S. businesses more than $2 trillion each year. Compliance costs were highest for regulations focusing on the environment and worker safety and fell disproportionately on manufacturers and small businesses. The average manufacturing company paid compliance costs of nearly $20,000 per employee annually, nearly double the average cost paid by all U.S. businesses. "There's no question it's harming our country's economic growth," said the National Association for Manufacturers' president. "This is hidden tax. It's a cost to the economy."[21]

But other economists pointed out that the Crain study, commissioned by the National Association of Manufactures, was flawed since it relied on the opinions of business executives who had a vested interest in overestimating regulatory costs. They also argued that the researchers failed to measure the benefits that regulations provided the country. Some

FIGURE 7.2
Spending on U.S. Regulatory Activities

Source: Susan Dudley and Melinda Warren, "Regulators' Budget Increases Consistent with Growth in Fiscal Budget," Regulatory Studies Center, The George Washington University and Weidenbaum Center, Washington University in Saint Louis, May 2015, *regulatorystudies.columbian.gwu.edu.*



[21] "New Study Places $2T Yearly Price Tag on Federal Regulation," *Pittsburgh Post-Gazette*, September 11, 2014, *www.post-gazette.com.*

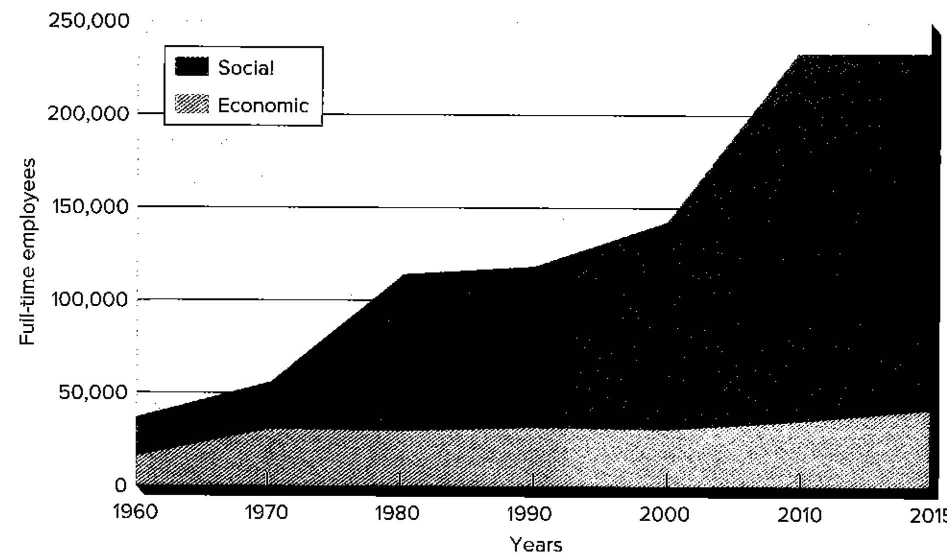
felt that the high cost of regulation on business was worth it since the stakes were so high. Controlling environmental pollution and protecting worker and consumer safety, for example, benefits many citizens. How do the costs and benefits of regulation compare? The federal government's Office of Budget and Management reported that the annual benefits of major federal regulations from 2003 to 2013 ranged somewhere from $217 billion to $863 billion, while the estimated annual costs ranged from $57 billion to $84 billion. Although different methodologies produced different estimates, in all scenarios the benefits exceeded the costs.[22]

In addition to paying for regulatory programs, it takes people to administer, monitor, and enforce these regulations. Researchers at two academic research centers have documented staffing regulatory activities in the United States since 1960, as shown in Figure 7.3. In 1960, fewer than 60,000 federal employees monitored and enforced government regulations. Two decades later, in 1980, staffing at federal regulatory agencies had risen to more than 146,000 employees. In the early 1980s, President Reagan led a campaign to cut government regulation. This campaign continued during both of the Bush presidencies and the number of full-time federal employees dedicated to regulatory activities modestly increased through 2000. As noted earlier, with the return to regulatory control and the addition of new funding and new agencies, the number of government employees at regulatory agencies increased to more than 277,000 employees by 2015.

