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In memory of Glenn Davis
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The subject of regulation involves questions of politics, economics, social organization, and values. Many of the existing works on the subject deal with only one of these areas, or else seek to argue one point of view, such as the desirability of more or less government involvement in the economy. Our intention in *The Uncertain Balance* is to offer the reader an interdisciplinary perspective—one that takes into account political, economic, and social issues—and to present a representative sampling of theories and points of view.

The text is organized in accordance with both a thematic and agency-by-agency structure. Part I, “Analyzing Regulations,” presents and discusses central theories and principles, thus providing a framework for the examination of federal regulators. The relationship between ideology and regulation is addressed along with the tenets held by those who are for and those who are against active government regulatory activity. Cost and benefit analysis is described as well as political-economic theory. Other areas of concern include agency personnel, the effects on government activity of public opinion and mood, and reform efforts.

Part II serves as background for the discussion of individual agencies that follows. Chapter 2 deals with economic concentration and the basic panorama of American economic development. Chapter 3 offers the two sides of regulation: the problems of underregulation—those difficulties relating to the lack of government intervention; and the problems of overregulation—those difficulties associated with government intervention.

The final section, Part III, is an agency-by-agency treatment, discussing the history, functioning, organization, and major criticisms of federal regulators in light of the concepts and arguments presented in the previous sections. The choice of regulators was designed to offer the reader a broad range of agency structures and functions. In general, agencies have either specific or relatively open-ended mandates. The Securities and Exchange Commission regulates the issuance and sale of corporate securities, while the Federal Trade Commission has the wide-ranging task of controlling “unfair business practices.” Another basic distinction between regulators is their political form. The term *agency* applies to both commissions and
administrative agencies. However, the commission is essentially a committee led by a chairman, and decisions are deliberated and voted upon by a group; this form is exemplified by the Nuclear Regulatory Commission. The administrative agency, on the other hand, is the more conventional bureaucratic form, where an administrator is in charge and there exists a more distinct chain of command; the Antitrust Division of the Department of Justice is one such agency.

Regulatory agencies cut across almost every level of the economy, regulating the direct operation of business, the environment, and the safety of the individual. The Interstate Commerce Commission and the Civil Aeronautics Board regulate the operation of various modes of transportation, affecting areas such as entry into the market, pricing, and customer service. The Environmental Protection Agency is concerned with the ecosystem, and the Food and Drug Administration monitors what the individual consumes. All agencies ultimately become involved in business, the environment, and the regulation of the individual. The Nuclear Regulatory Commission, for example, affects business by licensing plants; affects the environment by its reactor safety standards; and ultimately affects the individual by the resulting quality of the environment and the price of energy.

Our intention is not to argue for or against regulation in general. It is rather to indicate the areas of concern and the components of the subject via a representative sampling of agencies—one that illustrates their concerns and diversity. We explain how the regulatory system developed and summarize the schools of thought and criticism that regulation has evoked. The reader will thereby obtain a foundation upon which further study can be based.
PART I

Introduction
THE STUDY OF REGULATION

In a general sense, a regulation is an authoritative rule that applies to the procedures involved in an activity. An authority is an entity that people either choose to or are forced to follow, and it may take the form of an individual, group, body of ideas, or institution. We are here concerned with government regulation of business, or government limitations and prescriptions on private economic activity, enforced by the rule of law and the threat of sanctions.

Since colonial times, American legislatures on the local, the state, and later the national level have regulated business; but during the past century, agency regulation has become both prominent and controversial. Agencies—divisions of government created by legislatures to take on business regulatory tasks and run by a single administrator in the administrative agency form, or by a group of commissioners in the commission form—are often viewed as comprising the “fourth branch” of government. This somewhat provocative label points to the fact that agencies are neither purely legislative, nor executive, nor judicial, but often perform all of these functions: the agency may make rules (laws), administer them, and finally judge their merit and applications.

In any field as complex as the government regulation of business, it is useful to consider a series of questions that serves as a framework for analysis. For this reason, we offer seven queries, each pertaining to an issue that is addressed throughout the text.

1. Justification for government regulation. Should regulation be a responsibility of government? Is it related to values and political ideology?
2. *Theory and practice of bureaucratic process and structure.* How do regulatory agencies develop? What groups and individuals control them? What are the obstacles to effective regulation? How do agencies time their activities? How do they react to crises? How do they react to change?

3. *Costs and benefits.* How should cost-benefit analysis be applied to government regulation? What is the impact of regulatory agencies on productivity, technology, and innovation? Are there implications in the areas of risk taking and business organization?

4. *Personnel.* What are the backgrounds, skills, and intentions of the people that staff the agencies?

5. *Psychology of agencies and public perception.* What roles do agencies play in terms of people’s emotions and attitudes? Often, effectiveness is tempered by expectations, so that the level of public confidence becomes relevant.

6. *Regulatory reform.* How can agencies be changed? Are there governmental alternatives to agency regulation? Thinking in terms of options is an integral part of a dynamic process. For agencies concerned with change—both within the agency as well as in society—a constant reevaluation is necessary.

7. *Scope of regulation.* How extensive is the coverage of government regulation? If it affects a particular industry, how comprehensively does it monitor individual companies, and what is the extent of its penetration into each company’s functioning?

**RATIONALES PRESENTED IN SUPPORT OF AND AGAINST REGULATION**

The federal regulation of business has been a fact for at least a hundred years. Yet, it has never become a “given”—a universally accepted structural beam in the national architecture. Rather, it has found its place in discussions of ideology, values, and basic political philosophy.

What follows are two sides of a coin: the rationale of those seeking to justify or increase the level of government regulation; and the rationale of those seeking less government involvement. Neither side has a monopoly on truth. The rationales are worth examining because they clarify certain common assumptions and values; they show the basic philosophies that often color the perception of specific regulatory issues.

Political ideology is the overall conception of how a society should be governed—the set of values that forms the framework for the role of government and public participation. As such, an individual’s ideology greatly influences his or her position on regulation. The “political
spectrum" categorizes ideologies on a continuum that moves from left to center to right. Those on the far right and left both advocate a highly regulated economy. The socialist and communist viewpoint from the left is that the state should not only regulate the economy but should own the means of production as well. While Marxism calls for an entirely worker-owned society, socialism envisions less extensive state control of the means of production. From the right, the fascist view is that privately owned business should work in cooperation with the state. The state, in turn, should closely direct the economy, set production quotas, and favor certain large, privately owned corporations.

Since the United States has never been dominated by a far left or right government, its political experience essentially falls into the moderate range. Liberals generally advocate more government involvement in the economy. They are more often than not Democrats and are concerned with issues of the general welfare of consumers and labor. Conservatives usually call for less government involvement, are commonly Republican, and further the interests of business and corporate management as being consistent with the general good.

It is important that the above description of regulatory liberals and conservatives be qualified. Conservatives often advocate increased government regulation, but it tends to be more focused than general in nature. Speaking for their own industry, businessmen may seek favorable legislation or agency roles and actions that further their specific interests. In such instances, liberals and conservatives may trade arguments.

Both liberals and conservatives endorse what might be termed a "threshold level" of regulation that is composed of a core area of controls. For example, most people believe that the federal government should enforce minimum health and nutritional standards concerning food. Some regulation of the transportation industry, the production of hazardous materials, and banking is necessary so that a complex society may function. It is the extent of regulation, the rate of agency growth, the size of agency budgets, and the compliance costs for businesses that separate liberals and conservatives.

A major spokesman for the liberal approach to regulation is Ralph Nader, who labels the general interest point of view "consumerism." Consumerism, which developed within liberal camps and first became widespread during the years of Lyndon Johnson's Great Society,* looks to the federal government to enforce standards of product and service production and performance. It supports the notion of the "countervailing

* The term "Great Society" generally refers to the social and economic programs of the Johnson Administration, especially in the areas of civil rights, social welfare, and economic opportunity.
power" of the public interest working through government as a means of balancing the power of large corporations.\(^2\)

Consumerists emphasize the difference between regulation intended to protect and nurture business and that geared to protect those who make use of goods and services. Attacking the Federal Trade Commission and Interstate Commerce Commission for being too protective of business interests, they call for an activist regulatory system that remains focused on consumers and assume that business will find a way both to thrive economically and to meet regularized standards.

A prominent spokesman for the conservative viewpoint on regulation is Murray L. Weidenbaum, director of the Center for the Study of American Business at Washington University, and Reagan's first chairman of the Council of Economic Advisers.\(^3\) Weidenbaum often uses the term \textit{deregulation}, meaning the process of lessening governmental control of business. In some cases he calls for the dismantling of agencies, but his central concern is for either a moderate reduction or a slowing of the rate of agency growth. He writes, "There will not, in short, be a return to a simple status quo ante, since public concern with environmental quality, safety, equity, and similar social objectives will certainly remain."\(^4\)

THE FOUR APPROACHES TO REGULATION

Regulation-deregulation debates are usually based on one of four areas: politics, economics, communications, or ethics. Debates based on politics involve questions of the nature of power, the proper origin of power, and the preferred direction and form of power. Economic explanations are concerned with costs: the impact of government requirements upon the successful functioning and financial viability of businesses. The communications approach centers on the impact of regulation upon the collection and dissemination of information; and the area of ethics focuses on the moral issues associated with government involvement.

The Political Approach

The political approach to regulation centers on differing views about the desirable locus of regulatory power. To the regulationists, the regulators and the regulated should not be the same people. They see the notion of self-regulation—individual or groups of businesses abiding by their own rules—as impractical. Self-regulation of a group united by similar economic interests, they hold, is never entirely effective and usually leads
to a situation in which the more ethical individual is forced to yield to the less ethical one. Instead, separate divisions of the government are needed to serve as effective countervailing powers to business interests driven by the profit motive. Regulationists see a democratic element to agency regulation. Members of agencies are either appointed or nominated by a president elected by the people and are confirmed by a Senate that is also publicly elected. Rules often specify required party composition of agency leadership, as well, so that one political party does not dominate.

Another element of the regulatory case in the political area is pluralism, which political scientist David Truman defines as a political context of competing and overlapping interests. In a complex society, individuals are likely to belong to a variety of groups that express their interests but are not necessarily entirely compatible. For example, a consumer activist may belong to an organization seeking to promote higher quality air conditions, but may also choose to drive a car rather than opting for travel on the less-polluting mass transit system, and may join the American Automobile Association (AAA). Regulatory agencies, which include hearings procedures, provide a forum for the expression and sorting out of these interests by individuals and groups. Agencies may resolve conflicts and forge compromises.

The agency is open not only to the regulated industry but to consumers and competing interests as well. A fruitful interaction is likely to occur at an agency hearing. If an environmental protection group testifies in front of the Nuclear Regulatory Commission along with a producer of nuclear energy, the producer is likely to realize that, besides being a producer, he or she is also a consumer of the environment and is likely to be affected by a pollutant. The agency itself is made up not only of individuals with a background in the nuclear industry, but also of other scientists, environmental specialists, energy specialists, and career bureaucrats, all with different and sometimes overlapping professional interests and perspectives. From this interaction of differences, shared interests are perceived and compromises reached.

A final regulatory political argument is that a system of agencies is policy-oriented. Goals tend to be overtly stated so that society becomes a purposeful and unified system. Without policy, they say, planning is difficult, and power becomes too diffused. With policy, the public at least knows what the government and the current direction of society are about and may endorse or reject them at the polls.

Deregulationists respond that these points draw misleading conclusions. The foundation of a true political-economic democracy, they believe, is the existence of basic political and economic "spheres," or sectors, that remain somewhat autonomous. Accepting a core of regulation necessary for safety and survival, they stress the essential
purpose of government: the protection of property; the assurance of rights; and the economic functions concerning taxes and finance. When the government penetrates too far into the internal operations of firms, it oversteps its proper power. Government should not be in the business of manufacturing, private management, or distribution. In the words of Weidenbaum, "Economic freedom is inseparable from political freedom."6

Deregulation, not regulation, is seen to democratize the political economy by virtue of lessening governmental dictation. Political control of agencies is indirect. Independent agencies, they say, are insulated from the executive and legislative branches and enjoy some of the protection from popular control that characterizes the judicial branch of government; lessening agency power leaves more power to the private sector.

The existence of agencies, according to deregulationists, may actually encourage special treatment of certain interest groups. Vocal and organized lobbyists may gain sympathetic rulings or protectionist policies. In a deregulated context, interests compete in the economic rather than the governmental "marketplace." Finally, on a political level, deregulationists prefer a diversity of goals to those neatly spelled out by the government. When the government proclaims a desirable ratio of surface to air transportation, it is an imposed dictate. When the goals of individual firms merge in the marketplace, the best ideas—the ones that work and that people are willing to endorse by their patronage—will grow in power.

The Economic Approach

From an economic point of view, those favoring regulation identify a regulatory tradition in the United States, beginning with the colonial period. At that time corporations chartered by the colonies were highly regulated, with the state controlling their operations, organization, and size. Common law brought over from England regulated matters such as price and professional standards.7 Even during the nineteenth century, regulationists point out, the federal government retained a somewhat active role in the regulation of business. A national bank granted loans, and tariffs protected developing businesses. During the 1840s, Congress offered subsidies for ships that carried mail, and somewhat later granted millions of acres of land to railroad companies.8

Regulationists emphasize the negative rather than the positive aspects of the relatively less regulated periods of history. Economic depression in the 1870s, 1890s, and 1930s seriously jarred the economy, and huge corporations sprung up, dominating their industries and dictating quality and pricing standards without the tempering influence of competition. In addition, regulationists say, advances in technology made it increasingly
difficult for consumers to be informed about their purchases, so that the dictum of *caveat emptor* (let the buyer beware) became increasingly meaningless from the consumer's standpoint.

Regulationists stress the tradition of government intervention rather than that of noninterference in economic affairs. The real turning points for the permanent establishment of the regulatory state came during the progressive period in the first decade of the twentieth century, and during the establishment of the New Deal in the 1930s. A major statement was made in 1909, when progressive writer Herbert Croly published *The Promise of American Life*. Croly wrote that the positive or activist state could replace chance in the determination of the general welfare. Rather than just promoting developing businesses, the federal government should be involved in more general economic development. By the election of 1912, all three presidential candidates—Wilson, Taft, and Roosevelt—endorsed programs of government regulation centering on antitrust activity. During the administration of Franklin Roosevelt (1933-1945), a huge regulatory apparatus became justified in terms of Keynesian economics, an approach to government intervention that went beyond Croly and held that the state would be a major spender in the economy.

Regulationists using an economic approach believe that government intervention may promote new industries, aid in the socially useful allocation of resources, and prevent scarcity through planning and the enforcement of rules. By dismantling monopolies, competition is preserved. When market dislocation occurs as a result of foreign competition, dips in the business cycle, crop failures, transportation breakdowns, labor strikes, loss of foreign markets or supplies, or other such events, the government may seek to reestablish a balance. It may temporarily alter prices, create subsidies and other means of protection, allow businesses to diversify, or change financial policy affecting the money supply and interest rates. The consumer, as well as the business sector, is protected by the requirement of fair prices and product and service quality. Regulationists associate economic progress with governmental regulatory activity. They point to periods in American economic history that appear to support that view and refer to a nation such as Japan, in which state-led, or regulatory capitalism coincides with strong economic performance.

From an economic point of view, those currently furthering deregulation cite instances in which economic progress was associated with a less activist state. When the state steps back, the forces of supply and demand in the market work toward economic growth. A classic source for deregulationists is Adam Smith's *The Wealth of Nations*: Published in 1776, Smith's work criticized the highly regulated system of mercantilism in effect since approximately 1500. According to Smith, the market
became an “invisible hand” that guided business decisions and propelled forward development. Deregulationists point to the nineteenth century and early twentieth century as a time of rapid economic development—a period in which business was far less encumbered by regulation than it is today. Former Republican Secretary of the Treasury William Simon writes, “The capitalist miracle, which created the extraordinary wealth of our nation, occurred in the United States because this explosion of wealth is uniquely a result of individual liberty. This is the true defense of capitalism.”

Acknowledging economic problems such as depression and recession, deregulationists relate these difficulties to the intervention of government. A regulatory state often handicaps productive individuals in order to subsidize nonproductive individuals. Rather than policing for illegalities, the regulatory state subjects everyone to endless rules and monitors actions before the commission of illegalities.

The deregulationist economic case states that when government involvement is minimized, it is the highest-quality companies that survive. Dips in the business cycle become “flushing out” periods, eliminating the mismanaged companies and ultimately encouraging the better and more necessary ones. Resources are allocated according to consumer demand—not according to some centralized plan. When the private sector is left free to make its own decisions, resource scarcity is not more likely to occur. Deregulationists indicate that a powerful human motive is the desire for economic survival. The oil industry, for example, has a huge stake in the exploration for new sources of oil, additional supplies of fossil fuels being a condition of its own survival. Deregulation may also prevent destructive competition, or periods in which prices become too low due to the crowding of the marketplace and the squandering of resources on firms that are doomed to failure. Such competition, they hold, is in part created when the government prevents the natural expansion of the best companies by overly aggressive antitrust actions. Less regulation, by reducing the costs of complying with regulations, allows for higher profits and a resulting increase in investment and growth.

The Communications Approach

In the area of communications, regulation, according to some, furthers the gathering and dissemination of data. A nationally oriented agency that has responsibility for an industry or a sector of the society such as consumer products or the environment is in a good position to collect, disseminate, and evaluate information. The Food and Drug Administration is continually publishing materials on the actions and side effects of drugs. The
Environmental Protection Agency communicates its knowledge of the way in which firms process and manage their waste products. The Occupational Safety and Health Administration is a storehouse of information on labor behavior and performance.

Because the agencies are national in scope and possess sophisticated tools of analysis they can standardize data and compare and contrast similarities and differences, communicating their results in a digestible form. Because of the generally high level of their personnel, the regulatory agencies combine power with expertise. The Nuclear Regulatory Commission, for example, employs nuclear scientists, economists with technical backgrounds, and lawyers specializing in the legal aspects of nuclear power.

Deregulationists counter that a vigorous market system is conducive to information. Competition for markets breeds research, improvements in production methods, and communication to consumers through advertising. In a deregulated context, industries tend to organize and formulate professional standards that are widely publicized. Deregulationists draw a distinction between regulation and the provision of information. Government may usefully provide information without regulation, and this service is welcomed. This deregulationist approach has its roots in a self-regulatory effort of the 1920s known as associatism, which became a widespread phenomenon.14

The Ethical Approach

Finally, other justifications for regulation are based upon ethical considerations. Important ethical questions lie in the area of rights and equity. Rights are entitlements: that which belongs to people by just claim. Equity is impartiality, or the application of rights according to general principle rather than special interest preference. Rights and equity involve matters of opportunity and discrimination, power and advantage, rewards and contributions.

Those favoring regulation relate rights and equity to contracts. An equitable contract embodies three aspects: the capacity of parties to understand its terms; the freedom of parties to enter, modify, or reject the contract; and the consideration, that is, the relinquishment of something of value by each side. Regulationists state that a condition of underregulation subverts the contract process. Individuals who lack education or any employment prospects are not really in a position to form contracts. They may not understand its terms, or they may be in a functional state of duress, that is, not truly free to enter or reject it because of economic
desperation. These individuals will probably take a job under any terms because they lack bargaining power. Underregulated contracts often become discriminatory; an employer may make prejudicial contracts by hiring practices, ignoring some individuals on the basis of sex, age, religion, or race.

The regulatory process has some influence over the ethics of reward and contribution. The overriding social value in reference to income is that it should reflect contribution and responsibility rather than position of power and advantage. The condition of monopsony—monopoly power on the buyer's side—in the labor market, for example, allows the dominating employer to set wages at will. Regulation of wages and income redistribution by taxation makes compensation more dependent upon social contribution and less dependent upon economic power.

Other ethical areas of regulation are fair business practices and environmental and individual protection. Regulation through the enforcement of fair business practices in areas such as disclosure of product information, pricing, and performance helps to minimize deception and fraud. By protection of the environment (the air, water, aesthetic quality) and of the individual (working conditions, food, medications) it ensures humane minimal standards that apply to all. Sanctions for violators provide punishment as well as provoking societal condemnation.

Those supporting deregulation also indicate an ethical basis for their position. They state that a less regulated economy connects economic opportunity and resource utilization with ability. The onus for unemployment lies more with the individual, who has not taken full advantage of educational opportunities, or who has failed to determine what kinds of manpower are required by society. The utilization of the nation's resources remains with business people in the marketplace. Since less regulation would encourage economic development, the economy would be in a better position to satisfy needs and wants so that both the environment and the individual would be better cared for. Accountability and responsibility is fostered by the demands of consumers, by competition in the marketplace, and by the competition of firms for high-quality labor and management. The ultimate sanction against a wayward company in a less regulated context is the nonsponsorship of the market and the resulting business failure.

Deregulationists claim not to seek the elimination of rules and laws. They do not seek to make polluting the environment lawful or endangering the safety of workers unassailable. Rather, they seek to return transgressors to the more traditional legal system. Violations of the law are attended to after the fact by law enforcement rather than by regulatory agencies. When an individual's rights are violated, remedies are sought in the courts. Instead of a continual monitoring and governmental dictation
Table 1.1
Reasons for and Against Intensive Agency Regulation

<table>
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<th>BASIS</th>
<th>FOR REGULATION</th>
<th>FOR DEREGULATION</th>
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<tr>
<td>Politics</td>
<td>1. Establishes agencies as countervailing power to business.</td>
<td>1. Further's political and economic &quot;spheres.&quot;</td>
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<td>2. Democratizes the political economy.</td>
<td>2. Democratizes the political economy.</td>
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<td>3. Negotiates competing and overlapping interests.</td>
<td>3. Minimizes the need for interest negotiation.</td>
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<td>4. Articulates unified goals and policies.</td>
<td>4. Encourages diversity.</td>
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<td>Economics</td>
<td>1. Promotes industry.</td>
<td>1. Demands efficiency and weeds out inefficiency.</td>
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<td>2. Rationizes resource allocation.</td>
<td>2. Further's demand-sensitive resource allocation.</td>
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<td>3. Guarantees service and quality.</td>
<td>3. Further's consumer-determined service and quality.</td>
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<td>5. Preserves constructive competition.</td>
<td>5. Prevents destructive competition.</td>
</tr>
<tr>
<td>Communications</td>
<td>1. Guarantees information for labor management, and consumers.</td>
<td>1. Competition for markets leads to research, advertising, and communication with consumers.</td>
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<td>2. Standardizes data.</td>
<td>2. Increases data available to public.</td>
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<td>3. Further's clarity and expertise in area of communications.</td>
<td>3. Further's clarity and expertise in area of communications.</td>
</tr>
<tr>
<td>Ethics</td>
<td>1. Further's equity of rights and resource allocation.</td>
<td>1. Associates opportunity and resource utilization with ability.</td>
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<td>2. Protects individuals and environment.</td>
<td>2. Protects growth and ultimate satisfaction of needs and wants.</td>
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<td>3. Avoids deception.</td>
<td>3. Requires education.</td>
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<td>5. Imposes sanctions.</td>
<td>5. Imposes sanctions.</td>
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</table>

of procedures, individuals and firms remain free to find their own solutions, or to err and then pay the penalties.

The four types of argument presented for and against agency regulation are summarized in Table 1.1.
BUREAUCRATIC PROCESS AND STRUCTURE: THEORY AND PRACTICE

The organization and function of agencies affect their performance. Although here we use the term agency to apply to all federal regulatory offices, a distinction should be made between the commission and the administrative agency. A commission is headed by a number of commissioners (normally five to seven), with a chairman. Commissioners, although nominated by the president, serve fixed terms. The administrative agency is headed by a single administrator, who is appointed by the president. The administrator, like the commissioners, is subject to the confirmation of Congress. However, in the case of the administrator, the president's influence is more direct, due to the power of removal. Administrators' salaries are also more subject to change than are those of commissioners.

The commission form is more democratic than hierarchical; however, it poses its own set of problems. Although the commission chairman's role varies, the chairman is often more a facilitator and less a leader than is the administrator. The commission chairman has considerable appointment and administrative powers but has only one vote on important matters; chairmen are powerless in voting matters when opposed by a majority of the other commissioners. The Ash Council, which evaluated federal regulations in 1971, recommended replacing commissioners with administrators. The commission found that collegial bodies—commissions in which decisions are often subject to voting—often fail to coordinate their policy with that of other executive agencies. They tend to get bogged down in details and cause delay, and they remain too insulated from Congress and the president.17

Collegial bodies are more susceptible to the hazards of group dynamics than are administrative agencies. Decision-making groups potentially have the advantage of bringing more different points of view to the decision-making process, as compared with administrator-headed agencies. In action, though, they often lose direction and may be unsuitable for crisis situations. One government study found that the optimal number of commissioners ranges from three to five. This number allows majority voting but is too small to allow for the creation of factions.18

Administrative agencies contain a swifter decision-making process than do the commissions. The single administrative chief simply passes on directives, rather than engaging in discussion and negotiation as do the commissioners. They are more likely to pursue a broad presidential policy, because they serve at the pleasure of the president and may be removed at any time. Actions in administrative agencies tend to be swifter, then, and more oriented toward broader presidential regulatory policy.
The importance of a structural difference such as that between the commission and administrative forms should not be overemphasized. There is no guarantee that the economy always benefits from one or the other. History indicates that Congress, which might have more control over the commission, and the president, who might have more control over the administrative agency, do not necessarily act in accordance with what will benefit society as a whole. Both Congress and the president may, on occasion, submit to the political pressures of special interests.

Another issue in the regulatory process is the matter of time required for regulatory functions. This stems from the nature of procedure. The agency must publish proposed rules in the Federal Register. Hearings then follow. After the hearings, each commission and agency has its own internal process of coming to a decision, involving the subunits of its organization. Regulations are adopted and published and must then be implemented. Implementation involves an entire judicial process; for example, the administrative law judges associated with each regulatory office hear disputes over licensing and violations involving fines or penalties. The recommendation of the administrative law court is read over by the agency itself—again a lengthy process—before a final decision becomes binding. Besides legislative and judicial functions, agencies perform an executive function by enforcing and executing their own requirements and sanctions. Finally, business may appeal regulatory actions through the federal court system.