The United States has experimented with different forms of government regulation for more than 200 years, and experts have learned that not all government programs are effective in meeting their intended goals. With new regulations being added each year, redundancy is likely to occur. In 2011, President Obama ordered a massive investigation of overlapping and duplicative regulatory programs. He noted that there were 15 different agencies overseeing food-safety laws, more than 20 separate programs to help the homeless, and 80 programs for economic development. Senator Tom Coburn, who strongly supported this investigation, estimated that between $100 and $200 billion in duplicative

FIGURE 7.3
Staffing of U.S. Regulatory Activities

Source: Dudley and Warren, Ibid.



[22] "2014 Draft Report to Congress on the Benefits and Costs of Federal Regulations," *OIRA Report to Congress*, Office of Budget and Management, 2014, *www.whitehouse.gov/omb*.

spending would be uncovered. In only 2 years, regulatory agencies proposed the following cost-savings changes:

- The Department of Health and Human Services finalized new rules to promote telemedicine to help hospitals and patients in rural areas, saving around $65 million over the next 5 years.
- The Department of Labor coordinated its hazards warning requirements with those of other nations, increasing safety and saving employers over $1.5 billion over the next 5 years.
- The Occupational Safety and Health Administration announced a new rule that removed over 1.9 million annual hours of redundant reporting burdens on employers, saving more than $40 million in annual costs.
- The Department of Agriculture modernized and streamlined poultry inspections rules, saving the private sector over $1 billion over the next 5 years while increasing safety in the process.
- The Federal Communications Commission eliminated over 190 redundant regulations.[23]

Continuous Regulatory Reform

The amount of regulatory activity often is cyclical—historically rising during some periods and declining during others. Businesses in the United States experienced a lessening of regulation in the early 2000s—*deregulation*—only to observe the return of regulatory activity in the late 2000s and early 2010s *reregulation.*

Deregulation is the removal or scaling down of regulatory authority and regulatory activities of government. Deregulation is often a politically popular idea. President Ronald Reagan strongly advocated deregulation in the early 1980s, when he campaigned on the promise to "get government off the back of the people." Major deregulatory laws were enacted beginning in 1975 when Gerald Ford was president and continued through the administrations of Jimmy Carter, Ronald Reagan, and George H.W. Bush, and returned during George W. Bush's administration. During these presidential administrations deregulation occurred in the commercial airlines, interstate trucking, railroads, and financial institutions industries. Some argued that when the 1933 Glass-Steagall Act was repealed in 1999 by the passage of the Financial Modernization Act, the lack of regulatory controls over the banking and securities industries led to the serious financial problems causing the economic recession in the late 2000s.

Deregulation has also occurred in Europe, especially in the arena of social regulation. In the United Kingdom, for example, the Approved Code of Practice (ACoP) governing various employee safety and health issues was downgraded to a "Guidance," a weaker form of regulatory control. In 2015, the U.K. passed the Deregulation Act that relaxed decades of increased regulatory control governing housing accommodations, motor vehicle insurance coverage, energy efficiency, and urban development, with the intention of less governmental influence in the lives of citizens.[24]

Proponents of deregulation often challenge the public's desire to see government solve problems. This generates situations in which government is trying to deregulate in some areas while at the same time creating new regulation in others. **Reregulation** is the increase or expansion of government regulation, especially in areas where the regulatory activities

[23] "Regulatory Reform Progress," January 30, 2012, *www.whitehouse.gov.* For an interesting ethical analysis of this regulatory investigation, see "The Obama Administration's Regulatory Review Initiative: A 21st Century Federal Regulatory Initiative?" Thomas Hemphill, *Business and Society Review,* Summer 2012, pp. 185–95.

[24] "Deregulation Act 2015," *Planning Resource,* April 13, 2015, *www.planningresource.co.uk.*

had previously been reduced. The scandals that rocked corporate America in the 2000s—and the failure or near-failure of a number of big commercial and investment banks in the late 2000s—brought cries from many stakeholder groups for reregulation of the securities and financial services industries. As a result, the United States has seen much reregulation in the 2010s with the passage of laws and rules governing the financial services and health care industries, as discussed earlier. As in the United States, many governments around the world reasserted their regulatory authority over the banking industry in the aftermath of the global recession. The economic think tank McKinsey & Company described the worldwide return to regulation, or *reregulation,* in these words:

> Since the financial crisis of 2008, governments have assumed a dramatically expanded role in financial markets. Policy makers have gone to great lengths to stabilize them, to support individual companies whose failure might pose systemic risks, and to prevent a deep economic downturn. . . . In short, governments will have their hand in industry to an extent few imagined possible only recently.[25]

Regulation in a Global Context

International commerce unites people and businesses in new and complicated ways, as described in Chapter 4. U.S. consumers routinely buy food, automobiles, and clothing from companies located in Europe, Canada, Latin America, Australia, Africa, and Asia. Citizens of other nations do the same. As these patterns of international commerce grow more complicated, governments recognize the need to establish rules that protect the interests of their own citizens. No nation wants to accept dangerous products manufactured elsewhere that will injure its citizens, and no government wants to see its economy damaged by unfair competition from foreign competitors. These concerns provide the rationale for international regulatory agreements and cooperation.