The rule-making, judicial, and executive functions of agencies are built in to their relatively self-contained method of proceeding. Sharing these functions with other organizations or branches of the federal government would probably create further delay. The system provides a due process that works against arbitrary power or the domination of favored parties. Potentially affected parties must be given an opportunity to speak, ample time to prepare their statements, and the opportunity to appeal. In addition, agencies are now required to conduct their proceedings regularly in public session so that businesses can know the status of actions involving their interests.19

The agencies, however, do not feel the positive pressure of time that affects other sectors of the government. Upcoming elections and calendars serve as a positive impetus for Congress to act; elections force the president to coalesce views and to push for the enactment of programs. The very insulation that helps the agencies to assume a posture of disinterest tends to disassociate them from the clockwork of an economy under pressure. An amendment to administrative procedure law that sets maximum time limits for certain aspects of regulatory activity—specifically, the hearings stage—could induce some positive pressure into the system.
Theories of Regulatory Structure and Process

The Life Cycle Theory

Several theories attempt to explain the nature and behavior of the regulatory offices of government. One of the most widely discussed is political scientist Marver H. Bernstein's life cycle theory, which, although formulated in reference to the regulatory commission, may also be applied to administrative agencies. It is an organic perspective, since it is based on biological concepts, viewing agencies as going through an aging process. Bernstein identifies four stages: gestation, youth, maturity, and old age. Gestation, which may require twenty or more years, is marked by a "period of slowly mounting distress over a problem." Organized groups then perceive some stress and make demands on the government. After a period of agitation and political pressure, a statute is enacted. This statute is general in nature, reflecting its compromise nature.

In its youth, the commission is aggressive and may take on a crusading spirit. The environment is adversarial; the calendar is filled with conflicts. Yet, at this very time, opposition in the broader society is becoming more organized, more influential. By the time of its maturity—the third phase—the commission becomes devitalized. In the face of decreased public support, it becomes more of a manager and less of a crusader or policeman. As a means of avoiding further attack, it opens itself to challenge and invests much of its time in adjudication. Because of case backlogs and general inefficiency, the commission becomes a "captive" of the industry it is supposed to regulate and is "accepted as an essential part of the industrial system." Watching over the health of its industry, the commission becomes a quiet promoter.

The final phase, old age, is marked by debility and decline, when procedures are sanctified and the status quo fossilized. Actions are reflexive and cut off from public sentiments or current trends. The commission is now "the recognized protector of the industry." Along with a decline in function, there is a budgetary decline. Congress and the president have become wary of investing substantial funds into such staid organizations. The commission either hobbles along or is eventually disbanded.

The Capture Theory

Political economist Sam Peltzman argues that industries gain their influence according to their impact upon voters, who reflect the power of large firms by voting according to the interests of the large corporation.
Analyzing Regulations

According to this view, economic wealth and position is translated directly into political impact. Stated another way, the voter comes to feel that "what is good for General Motors is good for the country."

A widely read exponent of the capture theory is economic historian Gabriel Kolko, who unlike Peltzman, concedes that other forces besides regulated industries are involved in the creation of agencies. In the case of the Interstate Commerce Commission (ICC), farmers and shippers first advocated federal control. But the creation and initiation of the ICC, says Kolko, served the railroad interests by ensuring rate and profit stability. He concludes that rather than being an example of "progressivism," in which the welfare of the average and vulnerable citizen is protected, the ICC is more a protector of railroad interests. Yet Kolko never really analyzes the market structure, and the reader is at a loss to determine what rates would have been in the absence of regulation. Also underplayed is the nature of railroad competition. Before 1900, 874 railroad lines existed; by 1907, the number had increased to 1,564. Under the Interstate Commerce Commission, railroad power became diffused rather than more concentrated. Should many railroads have failed in the absence of regulation, it is possible that rates of the concentrated railroads would have increased.

Capture theory, it should be noted, ignores the differences of interests between small businesses and large ones within the same industry. A small bank, for example, may have a different view on regulations affecting the requirements of branch banks than does a large one.

The Bureaucratic Behavior Theory

Another category of ideas on regulation comes under the theory of bureaucratic behavior. Many of the characteristics of bureaucracy, some argue, seriously hinder bureaucratic effectiveness; organization in itself becomes an obstacle to the effective regulation of business.

Parkinson's Law, named after C. Northcote Parkinson, who observed the English navy, states that organizations will seek to expand their size and influence, regardless of the objective need, and that bureaucrats will always seem busy since work tends to expand to fill the available time. Two important processes at work in Parkinson's Law are that officials want to multiply their subordinates and not their rivals and that officials within a bureaucracy tend to create work for each other. A related dynamic is Morton Halperin's notion of bureaucracy as a vested interest that seeks to maximize its impact on government functioning and addresses governmental solutions in terms of its own interests.
The "Peter Principle" supplies another reservation to the reliance upon government agency regulation. It states that an individual is continually promoted until he reaches his level of incompetence. The result is that bureaucracies are filled with individuals who are either in a state of mobility or are functioning poorly.25

A broad critical explanation of agency functioning is related to interest-group liberalism, a concept described by Theodore J. Lowi in a highly influential book appearing after the disappointing performance of the Great Society, titled The End of Liberalism.26 Interest-group liberalism, holds Lowi, endorses the positive role of the state in order to express the interests of highly organized groups. Expectations are so high that broad mandates, rather than specific goals, are assigned to government organizations. Those with vested interests are allowed to share in policy formation. Explicit legislative standards are replaced by imprecise enabling instructions that are long on ambition and short on oversight and accountability. Regulatory agencies, then, especially the new social regulators of the 1970s, placed in this context will tend to spend and to promise but to deliver little.

Placed in this perspective, a successful agency is the Securities and Exchange Commission (SEC), whereas a less successful one is the Federal Trade Commission (FTC). The SEC has a clear and realistic mission and a continual focus: regulating securities brokers and dealers in the issuance and trading of securities in publicly held companies. The FTC, on the other hand, is saddled with the general task of addressing "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce," a function that cuts across the entire economy rather than a specific industry.27

A particularly useful approach to the entire regulatory and economic system involves the application of biological concepts. As defined by organizational theorist Mason Haire, "the biological model for social organizations . . . means taking as a model the living organism and the processes and principles that regulate and describe its growth and development."28 According to this view, the essence of life is change. Organisms either continue along a developmental path or begin to deteriorate. Inbreeding causes fragility, and the lack of innovation fosters decay. In terms of human biology, with the possible exception of the appendix, each part of the normally functioning body performs a positive function. Intruders into the body, such as excess body fat or tumors, often cause harm. While not every basic component of the body is essential to survival, each contributes to its total functioning and allows the individual to develop and to grow. The body's regulatory process seeks to keep the components interacting effectively by nourishing those that contribute to development and by eliminating those that create unnecessary waste, disease, or stunted development.
The biological approach to regulation relates the regulatory functions of a political economy to the regulatory functions of the body. A social regulatory system attempts to identify the “fat” and excise it. It attacks potentially harmful elements. It seeks to create the proper balance between resources and production, supply and demand, leading to a condition of homeostasis, the maintenance of stability or equilibrium of energy consumption and expenditure in the body.

**Levels of Analysis**

Dividing the components involved in agency regulation into various levels makes it easier to grasp the range of factors that affect the nature and impact of regulation. These levels may be described as agency, governmental, direct regulatory, and systemic. Agency-level dynamics encompass those elements distinctive to intra-agency functioning: personnel, organization, budget, procedures. The governmental level involves the ways in which other portions of the government affect the office in question: congressional oversight and the budgeting process, nonbudgetary legislation, political pressure, appointments, support functions (e.g., interagency liaison, informational cooperation). Third, the direct regulatory sectors, are those sectors of the economy directly affected by the office in question. Key considerations here are the agency’s responsiveness to consumer and business interests, how the industry makes its views felt, the relation of the regulated industry to other industries, and the impact of the regulated industry upon other sectors of government, which in turn may affect the agencies. Finally, there is the systematic level, the political economy of the society as a whole. The relevant independent variables here (factors that affect the behavior of agencies) are the performance of the economy, the dominant political mood and ideology, and reactions to international factors such as trade and political stability.

One problem with most theories of regulation is that they do not take into account all of the levels of analysis. To use the biological analogy, a physician, in analyzing the functioning of an organ of the body, analyzes the integrity of the organ itself, its functioning within the organ system (e.g., the left lung in the respiratory system), the metabolism of the body affected by that organ system, as well as the impact of the entire body upon that organ. There may be tissue weakness in the lung. It could relate entirely to intralung cell metabolism, or perhaps the basis is malfunction of the breathing apparatus in the organ system involving the diaphragm muscles, or a problem with the oxygen levels of the blood feeding the lung.
tissue and relating to both the respiratory and circulatory systems, or else a general nutritional deficit relating to the entire individual.

Likewise, in the political economy, levels tend to interact with each other. The level of the economy influences business decisions within an industry, yet industry decisions affect the economy as a whole. In the same way, the system level interacts with the governmental and agency levels. The interaction of regulated industries with agencies is well known: Agency decisions affect the operations of business; and business representatives testify at agency hearings and lobby members of the legislation and policies. The government is influenced by public opinion and mood, as it can also alter the public's opinion by its own image and performance. Agencies seek to influence decisions of the other sectors of the government by testifying at congressional hearings, for example. Agencies also base their decisions on systemic factors. Figure 1.1 illustrates this interactive process.
COSTS AND BENEFITS

During periods of economic difficulty, economic rationales for regulation become especially relevant. In recent years, the economic approach has become formalized as an area of the field of political economy termed cost-benefit analysis. Proponents of this type of analysis indicate that it is extremely practical, geared toward how things actually work rather than toward abstract theory. Instead of focusing upon ideal situations, cost-benefit analysis asks the central question, Do the benefits of a particular regulation outweigh its costs?

One response to the subject of costs and benefits is the philosophical position of utilitarianism. The utilitarian adds up positive consequences of actions in terms of human satisfaction. The option that creates the greatest satisfaction is the desirable one. The emphasis remains on feelings so that costs are viewed in terms of their perceived discomfort. The utilitarian asks, for example, how much the payment of a tax offsets the satisfaction created by the agency for which it pays. Most cost-benefit analysis, however, is economic rather than psychological and attempts to quantify effects in dollar terms. The major difficulty here, however, is the matter of scope, or determining just where a cost or benefit ends.

In terms of costs, when a business calculates its costs of compliance, it isolates some obvious figures such as costs of administration, changes in ingredients and machinery, and alterations in plant construction. But what about the impact of the redirection of capital? Is part of the compliance cost the profits lost when available funds are directed to research and development or advertising and promotion instead of to regulatory compliance? Should one include the costs of well-paid executives devoting their time to redesigning operations, setting up government relations departments, and becoming versed in the subject matter of regulation?

The same may be said on the benefit side. A sum of money may be invested in improving the ventilation system of a plant. Calculating the statistical trends, one may demonstrate the resultant decrease in the number of sick days taken by workers. This is a benefit to the company. But one may go further and add the benefit to the worker and to society in reduced medical expenses. Some analysts would also include the benefits created for the worker's family. A healthy worker is probably better able to educate his children, who will in turn be more valuable to society as a whole. At what point do the indirect costs and benefits end, and what impact do they have on calculations for decision making?

The nature of risk is another problem in cost-benefit analysis. One kind of benefit is the minimization of risk. The degree of risk is difficult to measure, and the acceptance of risk involves social values. The Delaney Amendment to the Food, Drug and Cosmetics Act of 1958 expresses a
The Uncertain Balance

no-risk framework. This act allowed the Food and Drug Administration to ban any substance that created cancer in man or animals, regardless of the dosage levels required to produce cancer or of the costs involved in banning the substance.

The problems with the no-risk position led to four additional alternative regulatory frameworks involving cost, benefit, and risk. The regulation of nitrates forced the issue. Although eating nitrates involves some risk of cancer, it also protects from botulism. A risk-risk framework emerged under which regulators could balance the risk of consuming a substance against the risk of not consuming it. The very low probability of cancer was matched against the much higher probability of food contamination, and therefore the limited use of nitrates was justified.

A third framework is the risk-benefit approach. Here the risks and benefits of the same action are weighed. An agency considers all the effects of a single action and endorses it if the positives sufficiently overshadow the negatives. A fourth option places risk within a cost framework and is known as the regulatory budget approach. The legislature decides not only the budgets for each agency, but the total compliance costs that are justified. Thus in one motion Congress decides how much money may be invested in a specific regulatory arena.

Last is the formal benefit-cost framework, which carries quantitative analysis to its limit and places a value on all possible costs and benefits. It requires, for example, figures for the number of lives that would be saved by the elimination of a chemical from the environment and places values (usually dollars) on the years of lives saved. The bottom line is a summation of positive and negative effects, with a decision identical to a business decision based on expected profits or losses.

Several conclusions are apparent from these alternatives. First, decisions cannot be based solely on either quantitative or qualitative measures. The formal benefit-cost framework attempts to quantify the unquantifiable. It is impossible to place a dollar value on a human life. Although an individual may buy a life insurance policy and therefore assign an implied value to his life, this is a private contract and is based on the costs of premiums and needs of the survivors, not on a real measure of the individual as a social commodity. The worth of a life lies firmly within the realm of subjective values. On the other hand, a life has quantitative aspects. A worker produces so much each year; a doctor treats so many patients. But the total value involves facets that are impossible to quantify: the emotional sustenance of a family; the uniqueness of the individual and the impossibility of replacing him or her. The total life involves the quantitative and qualitative. The total cost framework, whereby Congress dictates maximum compliance costs, likewise relies too heavily on assigning dollar values.
Nor can regulatory decisions be divorced from costs, however. The no-risk framework may appeal to some because it addresses their fears, but it is impractical. All drugs, for example, have side effects and pose some risk. It makes no sense to deny all the antibiotic benefits of penicillin because some people may be allergic to it. As illustrated by the formal benefit-cost framework, costs should not totally dominate, but they should not be ignored either.

The risk-risk and risk-benefit approaches have the limitations of focusing on one option without relating it to alternatives. Risk-risk balances the risks of action against inaction, in the case of nitrates, cancer or botulism; risk-benefit moves beyond risks and examines benefits, but again, it is tied to one action or decision.

One useful way to draw upon these options is a sixth alternative, which we term the risk-benefit-cost approach, whereby the decision maker first defines a problem and then lists as many options as possible. An example is illustrated in Figure 1.2, concerning the reduction of cancer. Each option has six categories based on action or inaction in the areas of risk, benefits, and costs. The values may be quantitative or qualitative (e.g., nonaction on nitrate elimination may be qualitatively high-risk, medium-risk, or low-risk). The approach compels the decision maker to consider risks, benefits, and costs, but it does not mechanically calculate a decision. Final action remains an informed but human decision based on objective and subjective values.

**Figure 1.2**  
**Risk-Benefit-Cost Approach**

<table>
<thead>
<tr>
<th>CANCER CONTROL</th>
</tr>
</thead>
<tbody>
<tr>
<td>options: nitrate elimination auto exhaust control asbestos elimination</td>
</tr>
<tr>
<td>risk benefit cost</td>
</tr>
<tr>
<td>a. i. a. i. a. i.</td>
</tr>
</tbody>
</table>

Decision factor line

*a. = activity  
i. = inactivity*
The approach holds implications for the locus of regulatory power. When options are maximized, they cut across regulatory jurisdictions. In the case of cancer, the Food and Drug Administration, Consumer Product Safety Commission, and Environmental Protection Agency are all involved. The most effective and efficient decisions, then, involve multiple agencies and require excellent interagency liaison and coordination.

Information on regulation should always be carefully interpreted. Often, arguments are drawn and data is presented in support of a political position. Most importantly, a discussion of the costs of regulation that does not consider the benefits has limited application. For example, a study produced by the Center for the Study of American Business of Washington University, *Costs of Regulation and Benefits of Reform*, is in effect a political statement calling for a reduction of regulatory activity. All the information is detailed and accurate. It includes figures on regulatory expenditure in terms of regulatory budgets and compliance costs, as well as figures on the estimated increase of automobile prices due to federal regulations. But the study fails to address estimated costs of *not regulating*.

Due to the problem of the scope of costs and benefits—the difficulty in drawing limits—analyses will tend to reflect the political purposes of the writer. At the least, the analysis should attempt to balance costs and benefits in order to determine a truer picture of the costs.

In testimony to the Committee on Interstate and Foreign Commerce, the Corporate Accountability Research Group, an organization affiliated with Ralph Nader but with its own political biases, attempted to summarize the costs and benefits of government regulation. They concluded that the benefits of regulation in 1978 outweighed costs by a total of $5.7 billion. While the debatable area is the specific figures, they are entirely accurate in approaching the problem in terms of a ratio of benefits and costs. That is, the costs of *not regulating* are the benefit figures (see Table 1.2).

**PERSONNEL**

On a less theoretical level, the individuals that compose the agencies are an important consideration in agency performance. The Center for the Study of American Business cites a 216 percent increase in agency staffing from 1970 to 1979. It should be remembered that the figure represents not only an increase in staffing of existing agencies but also the staffing of a considerable number of new agencies that came into existence during the early 1970s. Another qualification is that the federal government has not
### TABLE 1.2

**ESTIMATED COSTS AND BENEFITS OF SELECTED REGULATORY ACTIVITIES**

(BILLIONS OF DOLLARS)

<table>
<thead>
<tr>
<th>AGENCY</th>
<th>COSTS IN 1978</th>
<th>BENEFITS IN 1978</th>
<th>BENEFITS IN 1983</th>
<th>POTENTIAL BENEFITS (DAMAGES IN 1978)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Occupational Safety and Health Administration</td>
<td>4.3&lt;sup&gt;a&lt;/sup&gt;</td>
<td>6.4</td>
<td>7.2</td>
<td>73.0</td>
</tr>
<tr>
<td>Environmental Protection Agency</td>
<td>22.7&lt;sup&gt;b&lt;/sup&gt;</td>
<td>23.3</td>
<td>44.2</td>
<td>56.0</td>
</tr>
<tr>
<td>National Highway Traffic Safety Administration</td>
<td>4.0&lt;sup&gt;c&lt;/sup&gt;</td>
<td>6.0</td>
<td>26.0</td>
<td>68.0</td>
</tr>
<tr>
<td>Food and Drug Administration</td>
<td>0.4&lt;sup&gt;d&lt;/sup&gt;</td>
<td>1.4</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Consumer Product Safety Commission</td>
<td>N/A</td>
<td>N/A</td>
<td>0.8</td>
<td>9.5</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$31.4</strong></td>
<td><strong>$37.1</strong></td>
<td><strong>$80.6</strong></td>
<td><strong>$206.5</strong></td>
</tr>
</tbody>
</table>

**Note:** N/A indicates data not available.

<sup>a</sup> Annual McGraw Hill Surveys, *investment in Employee Safety and Health, 1972-78.* This figure is for 1978.


<sup>c</sup> Mr. Weidenbaum's corresponding estimate for auto safety regulation is $438/car.

<sup>d</sup> Mr. Weidenbaum's 1976 figure for FDA is calculated by multiplying annual prescription drug sales by 47. This figure applied to the $11 billion in such sales in 1978 yields the figure in the table, rounded to the nearest hundred million.


Greatly expanded with respect to changes in the total population: 13.9 federal employees existed for every 1,000 Americans in 1949; 13.2 in 1976; and the number has never been higher than 16.3 (1952). In addition, although the rise in the number of employees in federal regulatory agencies was 82 percent for 1972, the rise decreased to 2 percent for 1979.

Besides numbers, the appointment process is a relevant manpower issue, which has both political and procedural implications. Whether appointments to commissions and administrative agencies is an example of patronage politics or of connecting the right people with the right jobs, or both, depends on the individuals making the appointments. Some
26  The Uncertain Balance

TABLE 1.3
RESPONSIVENESS OF COMMISSION/BOARD MEMBERS

<table>
<thead>
<tr>
<th></th>
<th>CAB</th>
<th>FCC</th>
<th>FMC</th>
<th>FPC</th>
<th>FTC</th>
<th>ICC</th>
<th>NRC</th>
<th>SEC</th>
</tr>
</thead>
<tbody>
<tr>
<td>RESPONSIVENESS TO INDUSTRY</td>
<td>-.10</td>
<td>.26</td>
<td>.17</td>
<td>.59</td>
<td>-1.2</td>
<td>-.35</td>
<td>.7</td>
<td>-.45</td>
</tr>
<tr>
<td>RESPONSIVENESS TO CONSUMERS</td>
<td>-.47</td>
<td>-.52</td>
<td>-.61</td>
<td>-.73</td>
<td>-.77</td>
<td>-.20</td>
<td>-.86</td>
<td>.04</td>
</tr>
<tr>
<td>RESPONSIVENESS TO THE PRESIDENT</td>
<td>.71</td>
<td>.34</td>
<td>.46</td>
<td>.55</td>
<td>-.02</td>
<td>.14</td>
<td>.56</td>
<td>.42</td>
</tr>
<tr>
<td>RESPONSIVENESS TO CONGRESS</td>
<td>.06</td>
<td>.15</td>
<td>.11</td>
<td>.12</td>
<td>.30</td>
<td>.42</td>
<td>.03</td>
<td>.29</td>
</tr>
</tbody>
</table>

NOTE: Numbers in table cells represent the mean scores of a seven-point scale scored from -3 (unresponsive) to + (too responsive). 0 represents "right amount" of responsiveness. Thus, scores around 0 represent the "best" score a commission could have received. Acronyms are as follows: CAB, Civil Aeronautics Board; FCC, Federal Communications Commission; FMC, Federal Maritime Commission; FPC, Federal Power Commission; FTC, Federal Trade Commission; ICC, Interstate Commerce Commission; NRC, Nuclear Regulatory Commission; SEC, Securities and Exchange Commission.


presidents, such as Lyndon Johnson, stressed political favors and patronage; others, such as Dwight Eisenhower, relied more upon the background of applicants and their suitability for a specific job. In general, presidents have never taken an intensive interest in the staffing of agencies, often simply endorsing the recommendations of their chief domestic advisors.

There are some outstanding examples of purely political appointments, such as Nixon's nomination of Alexander P. Butterfield, who served as deputy assistant, was in daily contact with Nixon during the first term, and was suggested by John Ehrlichman, the president's chief domestic affairs advisor, for the Federal Aviation Administration. Butterfield later confessed, "I don't think I even knew [the FAA] was part of the Department of Transportation, just to show you how unfamiliar I was with the domestic realm." Butterfield's appointment had little to do with his qualifications, but he became part of a general strategy to place presidential assistants of demonstrated loyalty into the federal bureaucracy.36

The two crucial issues involved in personnel are their levels of expertise and the locus of their interest, that is, if they are able to take a broad view of regulation rather than speaking only for special interests. The quality of personnel varies over time and from agency to agency. A detailed study by the Senate Committee on Governmental Affairs reached this conclusion through a poll in which administrative law judges, lawyers appearing before these judges, lawyers appearing before regulatory commissions,
and members of the Administrative Conference of the United States were questioned (see Table 1.3). The committee concluded that the quality of personnel had improved between 1963 and 1971, but that it was by no means outstanding. In 1971, particularly singled out as relatively strong were the Civil Aeronautics Board, the Federal Maritime Commission, and the Securities and Exchange Commission, while the Federal Trade Commission and Nuclear Regulatory Commission were given lower ratings. Members of the Federal Trade Commission were seen to be especially ill prepared to participate at hearings (see Table 1.4).

### Table 1.4

**Comparative Ratings of Commissions**

<table>
<thead>
<tr>
<th></th>
<th>CAB</th>
<th>FCC</th>
<th>FMC</th>
<th>FPC</th>
<th>FTC</th>
<th>ICC</th>
<th>NRC</th>
<th>SEC</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Preparation to Participate at Hearings</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1971</td>
<td>-23</td>
<td>.08</td>
<td>.38</td>
<td>-.08</td>
<td>-.65</td>
<td>-.14</td>
<td>.15</td>
<td>.19</td>
</tr>
<tr>
<td>1966</td>
<td>-.02</td>
<td>-.15</td>
<td>.24</td>
<td>-.46</td>
<td>-.46</td>
<td>-.06</td>
<td>.49</td>
<td>-.24</td>
</tr>
<tr>
<td>1963</td>
<td>-.24</td>
<td>-.19</td>
<td>.21</td>
<td>-.54</td>
<td>-.29</td>
<td>-.28</td>
<td>.61</td>
<td>-.38</td>
</tr>
<tr>
<td><strong>Independence</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1971</td>
<td>.35</td>
<td>.06</td>
<td>.29</td>
<td>.03</td>
<td>-.32</td>
<td>.06</td>
<td>.21</td>
<td>.5</td>
</tr>
<tr>
<td>1968</td>
<td>.06</td>
<td>-.10</td>
<td>.19</td>
<td>-.54</td>
<td>-.42</td>
<td>-.09</td>
<td>.37</td>
<td>-.39</td>
</tr>
<tr>
<td>1963</td>
<td>-.27</td>
<td>-.11</td>
<td>.29</td>
<td>-.69</td>
<td>-.21</td>
<td>-.16</td>
<td>.25</td>
<td>-.15</td>
</tr>
<tr>
<td><strong>Competency</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1971</td>
<td>.50</td>
<td>.02</td>
<td>.46</td>
<td>-.15</td>
<td>-.70</td>
<td>.17</td>
<td>-.19</td>
<td>.39</td>
</tr>
<tr>
<td>1968</td>
<td>.05</td>
<td>-.35</td>
<td>.23</td>
<td>-.50</td>
<td>-.71</td>
<td>.10</td>
<td>-.09</td>
<td>-.72</td>
</tr>
<tr>
<td>1963</td>
<td>-.29</td>
<td>-.38</td>
<td>.4</td>
<td>-.45</td>
<td>-.46</td>
<td>-.33</td>
<td>-.13</td>
<td>-.44</td>
</tr>
</tbody>
</table>

**Note:** Numbers in table represent the mean scores of a seven-point scale scored from −3 (unresponsive) to + (too responsive). 0 represents "right amount" of responsiveness. Thus, scores around 0 represent the "best" score a commission could have received. Acronyms are as follows: CAB, Civil Aeronautics Board; FCC, Federal Communications Commission; FMC, Federal Maritime Commission; FPC, Federal Power Commission; FTC, Federal Trade Commission; ICC, Interstate Commerce Commission; NRC, Nuclear Regulatory Commission; SEC, Securities and Exchange Commission.