In cases where businesses operate in multiple countries, regulations imposed in one jurisdiction can affect companies operating out of others. But imposing regulatory controls on businesses from other countries can be difficult.

> For example, in 2012, the European Union imposed a carbon emissions fee on all airlines flying in and out of EU airspace in an effort to limit greenhouse gas emissions, a serious environmental problem discussed in Chapter 9. Within one month after the new rule went into effect, more than two dozen countries expressed their opposition to the EU's carbon emissions fee. The Chinese Air Transport Association, which includes China's four largest airlines, issued a prohibition on its airline members from paying the EU emissions fee. A few months later, India joined the group of nations protesting the fee, which had grown to 26 nation members, including airlines from the United States, Russia, and Japan. Despite these objections, the EU reported that "more than 99 percent of all major global airlines have complied with the first step" of Europe's carbon emission fee. But, six months later, the EU announced it was putting the fee "on hold" to allow the United Nations' International Civil Aviation Organization time to reach a global agreement on aviation emissions.[26]

[25] "Leading through Uncertainty," *McKinsey Quarterly,* December 2008, *www.mckinseyquarterly.com.*

[26] "China Bans Its Airlines from Paying EU Emissions Fee," *The Wall Street Journal,* February 6, 2012, *online.wsj.com;* "EU Hails Airline Emission Tax Success," *The Guardian,* May 15, 2012, *www.theguardian.com;* and "EU Halts Carbon Emission Fees for Airlines," *The Hill,* November 12, 2012, *www.thehill.com.*

At other times, the issues themselves cut across national borders, so international regulation is needed. Sometimes, nations negotiate agreements directly with one another, and at other times they do so under the auspices of the United Nations or regional alliances. For example, the United Nations monitors international uses of nuclear power due to the great potential for harm to those living near nuclear power plants and based on the threat of converting this technology into nuclear weapons.

> In 2012, the United Nations was called to Iran to investigate and determine if this country was developing enriched uranium that could be used for nuclear weaponry. Some enriched uranium was discovered, but it was unclear if Iran was developing nuclear weapons. Three years later, the world's major economic powers—the United States, the United Kingdom, France, Germany, Russia, and China—reached an accord with Iran that would require Iran to dismantle its nuclear program in exchange for the lifting of some economic sanctions by the United Nations and the major economic powers.[27]

Whether at the local, state, federal or international levels, governments exert their control seeking to protect society through regulation. The significant challenge involves balancing the costs of this form of governance against the benefits received or the prevention of the harms that might occur if the regulation is not in place and enforced. Businesses have long understood that managing and, if possible, cooperating with the government regarding regulation generally leads to a more productive economic environment and financial health of the firm.

Summary

- Government's relationship with business ranges from collaborative to working at arm's length. This relationship often is tenuous, and managers must be vigilant to anticipate any change that may affect business and its operations.
- A public policy is an action undertaken by government to achieve a broad public purpose. The public policy process involves inputs, goals, tools or instruments, and effects.
- Regulation is needed to correct for market failure, overcome natural monopoly, and protect stakeholders who might otherwise be hurt by the unrestricted actions of business.
- Regulation can take the form of laws affecting an organization's economic operations (e.g., trade and labor practices, allocation of scarce resources, price controls) or focus on social good (e.g., consumer protection, employee health and safety, environmental protection).
- Antitrust laws seek to preserve competition in the marketplace, thereby protecting consumers. Remedies may involve imposing a fine, breaking up a firm, changing the firm's conduct, or requiring the disclosure of information to competitors.
- Although regulations are often very costly, many believe that these costs are worth the benefits they bring. The ongoing debate over the need for and effectiveness of regulation leads to alternating periods of deregulation and reregulation.
- The global regulation of business often occurs when commerce crosses national borders or the consequences of unregulated business activity by a national government are so large that global regulation is necessary.

[27] "Iran, World Powers Reach Nuclear Deal," *The Wall Street Journal*, July 14, 2015, *www.wsj.com*.