In the related issue of responsiveness to particular groups, the study lends some support to capture theory; regulators in the early 1970s remained more responsive to regulated industry than to consumers (though the situation subsequently changed with the advent of social regulation and deregulation). Yet, the conclusion must be modified in that it somewhat belies the statistics. Responses to a U.S. House Subcommittee on Oversight and Investigations questionnaire showed that of 1,917 upper-level personnel, only 262 had had prior employment in the industry regulated by their federal agency or commission. The same study found that while one-third of commissioners or administrators became involved with the regulated industries within five years after leaving office, most of them gained contact as legal counsel or consultant rather than through direct employment.37

Paul Quirk’s recent study, *Industry Influence in Federal Regulatory Agencies*, concludes that industry influence is neither consistent nor effective and that the data requires “skepticism toward the assertion that regulatory agencies tend to favor regulated industry interests.”38 Furthermore, federal ethics codes have strict requirements on the periods of time required after federal service before contact and employment with regulated industries is allowed (generally, one to two years). It should also be remembered that agency experience does not necessarily mean conflict of interest. Such experience may deepen an understanding of industry problems and functioning and allow individuals to recommend more realistic and effective regulations. Regulators also have professional affiliations. Often joining agencies as a means of furthering their standing, lawyers, economists, academicians, and other professionals tend to balance loyalties to a specific industry.

Several writers attempt to place agency personnel in various classifications based upon backgrounds, orientations, and roles. James Q. Wilson states that there are at least three types of employees, defined in terms of their motives: careerists, politicians, and professionals. Careerists are dedicated to the agency and identify their careers with it; politicians believe they have a future in government (in appointive or elective office) and see the agency as a stepping stone; and professionals receive their reward from membership in their profession—future employment may lie elsewhere, but is dependent upon agency performance.39

Anthony Downs sees five regulator types that are based upon personal goals and motivation: climbers, conservers, zealots, advocates, and statesmen. Climbers seek such self-interest goals as power, income, and prestige; conservers want security and convenience; zealots push for a distant policy that is connected to their own self-interest goals; advocates, also possessing self-interest goals, push for the broader goals of the agency; statesmen continually stress the goals connected to the benefit of society as a whole.40
A further distinction should be made in terms of personnel behavior based upon background. Those belonging to a profession are likely to express the perspective of that profession. An example would be the lawyer, who tends to see the world in an adversarial light, identifying distinct sides to an issue and looking for clear-cut outcomes. Another would be the economist, who is attuned to costs and benefits, seeking to put a program together, to synthesize rather than to identify support and opposition. The political scientist is geared toward political influences and forces; the career bureaucrat sensitive toward procedures and roles. Agency personnel who come from business organizations tend to be decision-oriented, to see the practicality and profitability of various courses of action as well as the necessity for planning. More than the other groups, they are likely to comprehend fully the difficulties of the regulated industries, though this does not necessarily mean conflict of interest.

There is no formula for ideal agency personnel, yet several guidelines are important, including some substantive background in the regulated industry as well as a demonstrated lack of conflict of interest. The former is somewhat easier to establish than the latter. Backgrounds in the regulated industries should come from different perspectives, from disciplines such as economics, law, ecology, technology, each decision maker being able to relate his or her perspective to the general interest of socioeconomic conditions. A blatant conflict of interest, such as stock holdings in regulated companies or corporate directorships, are easy to document. But actions with future intent are almost impossible to monitor, and therefore the matter spills over to issues of personal integrity. For this reason, the congressional confirmation process should be less routine and superficial; for example, funds could be appropriated for staff surveys of nominee backgrounds.

PUBLIC OPINION AND MOOD

In explaining social, political, and economic change, social scientists tend to emphasize either the large- or small-scale, macro or micro level of analysis. The micro level includes areas such as biography, microeconomics (the study of individual firms), and in general the individual components that make up a system, be they individuals, institutions, or procedural mechanisms. The macro level involves the factors involved in the total system functioning, such as culture, the behavior of large groups, ideology, public opinion and mood, and principles and dynamics that affect the society, the total environment. The macro level is actually composed from the micro level, though its total impact is never equal to the exact sum of the smaller parts.
Although we emphasize the interaction of all levels, it should be noted that the macro level has the potential to affect the regulatory system in major ways. Public opinion and mood is the overall outlook on society, the perception of conditions, and it holds with it predispositions either for change or for maintaining the status quo.

In general, this century has seen three periods when the American people were especially predisposed to change, in the mood to see societal alterations: the first two decades of the century (the progressive era); the New Deal in the 1930s, and the early and mid-1960s, during the Kennedy and Johnson administrations. It is clear that the theme of the 1980s so far involves change, but change of a different sort. The majority of the public is interested in a period of consolidation and retrenchment, in which government becomes more efficient and unnecessary governmental functions are eliminated. The mood involves a certain amount of fear and a desire to bring things such as “runaway inflation,” “bloated interest rates,” and “soaring crime rates” under control.

The actions and priorities of the federal government correspond in many ways to the changes in hopes or fears of the electorate. One poll of goals indicates an increase of concern during the 1970s for economic stability, personal wealth, and safety, as well as improved quality in government, while fears increased concerning economic stability, social decay, law and order, integrity in government, and the deterioration of the environment.41

A ranking of national problems indicates basic changes when 1965, 1970, and 1980 are compared. Concerns peaked in the areas of environmental pollution, helping the poor, reducing racial discrimination, and highway safety in 1970, and they increased substantially after 1970 in the areas of reducing crime and unemployment.42

On the basis of public opinion, the stage is currently set for a protracted period of deregulation during which the scope and importance of agencies will decrease. Whether this is an economically sound direction is one of the main issues this volume addresses and can best be answered on an agency-by-agency basis, as well as in a discussion of the underregulated economy (see Chapters 3-10).

Psychologist Robert L. DuPont uses the example of nuclear power to describe the ways in which fear works in the public mind and how it influences perceptions of regulation.43 DuPont describes the nature of such fear in terms of three basic principles. First, the most important consideration is whether the individual believes he controls the risk. When he feels he has an element of control and choice, he is less afraid. Second, fears are greater for those hazards that show up in a great event rather than a series of less dramatic events. And third, fear is a function of familiarity. An individual fears the familiar less, regardless of whether it is less dangerous than the unfamiliar. Thus, DuPont argues, people are more
afraid of nuclear power plants and jet airplanes than cars and cigarettes, even though far more people die because of the latter than the former. A person controls the car or cigarette by driving or choosing to smoke it, a car accident is not as spectacular as a jet accident, cigarette-induced cancer occurs very gradually over a long period of time, and people understand what cars and cigarettes are and how they function far better than nuclear energy or jet propulsion.

The principles of control, drama, and familiarity hold special implications for social regulations because they involve perception rather than reality, the reliance upon subjective experience over more detached assessment. Apparently, an issue must have a negative impact in all three areas in order to gain public attention. Food additives lack familiarity, for example, but their effects are undramatic, and they present the appearance of control, that is, people believe they have the ability to avoid them by diet choices (although this is not always the case). It is highly unlikely that public perception will coincide with objective risks.

In many respects, public opinion is similar to the question of bureaucratic organization: The existence of opinion is neither good nor bad in itself but depends on its content (the way organizations depend on individuals that run them). In this democratic society, where a major value is the importance of the will of the majority, a dilemma is posed when the popular will contradicts sound empirical analysis. This is one of the central conflicts in any democracy. It is easily demonstrated, for example, that American public opinion was more bellicose than the Carter administration during the Iranian hostage crisis of 1979 and called for actions more likely to cause war in the Middle East, actions based upon emotional responses to the crisis. Carter's more prudent position probably prevented an escalation of the difficulties.

The basic accommodation of the problem lies in the partial political insulation of regulatory agencies. Because they are involved in business matters requiring detachment and expertise, they operate somewhat more detached from the interface of public opinion and government than does, say, Congress. On the other hand, they do not lie entirely outside of politics and do not become a form of "technocracy" due to the controls of the government described in the preceding sections. These controls temper and indirectly express the public will through the legislation of an elected Congress, the direction of a popularly elected president, and the final authority of governmentally appointed courts.

REFORM

Regulation is a dynamic process, a process that is in a constant state of change. Alterations in government regulation of business may take two
basic approaches: first, changes of the structure and processes of the agencies themselves; and second, the assumption of agency functions by other offices of government. A series of studies of the regulatory system originating within the executive branch began when President Franklin D. Roosevelt established the Committee on Administrative Management, known as the Brownlow Committee. Becoming a part of the general Roosevelt effort to consolidate and expand the powers of the presidency, this report urged the abolition of independent commissions and their integration into the executive departments, where they could be coordinated and supervised by the president.

The first Hoover Commission (1947-1949) established by President Truman, was likewise critical of regulatory performance, but rather than abolition of the commissions, it argued for more authority for their chairmen. It also suggested an administrative management director in the Bureau of the Budget who would coordinate the various agency activities, watching for overlap and conflict of function. The second Hoover Commission (1953-1955) endorsed a clearer distinction within agencies between judicial and executive functions by increasing the independence of the hearing examiners and establishing a special administrative court, two suggestions that were never instituted.

John Kennedy commissioned a smaller-scale study by James M. Landis, who, reiterating the call of the Brownlow report, spoke of the necessity of overall presidential policy leadership by increasing the power of chairmen and their interaction with the president. Landis further proposed the creation of an executive office with an administrator responsible for all regulatory policy.

Another study originating with the president was conducted by Nixon's Advisory Council on Executive Organization, known as the Ash Council, named after its chairman, Roy L. Ash, who served as chairman of Litton Industries. The 1971 report includes an analysis of agency characteristics and problems, as well as proposals for change. The problem with commissions, according to Ash, are the essentially equal commissioners and their insulation from the executive branch so that only Congress can effect a major change. Ash describes a shortcoming that is similar to Theodore Lowi's description of vague mandates and ill-defined goals: Commissions do not really know what they are about. The result is often a redundancy of functions between agencies. In light of these problems, the Ash Council recommended a limitation to the number of commissioners, where possible replacing the commission by single administrators and placing the administrators within the executive branch, the limitation of intra-agency review by the creation of an administrative court, and the redistribution of agency functions in order to avoid redundancy.
Congressional committees are also responsible for studies on regulation, studies which oftentimes recommend reforms. For example, the Special Committee on Legislative Oversight under the chairmanship of Oren Harris, held fifty-two days of hearings during 1959 and 1960, and concluded that agencies should balance their sources of information so that they rely less on industry-supplied data. They should also establish and publish procedures and impose more consistent sanctions for violations. A House Subcommittee on Oversight and Investigations study of 1976 ranked the various agencies and concluded that the Interstate Commerce Commission and Federal Power Commission are the most in need of reform, while the Securities and Exchange Commission and Federal Trade Commission show the greatest signs of improved performance.

Some recommendations for reform come from private organizations such as the American Bar Association. In an extensive report in 1979, the ABA sought a greater emphasis upon market forces protected by antitrust regulation, greater agency review by means of executive orders from the president, economic impact statements, greater flexibility in procedure (including informal procedures for hearings and information gathering), speeding up the intra-agency review process, establishment of policy consultation boards, institution of deadlines for specific classes of activities, and sunset legislation requiring review and reauthorization periodically by the Congress (based on evaluations of the Office of Management and Budget and the General Accounting Office.)

The major proposals of all these groups have not been instituted. No super-regulatory office exists, nor does a separate administrative court system. Both commission and administrative forms of agencies still exist, and the chairmen have not been given substantial additional powers. Within this category of more modest reform involving alterations of existing structures, there have been several developments. Presidents Ford and Carter required inflation impact statements prior to the issuance of new regulations by two executive orders. And in October of 1978, President Carter instituted a regulatory council charged with the coordination of regulatory activities.

Political scientist David Welborn conceives of a typology of regulatory reformers. The traditionalist examines the abuses of economic power and seeks to improve agency functioning by periodic review, whereas the restrictivists are uncomfortable with government regulations and wish to cut back on government activity. The populists want to preserve agency regulation that achieves socially oriented goals and dismantle that which furthers corporate special interests.

By far the most interest for regulatory change currently lies in the area of deregulation and finding alternatives to agency control. The deregulation
impetus has already taken effect, Congress passing the Airline Deregulation Act of 1978, which terminates the Civil Aeronautics Board in 1985, as well as the Motor Carrier and Railroad Deregulation Acts of 1980, substantially deregulating those industries. Two proposals that are consonant with the deregulation drive are the legislative veto, which would allow Congress to veto individual regulatory actions, and sunset laws, which require periodic rechartering of agencies by Congress after a review and analysis. Congress in the past has established a veto over Federal Trade Commission actions. However, in June 1983, in the case of *Immigration and Naturalization Service (INS) v Chadha*, the U.S. Supreme Court surprised the country by ruling that the legislative veto was a power that Congress was not intended to have and was, therefore, unconstitutional. Although it is still unclear whether all legislative veto provisions have been struck down, there is no question that this decision will weaken Congress's ability to check the powers of the executive branch. In the area of government regulation, the Chadha decision will reduce Congress's power to directly interfere with the rules and regulations promulgated by the Federal Trade Commission and the Environmental Protection Agency, since previous legislation giving Congress such power is now in question. The regulatory process may also be indirectly affected by weakening Congress's power to prevent presidential impoundment of funds as well as its control over executive reorganization. At this time, however, it is too soon to appreciate all the implications the Chadha case may have regarding the regulatory process. One may speculate, though, that Congress will tread cautiously from this point on when delegating power, regulatory or otherwise, to the executive branch if it perceives of itself as no longer possessing as much control over executive branch actions as it has had in the past.

Supporters of deregulation suggest regulatory processes that entirely sidestep the regulatory agencies. One proposal is the reliance upon taxation to affect certain industry actions, such as a tax on polluters that surpasses the cost of not polluting the environment. Another approach is the change in liability rules, so that it is easier for consumers and workers to sue for damages created by services, products, or the work environment. Bargaining is presented as another alternative, whereby different groups such as consumers, management, and labor, perhaps mediated by government, make arrangements for specific cases. The disclosure approach emphasizes the importance of information, so that when products and services are registered, well labeled, and in other ways understood by consumers, the market will function properly without undue interference from government.47

The analysis of regulation indicates the complexity of the subject. Both criticism and support should take into account rationales for and against
the existence of agencies. It should consider theories of agency functioning and structure, addressing their relevance and limitations. Evaluations should also take into account economic costs and benefits, the quality and performance of personnel, the broad context of political and social mood, as well as the strength of proposals for reform.

The concepts in this chapter will aid in formulating questions rather than providing final answers. Chapters 2 and 3 on the performance of the economy and problems associated with overregulation and underregulation serve as further background for the sections on specific agencies that follow in Part III.

NOTES


6 Weidenbaum, Future of Business, p. 10.


8 An excellent treatment of the government as promoter of business appears in Martin C. Schnitzer, Contemporary Government and Business Relations
The Uncertain Balance


Analyzing Regulations


31 Weidenbaum, *Costs of Regulation*.


34 Office of Management and Budget figures.


44 A summary of regulatory reform studies appears in U.S. Congress, House Subcommittee on Oversight and Investigations, *Federal Regulation and Regulatory Reform*, 94th Cong., 2nd sess., October 1976; James M. Landis,

45 Executive Order 11821, November 27, 1974; Executive Order 12044, March 24, 1978.


PART II

Regulation and the Political Economy
Regulationists and deregulationists agree that competition is a central issue for the political economy. While a number of firms should exist for healthy rivalry to continue, a few firms may come to dominate a market in a condition of oligopoly; one firm may even gain control in a condition of monopoly. The degree of economic competition in the United States has varied over the years. When competition faltered during the early twentieth century, regulation in the area of antitrust intensified, and when a prolonged economic depression occurred during the 1930s, new agencies came into being as part of Franklin Roosevelt's New Deal. During the late 1970s, on the other hand, dips in economy performance signaled a decrease in regulation.

The existence of at least some government regulation of competition is part of the core regulation about which both regulationists and deregulationists agree. Part of the reason for this agreement lies in the nature of competition, which holds within it a paradox. Competition, albeit a positive economic force, holds the seeds of its own destruction: strong companies move to the forefront, but there is no guarantee of a continual supply of contenders. Thus, without government involvement, competition may eventually disappear. Only the few monopoly and oligopoly companies themselves would favor such a condition.

This chapter traces the “waves” or periods of mergers of firms as well as the types of business organization and practices associated with such activity and then discusses the debate concerning the optimal size of companies for the benefit of society as a whole.

MERGER MOVEMENTS AND PATTERNS

There have been three distinct periods of mergers in the twentieth century: 1897 to 1905 (which led to the establishment of the Antitrust Division of
the Justice Department and the Federal Trade Commission in 1903 and 1914; 1925 to 1929; and 1960 to 1969. The first wave was the most intensive and extensive, so much so that it transformed the structure of American business. The existence of a strong capital market and the institutions to make the capital available, as well as technological advances (especially in transportation and communication), allowed companies to expand on a greater scale than ever before.

A merger, the takeover of one or more corporations by another one, is effected in several ways. First, a firm may be in financial difficulty and thus spared total dissolution by being merged, or else profits will rise through merger, especially if a dominant market share is thereby gained. During this first wave of merger activity, single corporations controlled at least 90 percent of the market in areas such as cigarettes, sugar refining, tin can production, farm machinery, and kerosene refining. While total merger capitalization remained at $29.7 million for 1896, it ballooned to $650.6 million in 1898 and to $2,262.7 million in 1899. Finally, by 1913, single firms dominated enough to control the market in nearly 30 industries, including those that produced or processed asphalt, cotton, yarn, meats, gunpowder, and many other important commodities. By far the biggest merger was the creation of U.S. Steel in 1901 from over 80 mining companies, 40 manufacturing companies, over 30 transportation companies, as well as other concerns. The corporation controlled a total of over 200 plants.

The second merger wave, during the 1920s, peaked in 1928 and 1929, when 1,058 and 1,245 firms disappeared by merger, respectively. The greatest activity occurred in iron, steel, and machinery, followed by food and liquor, and finally petroleum and nonferrous metals. The mergers typically involved less capital than those during the first period, though they were greater in number. Firms merged that were not as related as those of the first period, forming conglomerates from suppliers, manufacturers, and distributors, or else diversifying in products within one industry, such as foods. More characteristic in this period are oligopolies, in which a few firms control the market, rather than monopoly, in which a single firm dominates.

Mergers increased steadily in the 1950s but increased sufficiently from 1967 to 1970 to create a third merger wave, when over one in five manufacturing and mining corporations with over $10 million in assets were acquired. The pace slowed in the early 1970s and 1976 saw yet another increase in activity. Another pattern in the 1960s is the number of oil companies involved in merger activities, during which 20 major firms acquired 20 major oil refiners, as well as corporations in nonpetroleum areas. The 1960s set a pattern of oligopoly, wherein the 4 largest firms
**Table 2.1**

**Merger Movement in American Industry, by Number of Firms and Capitalization, 1895—1910**

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Firms Disappearing by Merger</th>
<th>Merger Capitalization (Millions of Dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1895</td>
<td>43</td>
<td>40.8</td>
</tr>
<tr>
<td>1896</td>
<td>26</td>
<td>29.7</td>
</tr>
<tr>
<td>1897</td>
<td>69</td>
<td>119.7</td>
</tr>
<tr>
<td>1898</td>
<td>303</td>
<td>650.6</td>
</tr>
<tr>
<td>1899</td>
<td>1,208</td>
<td>2,262.7</td>
</tr>
<tr>
<td>1900</td>
<td>340</td>
<td>442.4</td>
</tr>
<tr>
<td>1901</td>
<td>423</td>
<td>2,052.8</td>
</tr>
<tr>
<td>1902</td>
<td>379</td>
<td>910.8</td>
</tr>
<tr>
<td>1903</td>
<td>142</td>
<td>297.6</td>
</tr>
<tr>
<td>1904</td>
<td>79</td>
<td>110.5</td>
</tr>
<tr>
<td>1905</td>
<td>226</td>
<td>243.0</td>
</tr>
<tr>
<td>1906</td>
<td>128</td>
<td>377.8</td>
</tr>
<tr>
<td>1907</td>
<td>87</td>
<td>184.8</td>
</tr>
<tr>
<td>1908</td>
<td>50</td>
<td>187.6</td>
</tr>
<tr>
<td>1909</td>
<td>49</td>
<td>89.1</td>
</tr>
<tr>
<td>1910</td>
<td>142</td>
<td>257.0</td>
</tr>
</tbody>
</table>


controlled 100 percent of the primary aluminum industry, 97 percent of locomotive manufacturing, 94 percent of telephone and telegraph equipment, 92 percent of electric light bulb production, and 91 percent of motor vehicle production.6
Table 2.2
Yearly Time Series of Merger Activity in Manufacturing and Mining, 1919–1930

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Disappearances</th>
<th>Merger Values (Millions of Dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1919</td>
<td>159</td>
<td>777.4</td>
</tr>
<tr>
<td>1920</td>
<td>163</td>
<td>809.4</td>
</tr>
<tr>
<td>1921</td>
<td>70</td>
<td>430.0</td>
</tr>
<tr>
<td>1922</td>
<td>122</td>
<td>501.8</td>
</tr>
<tr>
<td>1923</td>
<td>143</td>
<td>1,171.1</td>
</tr>
<tr>
<td>1924</td>
<td>149</td>
<td>466.0</td>
</tr>
<tr>
<td>1925</td>
<td>257</td>
<td>720.7</td>
</tr>
<tr>
<td>1926</td>
<td>265</td>
<td>1,135.0</td>
</tr>
<tr>
<td>1927</td>
<td>306</td>
<td>727.4</td>
</tr>
<tr>
<td>1928</td>
<td>507</td>
<td>1,653.2</td>
</tr>
<tr>
<td>1929</td>
<td>587</td>
<td>1,993.3</td>
</tr>
<tr>
<td>1930</td>
<td>281</td>
<td>1,756.8</td>
</tr>
<tr>
<td>Total</td>
<td>3,009</td>
<td>12,142.1</td>
</tr>
</tbody>
</table>


The Anatomy and Process of Monopoly and Oligopoly Control

Business Organization

There are several types of consolidation: First are the horizontal mergers, whereby control is sought in a specific market or industry. Second, vertical mergers involve acquisitions in which the firms furnish different goods or services but are in the same "flow" of production, such as oil transportation and oil refining companies. Finally, conglomerate mergers are those that involve neither the same market nor flow of production, but unrelated goods and services, such as the merger of a business machine.
Table 2.3

Mergers in Manufacturing and Mining Involving Firms with Assets of $10 Million or More, 1960–1976

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Acquisitions</th>
<th>Assets of Acquired Firms (Billions of Dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960</td>
<td>51</td>
<td>1.5</td>
</tr>
<tr>
<td>1961</td>
<td>46</td>
<td>2.0</td>
</tr>
<tr>
<td>1962</td>
<td>65</td>
<td>2.3</td>
</tr>
<tr>
<td>1963</td>
<td>54</td>
<td>2.5</td>
</tr>
<tr>
<td>1964</td>
<td>73</td>
<td>2.3</td>
</tr>
<tr>
<td>1965</td>
<td>64</td>
<td>3.3</td>
</tr>
<tr>
<td>1966</td>
<td>76</td>
<td>3.3</td>
</tr>
<tr>
<td>1967</td>
<td>138</td>
<td>8.3</td>
</tr>
<tr>
<td>1968</td>
<td>174</td>
<td>12.6</td>
</tr>
<tr>
<td>1969</td>
<td>138</td>
<td>11.0</td>
</tr>
<tr>
<td>1970</td>
<td>91</td>
<td>5.9</td>
</tr>
<tr>
<td>1971</td>
<td>59</td>
<td>2.5</td>
</tr>
<tr>
<td>1972</td>
<td>60</td>
<td>1.9</td>
</tr>
<tr>
<td>1973</td>
<td>64</td>
<td>3.1</td>
</tr>
<tr>
<td>1974</td>
<td>62</td>
<td>4.5</td>
</tr>
<tr>
<td>1975</td>
<td>59</td>
<td>5.0</td>
</tr>
<tr>
<td>1976</td>
<td>81</td>
<td>6.3</td>
</tr>
</tbody>
</table>


corporation with a food processor. The first merger wave consolidations were primarily of the horizontal type, the second wave both horizontal and vertical, and the third conglomerate in addition to horizontal and vertical.7 The basic business form that allows for and is oriented to expansion is the corporation. In the individual proprietorship, the owner is subject to unlimited liability for losses or damages and has some difficulty obtaining capital for expansion since he must rely on his personal resources. Difficulties also arise upon the death of the owner in that the business has...
no existence beyond the life of the owner (unless special arrangements are made). The partnership form allows for the combination of more capital, but the liability and continuance problems are the same as for the individual proprietorship.

The corporation may sell shares to investors and obtain capital for expansion, each shareholder holding limited liability for losses or damages that may not exceed the amount of the investment. Shares may be bought and sold, ownership rights of stock may exist indefinitely, and shareholders may vote for a board of directors, each share of stock representing one vote for its owner.

While there is nothing inherent in the corporate form that works against competition, several forms of business organization involving corporations did emerge that threatened competition. First, the pool is an (informal or formal) agreement between producers of goods or services to share sales, customers, territories, or profits. By doing this, firms hope to eliminate the competition that could lead to price reductions or increased costs of doing business. One type of such an arrangement is the "conference" type, or gentlemen's agreements, whereby there are no sanctions for failure to abide. A more formal type of pool is the clearinghouse, whereby a central office monitors and reports upon member compliance, a function fulfilled by the American Wall Paper Company from 1880 to 1888, for example. Finally, the disciplinary pool, such as the Southern Railway and Steamship Association, provides for penalties for noncompliance. Pools became widespread in the 1870s, especially among the railroads, but almost disappeared in the latter part of the nineteenth century.

To a certain extent, pools fell because of weaknesses in their operation. Their problem is mainly political and analogous to activities at the United Nations. Because each member holds sovereignty, compliance is not only contractual but, in fact, voluntary. The force of competition, firms trying to gain an edge, managed to make itself felt. Hard times, such as the depression of 1893-1895, strained pool discipline and tempted some to step outside of the agreements in order to ensure their own survival.