Key Terms

antitrust laws, *144*
cost–benefit analysis, *149*
deregulation, *151*
Dodd-Frank Act, *144*
economic regulation, *144*
fiscal policy, *140*
market failure, *142*
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natural monopoly, *143*
negative externalities, *142*
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social regulation, *146*

Internet Resources

www.cato.org	Cato Institute
www.consumerfinance.gov	U.S. Consumer Financial Protection Bureau
www.economywatch.com	Economy Watch
www.federalreserve.gov	Board of Governors of the Federal Reserve System
www.ftc.gov	U.S. Federal Trade Commission
mercatus.org	Mercatus Center, George Mason University
www.ncpa.org	National Center for Policy Analysis
www.reginfo.gov	U.S. Office of Information and Regulatory Affairs
www.regulations.gov	Regulations.gov
www.un.org/en/law	International Law, United Nations
www.usa.gov	Government Made Easy

Discussion Case: *Should E-Cigarettes Be Regulated?*

The tobacco industry and government regulators worldwide spent decades battling over whether tobacco cigarettes should be regulated. By the mid-2010s, almost all governments had passed legislation to control the ingredients in cigarettes, how this product could be advertised, and limited their sale to individuals of a certain age, typically 18 years and older. But a new, related issue was just emerging: whether or not governments should regulate e-cigarettes.

Electronic cigarettes, or e-cigarettes, are products designed to deliver nicotine or other substances to a user in the form of a vapor. Typically, they are composed of a rechargeable, battery-operated heating element, a replaceable cartridge that may contain nicotine or other chemicals, and an atomizer that, when heated, converts the contents of the cartridge into a vapor. This vapor can then be inhaled by the user. These products are often made to look like cigarettes, cigars, or pipes. They are also sometimes made to look like everyday items such as pens and USB memory sticks, for people who wish to use the product without others noticing.

Introduced to the global marketplace in 2004, e-cigarettes have become increasingly popular around the world. By 2015, 466 brands of e-cigarettes were available globally, generating $3 billion in sales. Most e-cigarette sales initially occurred on the Internet, making the product easily accessible to both adults and teens, and at specialty vape shops. More recently, e-cigarette manufacturers have packaged their products and sold them at higher prices in convenience and grocery stores.

Advocates of e-cigarettes argued that they did not have the same harmful effects as tobacco cigarettes, claiming that they did not produce harmful secondhand smoke affecting nonsmokers. They also touted the product as a possible smoking cessation aid. Early research on the effects of e-cigarettes showed that the nicotine in e-cigarettes was addictive, just as it was in tobacco cigarettes, but because e-cigarettes did not produce smoke they were less harmful to a user's lungs than tobacco. However, much remained unknown. As one medical school professor explained, "E-cigarettes may be less harmful than cigarettes, but we still don't know enough about their long-term risks or the effects of secondhand exposure."

A few countries took up the issue of e-cigarette regulation. In 2013, Singapore banned importing and selling e-cigarettes. This move surprised many, as most Asian countries have a high tolerance for smoking and Singapore did not restrict the importation or sale of tobacco cigarettes. In 2014, the European Parliament approved rules governing e-cigarettes. Beginning in mid-2016, e-cigarette advertising was banned in the 28 nations of the European Union, as it already was for ordinary tobacco products. E-cigarette packages were required to carry a graphic health warning and be childproof. The amount of nicotine was limited to 20 milligrams per milliliter, similar to ordinary cigarettes. But the issue of regulating e-cigarettes soon moved to the global stage.

Despite the inconclusive evidence of harms caused by e-cigarette smoking, the World Health Organization (WHO) urged governments to restrict its use. The WHO report recommended that governments "ban the use of electronic cigarettes indoors and in public places and outlaw tactics to lure young users." It argued that the ban on indoor use was necessary "until exhaled vapor is proven to be not harmful to bystanders." It also called for regulation to ensure the products contained a standard dose of nicotine (since the dose varied widely among manufacturers), ban sales to minors, and prohibit the manufacture of fruity, candy–type e-cigarette flavorings.

Initially, most of the e-cigarette regulatory activity in the United States occurred at the state and local levels. By 2015, three states—North Dakota, New Jersey, and Utah—had banned e-cigarettes in public places such as restaurants and bars, and 18 states had passed some limitations on the use or sale of e-cigarettes. Nearly 400 cities or countries had restrictions on e-cigarettes. Yet, actions taken by the U. S. Food and Drug Administration in 2009, when it aggressively attacked the manufacturing, sale, and use of tobacco cigarettes by enforcing the Family Smoking Prevention and Tobacco Control Act, set the stage of more regulation targeting e-cigarettes.