By the 1880s, trusts had replaced pools as the major anticompetitive form of business organization. In trusts, stockholders with a controlling interest in the firms of an industry agree to entrust their shares to individuals known as trustees in return for trust certificates. The certificates are based upon equitable interest, or reflective of the value of stock held.

The trust idea was initiated by John D. Rockefeller and his associates, when they formed the Standard Oil Trust in 1879. Rockefeller, believing that competition creates waste and works against fair profits and economic stability, combined the resources of various companies within Standard
Oil. While control remained with nine trustees, the concept involved formal legal arrangements that preserved the individual company entities in spite of the centralization of their control. The trust entity became powerful enough to lower prices, drive out competition, and then raise prices once the consumer's options became limited.9

As with pools, trusts held the prospect of their own decline, since agreements became formal and written and contradicted common law and many state statutes. The dissolution of the trusts gave rise to the holding company as the principal form of anticompetitive organization. Holding companies own the assets of other corporations, assets that are in turn used in the purchase of other companies. Firms controlled by the holding company are considered its subsidiaries. Since a bare majority of shares is required for controlling interest in a corporation, a pyramid effect is created, where, say, $1.00 of stock can control $1.99 in the subsidiary, and then $3.99 in the next subsidiary, or a nearly fourfold increase in control of the original dollar.

Economically, the holding company is similar to the trust, but legally, the certificates of the trust become stock of the holding company, the board of trustees becomes the board of directors, and the trust relationship is replaced by a permanent transfer of stock.10

Holding companies became legitimized, in part, because of the competition among the individual states to attract business. As a way of bringing business into the state, New Jersey added a holding company clause to its corporate law as amended in 1893, which explicitly legitimized the concept.11

While the holding company epoch began about 1899 and peaked by 1904, amalgamation and mergers eventually became the dominant form of reducing competition. A merger is a consolidation whereby one business is absorbed by another that retains its existence, while an amalgamation is the combining of a group of organizations that lose their individual identities entirely. In general usage as well as for our own purpose, merger applies to amalgams as well, which are considered a type of merger—a formulation consistent with all the statistics cited in this chapter.

Control of Price, Sales, and Entry

The purpose of the Federal Trade Commission is to ensure "vigorous, free, and fair competition in the marketplace." Just what constitutes fair competition is an economic and ethical value judgment that reflects historical experience. In the pursuit of minimizing competition, pools, trusts, holding companies, and mergers all have engaged in a series of methods involving price, sales, and entry (conditions influencing the
entrance of new firms into the marketplace), some of which have been declared illegal and all of which are carefully monitored and regulated.

Price may be affected by devices external to the demands of the market itself, devices that are almost always detrimental to the economy as a whole. In 1904, Ida Tarbell published an exposé of the Standard Oil Company in which she charged many shady practices by that company in the area of price manipulations.12 Our interest is in the practices she described rather than the extent of their perpetration by Standard Oil. Tarbell described methods such as the bribing of purchasers in client companies in order to induce them to halt orders from competing companies. She also quoted a study of the company Scofield, Shurmer and Teagle of Cleveland that demonstrated the differences in Standard Oil prices in competitive and noncompetitive areas. There, prices were temporarily lowered in order to drive out competing oil companies. Predatory pricing of this nature, Tarbell claimed, went on to the extent that Standard set up "bogus" companies that sold on or below cost, drove out the competition, and then disappeared from existence themselves. To Tarbell, it all came down to a matter of ethics. The business community needed to develop a clear set of standards as well as their own methods of punishing those individuals who violate them, offering the kind of censure "the athlete who abuses the rules receives."

One of the more common forms of price discrimination is the basing point system. According to this procedure, prices are set according to delivered price, which is the sum of the base price and "phantom" freight charges, charges determined "as if" the product were produced at a particular location. The system began when U.S. Steel charged by rates from Pittsburgh, regardless of whether the product originated from points closer to the consumer. When the rest of the industry agreed to price according to these methods, U.S. Steel was thereby protected from price competition and canceled out the factor of locale in the competitive process. As production expanded, U.S. Steel eventually set up basing point cities in Birmingham, Alabama, Gary, Indiana, and Los Angeles, California.

Mention has already been made of price discrimination, or predatory pricing, whereby a firm sets its rates according to the existence or nonexistence of competition with the long-term strategy of raising rates after the competitor is driven out of the market. The measure is especially suited to large firms, since they can afford to wait out the competitive periods and can draw funds from other areas should they be diversified in more than one product or service.

Yet another form of price discrimination is price fixing, which may take the form of either (a) collusion between business firms to set prices or (b) price leadership, wherein, as in the case of U.S. Steel, one firm sets the price.
Some states have promoted the artificial establishment of minimum rates by preventing discounting by retailers through resale price maintenance laws. Price-fixing attempts have often taken the form of trade association policies, secret industrywide agreements, and professional association actions.

Competition is also hindered by sales actions in the marketplace. Preemptive buying involves the hoarding of all the supplies and resources needed to produce a product or service, regardless of whether the buyer needs them. Railroads bought up lands for this purpose, and more recently, the Alcoa Aluminum Company attempted to buy up bauxite deposits in order to deny their use to competing manufacturers.

According to reciprocal agreements, firms agree to do a certain amount of business with each other in advance, and one or both firms threaten to cancel orders unless its own goods or services are purchased. This is not considered inherently unfair, unless competition is substantially affected. In exclusive sales arrangements, manufacturers deal with distributors and retailers only if they agree not to handle the competitors. In finalizing agreements, companies require the purchase of additional products or services as a condition of sale of the original item.

While firms have an interest in reducing the number of competing firms, they also have an interest in keeping the number down by control of the entry process. Entry is a general term applying to the process of entering the market. Entry into a market usually applies to new firms, but it may also apply to firms that are initiating products or services in new areas for those firms. Firms are dependent upon a variety of factors in the entry process, such as sources of capital, availability of physical resources, and a means of marketing. One means of controlling entry is in the area of patents. The federal government grants patents guaranteeing exclusive control of articles and processes for 17 years as an incentive to invention, but patents may be manipulated to the detriment of the competitive process. A firm may receive a patent on a modified version of the original form in order to retain control, or it may acquire competing patents with no intention of putting them into production, but with the idea of preventing competitive production instead. Finally, firms on occasion simply duplicate patent claims, which usually leads to extensive litigation.

Price discrimination and buying practices are also used to prevent the entry of new firms. When a producer hears of a business plan or observes a product introduction, he may temporarily lower prices, as mentioned. An alternative response would involve making the kinds of agreements that are detrimental to the new company; these include reciprocal agreements and preemptive buying. Huge advertising campaigns or even product misrepresentation may be launched when the market threatens to offer a new competitor.
RATIONALES AND SCALE

Brandeis and Croly

The notion of scale refers to the size and scope of business firms. Size indicates the quantitative aspects of the firm, the amount of capital, machinery, and inventory, the number of employees. The scope of a firm is the qualitative range of its activities, the number of products and services, the fields in which it is involved. The question of scale in business organizations first became a major issue in national politics during the first two decades of the twentieth century. Eventually, the thinking on size centered around two individuals, jurist Louis D. Brandeis, who became the spokesman for the Wilsonian Democrats, and Herbert Croly, spokesman for the Roosevelt Republicans and Progressives. Brandeis attacked bigness on ethical, economic, and political grounds. He felt that firms become large only through the types of questionable practices described above; he referred to a "curse of bigness," arguing that firms make up for the inherent economic disadvantages of size by the compromise of ethics in the pursuit of power. The issue of size becomes political in that it involves the distribution of wealth and control in society, which is at the heart of the political process. To Brandeis, mergers are even less desirable than pools, for example, in that they destroy entirely the identities of the smaller subsumed organizations. Brandeis supported government-imposed price floors because they serve to protect smaller businesses.\(^{13}\) The only alternative to the hegemony of large companies, Brandeis felt, was the establishment of rules to ensure fair competition, and he therefore endorsed the establishment of the Federal Trade Commission.\(^{14}\)

On the other hand, Herbert Croly associated excellence with the large corporation. Although he too endorsed the Federal Trade Commission Act in 1914, along with Brandeis, he did so for entirely different reasons.\(^{15}\) To Croly, the increase in the size of business organizations was as inevitable as biological evolution, and even some private monopolies could prove to be desirable. Because large-scale business was not by nature evil, but could do evil, it had to be regulated by the state. An adequate program called for, not the regulated competition of Brandeis intended to keep size under control, but regulated combination ensuring the socially beneficial functioning of growing corporations.

Productivity and Size

What, then, is the status of competition and firm size, and how does it relate to the regulatory system? Economist Walter Adams accurately
writes, "The unit of technological efficiency is the plant, not the firm... A firm producing such divergent lines as rubber boots, chain saws, motorboats, and chicken feed may be seeking conglomerate size and power; it is certainly not responding to technological necessity."\textsuperscript{16}

It is important to keep in mind that few individuals endorse the elimination of government antitrust activity. The arguments, rather, lie in the degree and intensity of antitrust regulation. Those interested in a relaxation of antitrust efforts generally point to the notion of economies of scale. The prototype for the modern economy of scale, in which a larger organization is preferable to a smaller, is the railroad. In railroads, the longer the trip and the greater the number of cars on the train, the lower the cost of transportation per unit becomes. Large scale may also lend itself to the effective and efficient division of labor, as first illustrated on a grand scale by the Henry Ford production lines. Another economy of scale is the possibility of large orders, which make the long production run possible: the plant runs day and night, and the ratio of "off" to "on" time is reduced. The large firm may also invest in research and expensive high-technology equipment. In the area of purchasing, the large organization may receive quantity discounts and benefit from higher priority from suppliers. The theory of the large firm proceeds further to hold that, due to greater productivity, larger firms are in a good position to expand, and they therefore push the economy as a whole forward, continually producing new jobs and making more efficient use of resources.

Those who are more enthusiastic about activist antitrust activity question these conclusions. They believe that the oligopoly is actually a shared monopoly. Ralph Nader associate Mark Green defines such a shared monopoly as a situation in which four or fewer firms control 50 percent or more of the market. In this situation, a few firms have market control and watch each other closely, so that when one company announces a price increase, the others follow with identical pricing. Rather than a pattern of increased value and productivity, Green holds, size is associated with inflated prices.\textsuperscript{17}

The antitrust argument continues that oligopoly contrasts to more competitive conditions, in which a large number of sellers offer comparable products to buyers who have knowledge of the product or services, and firms can make decisions independently and enjoy free entry and exit.\textsuperscript{18} Huge firms make entry and exit in the marketplace more difficult and, with the advent of huge advertising budgets, are more likely to create demand through psychological manipulation than are smaller businesses with smaller promotion budgets. Economist Roger Sherman concludes in his study of oligopoly that the fewer the number of firms, the easier it is to control price and entry, and that concentration could be reduced substantially without any reduction in productivity. Sherman adds that a
firm with large market shares is more reluctant to expand because it may reach a state of inelastic (nonexpanding) market demand sooner and may have to create more total demand.19 Those arguing for active antitrust regulation also indicate that huge organizations are more likely to engage in the questionable business practices described earlier in this chapter than are smaller ones, including pooling, price discrimination, and manipulation of the conditions of sale.

Competition and the scale of firms are several issues that have engendered debate. Regulationists and deregulationists, of course, disagree as to the appropriate balance between government intervention and freedom of action for business. Those enthusiastic about regulation specify a series of problems associated with what they term underregulation, whereas those who are skeptical about regulation identify problems associated with intensive agency activity, which they term overregulation. Chapter 3 treats in detail these sets of problems.

NOTES

7 Blair, Economic Concentration.
12 Tarbell, *Standard Oil Company*.
CHAPTER 3
Problems of Underregulation and Overregulation

There are no simple answers to regulatory difficulties because problems exist in both intensive and less intensive regulatory contexts. The first section of this chapter lists what regulationists term specific needs created in relatively less regulated situations. These needs are divided into the areas of business methods and practices, protection of the individual, and protection of the environment. The second section is an account of problems associated, according to the deregulationist view, with intensive regulation. The problems lie in the areas of the costs of running agencies, the costs of complying with agency rulings, and compromises in business innovations and expansions.

PROBLEMS OF UNDERREGULATION

Business Methods and Practices

Many questionable business practices were described in Chapter 2, including pooling, price discrimination, and manipulation of the conditions of sale. Another problem associated with business consolidations is the centralization of economic power. By 1911, the five largest investment banks controlled about 22 percent of the total banking resources of the country. This translated into great power for individuals, the most notable of them being J. P. Morgan, whose company was represented on the board of directors of 32 corporations. Although Morgan and Company had total deposits of $162 million in 1912, they controlled deposits in other concerns of $1.2 billion.\(^1\) Although the United States remained a political democracy, regulationists point out, it began to become an economic plutocracy, with power individuals deciding where money should be invested and what types of businesses merited funding, thereby affecting the socioeconomic fabric of the nation.
Another problem indicated by regulationists is the transfer of securities. Stocks, especially during the boom of the 1920s, were often misrepresented, that is, the consumer never learned the true status of the companies in which he invested. Insiders with exclusive information could manipulate the market. Credit practices and transaction terms fostered market instability, rather than reflecting educated investment decisions based upon sound capital and not overextended credit. Yet another area is hiring practices, where firms determine the social composition of the economy by hiring on the basis of race, religion, or gender.