In 2014 the U.S. Food and Drug Administration took a limited regulatory approach when it announced new rules that prohibited sales of battery-powered nicotine delivery devices to anyone under 18 years of age and required manufacturers to submit their products for FDA approval, in addition to disclosing ingredients and warning consumers that nicotine was addictive. But, the new FDA rules stopped short of attempting to ban advertising of e-cigarettes, Internet sales, or candy or fruit flavors, as recommended by the WHO. Makers of e-cigarettes breathed a big sigh of relief when they heard these limited restrictions. "I'm pleased the FDA has created a structure to treat these products differently than traditional combustible cigarettes," said Miguel Martin, president of Logic Technology Development, a leading e-cigarette maker.

Perhaps U.S. tobacco manufacturers had learned an important lesson from the severe regulatory controls imposed on the marketing of cigarettes, because they took initiative in effect to regulate themselves. Many placed the strongest health warnings ever on e-cigarettes, going even further than the warnings mandated on tobacco cigarette packages. Altria, the maker of Marlboro cigarettes, stated on its packages of MarkTen, its e-cigarette line, "People with heart disease, high blood pressure and diabetes should not use this product. Neither should children. Nicotine can cause dizziness, nausea and stomach pains, and may worsen asthma. Nicotine is addictive and habit forming, and is very toxic by inhalation, in contact with the skin, or if swallowed." Similarly, Reynolds American, makers of Camel cigarettes and Vuse, an e-cigarette product, printed on their e-cigarette packages the following warning, "This product is not intended for persons who have an unstable heart condition, high blood pressure, or diabetes; or persons who are at risk for heart disease or are taking medicine for depression or asthma." These warnings were entirely voluntary. Yet, some critics saw them as ploys to reduce potential legal liability or the threat that governments would ban this product altogether. A professor at Stanford's School of Medicine said, "When I saw [the warning labels on e-cigarettes], I nearly fell off my chair. Is this part of a noble effort for the betterment of public health, or a cynical business strategy? I suspect the latter."

The battle over the regulatory control on e-cigarettes will likely continue. After the FDA announced its rules in 2014, Senator Durbin of Illinois said, "Shame on the FDA. Parents across America lost their best ally in protecting their kids from this insidious product." The director of the FDA's Center for Tobacco Products told reporters it was continuing its investigation into the effects of e-smoking. "It's sort of like, walk before you run," indicating that more severe regulations could be forthcoming. Whether controls will come from Congress or the FDA, the issue of regulating e-cigarettes appears to be far from over.

Sources: "E-Cigarettes: Questions and Answers," *Food and Drug Administration* website, January 21, 2015, *www.fda.gov;* "E-Cigarettes: Health and Safety Issues," *WebMD,* accessed June 2015, *www.webmd.com;* "States and Municipalities with Laws Regulating Use of Electronic Cigarettes" *American Nonsmokers' Rights Foundation,* June 2015, *www.no-smoke.org;* "European Parliament Approves Tough Rules on Electronic Cigarettes," *The New York Times,* February 26, 2014, *www.nytimes.com;* "World Health Organization Urges Stronger Regulation of Electronic Cigarettes," *The New York Times,* August 26, 2014, *www.nytimes.com;* "E-Cig Makers Breathe Easier after FDA Proposes Rules," *The Wall Street Journal,* April 24, 2014, *online.wsj.com;* and "Dire Warnings by Big Tobacco on E-Smoking," *The New York Times,* September 28, 2014, *www.nytimes.com.*

Discussion Questions

1. Should the U.S. and other national governments ban or more severely regulate the manufacture, sale, and use of e-cigarettes? Why or why not?
2. Which stakeholders are most affected by the sale and regulation of e-cigarettes?
3. Is the tobacco industry demonstrating a strategy of working in a collaborative partnership with the FDA by its voluntary warning labels on e-cigarettes?
4. Using the elements of public policy presented earlier in this chapter, identify the inputs, goals, tools, and effects of the FDA's effort to regulate e-cigarettes.
5. What reasons, discussed earlier in this chapter, could the FDA or other national regulatory agencies use to justify greater regulatory control of e-cigarettes?