Individual Protection

Those seeking to justify regulation protecting the individual often refer to a colorful incident in which Theodore Roosevelt supposedly ate a sausage while reading *The Jungle* by reporter Upton Sinclair, an exposé of unsanitary practices of the food industry. Roosevelt jumped up, yelling, "I've been poisoned!" and threw the food out of the White House window, hitting a Secret Service agent on the head.

Food and drugs is pointed out as one of the first areas covered by protective government regulation. Precedents date back to the Middle Ages and before, such as when King John of England passed the first English food law, in 1202, proclaiming the adulteration of bread with ingredients such as ground peas or beans to be illegal. Massachusetts enacted the first general food law in the United States in 1784, and in 1848, after finding quinine shipped to U.S. troops in Mexico for malaria treatment to be adulterated, Congress passed the first federal law ensuring the quality of a drug. Even though the U.S. Department of Agriculture investigated food adulteration and Congress introduced over 100 food and drug bills during the last quarter of the nineteenth century, the problem remained so acute that Congress enacted a comprehensive Food and Drugs Act in 1906, prohibiting interstate commerce in misbranded and adulterated foods, drinks, and drugs. The same day it also passed a meat inspection act.

In spite of the act and its administration by the Bureau of Chemistry, and later the Food and Drug Administration (in 1931), the problem remained acute. The Supreme Court allowed medicine producers to continue their lofty claims, and an inadequate testing process led to the loss of 107 lives by the consumption of the "elixir of sulfanilamide" in 1937. Although in 1938 Congress gave the Food and Drug Administration the power to preclear new drugs, underregulation in this area allowed for the near approval of thalidomide, which caused severe birth defects and infant deaths in Europe in the 1950s. Active regulatory vigilance is so required
that in the period of 1973-1975 the FDA estimates it removed 47 million pounds of adulterated food from human consumption.2

The problem especially calls for centralized and expert research, say regulationists, because of the number of unknowns involved with food and drugs. Food involves a long chain beginning with the farm, where pesticides may affect its safety, leading to its transport and retailing, during which time it is susceptible to spoilage. Drugs react differently in combination, so that the consumer needs to be informed of their proper use. The long-term effects of drugs require constant study.

Another example of direct protection of the individual is the area of occupational safety and health. Since the days of child labor in the nineteenth and early twentieth century, when hazardous conditions directly caused workers' deaths or destroyed their health, the issue continues to be a problem. In 1970, the year the Occupational Safety and Health Act was passed, job-related accidents accounted for more than 14,000 worker deaths, nearly 2.5 million new worker disabilities, and an estimated 300,000 new cases of occupational disease.3 In following years, worker health remained a problem, although the situation improved. Reported injuries and accidents were close to 17 per 100 full-time employees in manufacturing in 1971, and they decreased to about 15.5 in 1973, and 13.5 in 1976.4

Environmental Protection

A form of protective regulation that protects the individual somewhat less directly than the above examples is regulation of the environment. The question arises as to whether firms produce more harm by their impact on the environment than they do benefit from their goods and services.

The scope and intensity of the problem of industrial waste materials in recent years is difficult to grasp. Synthetic organic chemical production is especially problematic for the environment, since it is energy-intensive (i.e., production requires a high degree of energy) and there are always byproducts that are not easily reused or processed into the environment. Between 1945 and 1970, there were enormous increases in mercury consumption, synthetic chemical production, and chlorine production; mercury consumption nearly doubled in the last five years of that period.5 Between the years 1947 and 1972, automobile emission became an intensified problem, the number of passenger cars increasing from over 30 million to nearly 96 million.6

Hazardous waste disposal has particularly attracted the attention of Congress. One research scientist testified at a congressional hearing that in the South Brunswick Township in New Jersey, a small community of
18,000 people, 20 cases of toxic waste dumping, which contaminated the water, were discovered; a single industrial firm polluted 525 million gallons of drinking water, a seven-month supply for the town, with merely 500 gallons of industrial solvents. In 1978, residents on the Love Canal in Niagara Falls, New York, began to smell unpleasant odors in their basements. Dioxin, a highly carcinogenic substance, was found in alarming quantity, requiring expensive cleanup and causing yet to be determined health damage. Yet, the Love Canal, though receiving the most media attention, is not unique. The Environmental Protection Agency had discovered health threats in about 100 of more than 600 inspected waste sites by June of 1980.

Even the oceans have not escaped pollution. Ocean dumping has increased, culminating in a high for 1973. The market price of fish—both fresh and salt-water—has skyrocketed and drinking water has required additional vigilance. Land around polluted waters must be monitored for toxic seepage.

Regulationists often bring up the example of nuclear energy because of both its drama and the potential hazards involved in its use. While it should be emphasized that nuclear energy represents a unique aspect of the economy, one that is not representative of problems of other areas of energy production, it does pose severe problems. The effects of radiation are especially toxic because it cannot be overtly detected by the human senses (except in massive doses), its effect is long-term and cumulative, and radioactive materials remain dangerous for long periods of time. Radioactive damage may not only affect the individual but by affecting the chromosomes, future generations as well. Another difference from nonnuclear waste is the toxicity of tiny amounts, atom for atom, radioactive lead being 20 million times more toxic than nonradioactive lead.

Inventories of radioactive waste have grown to the point of doubling every three to four years. At the same time technical uncertainties remain, such as the durability of containers, the earthquake resistance of nuclear plants, the intrusion of groundwater into waste sites, and even terrorist activity.

Thermal pollution is yet another problem resulting from nuclear energy. Shortly after the opening of the power station at Indian Point, New York, in 1963, thousands of dead striped bass were found in the Hudson River. Nuclear power plants are only 30 percent efficient, 30 percent of the energy becoming electricity and 70 percent being wasted as heat, heat which is removed from the plant by circulating cold water. Many forms of fish sicken or die in reaction to even slight changes in water temperature since heat changes the oxygen levels in water.
Nuclear accidents demonstrate other regulatory problems inherent in nuclear power production. The most publicized incident to date was the Three Mile Island accident of March 1979, when a pump failed to function and the operators on duty made the mistake of turning off the emergency cooling system. The reactor heated up dangerously and threatened to melt to the core. The accident proved that the industry is underregulated to the point that personnel are not adequately equipped to handle emergencies and equipment is subject to breakdowns. Siting is not completely rational either; plants often exist near heavily populated areas, and nuclear wastes are often transported through metropolitan areas.\(^\text{11}\)

**PROBLEMS OF OVERREGULATION**

While agreeing that many of the above problems and dangers should be addressed by some form of government regulation and could be a part of a core of justified regulation, deregulationists believe that the dangers do not justify the current extent of regulation. Regulation, they say, has grown into a massive web that touches almost every aspect of society.

**The Scope of Regulation**

Deregulationists point to three distinct periods of regulatory growth, each of which has penetrated deeper into the functioning of the economy. The first occurred during the first 16 years of the twentieth century, when five agencies and departmental divisions were created in the areas of antitrust, monetary policy and banking, trade, coastal regulation, and tariffs. With the New Deal came a new wave of regulatory activity in banking, food and drug regulation, credit, communications, corporate securities, maritime regulation, agricultural consumption and marketing, and air flight. Finally, from 1970 to 1973 there was a surge of regulatory activity in the areas of environmental protection, credit, highway safety, occupational safety, employment standards, consumer product safety, drug enforcement, and energy administration. Recent regulatory activity, sometimes termed new-style social regulation,\(^\text{12}\) moves beyond specific business decisions to the quality of life and social composition of society.

Besides the breadth of coverage, deregulationists stress the degree to which the internal operations of companies are affected by regulation. In regulated industries, almost every corporate activity, from the board room to the mail room, is now touched upon by the federal government. Beginning with top management, the board of directors reports directly to the Securities and Exchange Commission about security offerings,
financial reporting, and accounting. In research and development, the Consumer Product Safety Commission watches over the design and content of products, and the Occupational Safety and Health Administration and the Environmental Protection Agency monitor the functions of manufacturing plants and service facilities. Specific products, such as drugs, food, transportation equipment, and home appliances, are highly regulated. Marketing is controlled in many areas. The Federal Trade Commission handles representation in advertising. Product labeling is monitored by the Federal Trade Commission, the Food and Drug Administration, the Consumer Product Safety Commission, and other agencies that monitor special consumer warnings, readability, and content descriptions. Sales, pricing, and profits are all carefully regulated. Labor regulations pose requirements on hiring practices, wage and working conditions, promotions, and employee benefits. Virtually every mode of product transportation is regulated, and in this age of computers, so is the electronic transmission of information. The form of corporate organization is regulated by federal antitrust activity, which seeks to monitor and control the number of firms in particular industries and the areas of their activities.13

Deregulationists indicate that agency regulation is so intensive, many of them often become involved in one issue. The regulation of ethylene oxide (a chemical used in crop fumigation as well as in medical equipment sterilization) illustrates this process. The National Institute for Occupational Safety and Health and the Occupational Safety and Health Administration are both concerned with health hazards to the workers involved in the manufacture and application of the substance. The Food and Drug Administration considered action concerning the residues left by the material on drugs and medical devices, and the Environmental Protection Agency investigated the impact of the chemical on the environment. The National Coal Association reports that at least 12 executive departments and independent regulatory agencies have regulatory power over the coal industry.14 Likewise, pesticides must be registered with the Environmental Protection Agency; if they are purchased for home use, they are regulated by the Consumer Product Safety Commission, but for commercial uses they are covered by the Occupational Safety and Health Administration.15

An extremely complex case of shared agency power is that of the Nuclear Regulatory Commission. A series of NRC memoranda of understanding, dated from August 1980 to November 1981, detail specific agreements between the NRC and other major regulatory organizations. This is useful as an illustration of the complexity of modern technology in our contemporary economy. The transport of radioactive materials brings the Department of Transportation into the picture. One agreement places
responsibility for transportation of nuclear materials with DOT, but responsibility for the "receipt, possession, use, and transfer of byproducts, source, and special nuclear materials" with the NRC. The Department of Labor is involved in issues of worker safety. Yet another agency, the Environmental Protection Agency, handles the protection of the environment around nuclear power plants from radiation and contaminated materials. A Federal Emergency Management Agency, along with the other agencies involved with NRC, steps in during crises, such as the recent Three Mile Island incident. The Department of Energy monitors production levels and prices.\textsuperscript{16} The NRC works closely with the Justice Department in the area of monopoly and antitrust. The NRC Regulatory Guide calls for the attorney general's advice on matters of licensing and the avoidance of monopoly.\textsuperscript{17} This is just a sample of the interactions of various agencies on the same issue of nuclear power.

In sum, deregulationists believe that problems associated with the scope of regulation relate to overexpansion of the number and functions of agencies, much of which occurred during the early and mid-1970s, the most active time of agency formation. Figure 3.1 illustrates the growth of agencies during the past century. Deregulationists believe that the growth of agencies and their expansion of functions is detrimental primarily because of the resulting impact upon costs, costs to the private and public sectors.

The Costs of Regulation

Deregulationists divide the costs of regulation into three levels: primary costs, the costs of establishing and maintaining the agencies; secondary costs, the direct costs to businesses of complying with regulations; and tertiary costs, the costs to businesses and consumers due to increased operating expenses incurred in secondary costs.

Primary costs are reflected in the federal budget. In the area of social regulation (consumer safety and health, job safety and working conditions, the environment and energy), expenditures increased 760 percent from 1970 to 1979, and in the area of economic regulation (finance and banking, general and industry-specific rules), expenditures for the same period increased 171 percent.\textsuperscript{18} In 1970, regulatory budgets totaled $866 million; for 1982 they totaled over $5.5 billion. In 1970 dollars (adjusted for inflation), the 1982 figure is still over $3 billion.\textsuperscript{19} At the same time, the public debt portion of the federal budget increased from over $300 billion, to over $800 billion.\textsuperscript{20} Agency budgets are indicated in Table 3.1.
Secondary costs, or compliance costs, are too high, according to deregulationists. They quote various studies, such as one by the U.S. Council on Environmental Quality that estimates nationwide pollution abatement expenses to be $26.9 billion for 1978. The council believes that at the current rate of increase the costs will rise to $64 billion by 1987. The Center for the Study of American Business calculates the indirect costs of compliance to be about 20 times greater than the direct costs, defined as agency operating budgets, and concludes that the total issuance and compliance of all federal regulations comes to $126 billion for fiscal year 1980, or over $500 for every person in the nation.21
### Table 3.1

**Expenditures by Federal Regulatory Agencies for Fiscal Years 1974–1980**

**(Millions of Dollars)**

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<td>49</td>
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<td>90</td>
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<td>11</td>
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<td>180</td>
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<td>345</td>
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<td>51</td>
<td>54</td>
<td>61</td>
<td>68</td>
<td>68</td>
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<tr>
<td>All other</td>
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<td>83</td>
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<td>122</td>
<td>147</td>
<td>120</td>
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<tr>
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<td>2,834</td>
<td>3,268</td>
<td>3,597</td>
<td>4,062</td>
<td>4,862</td>
<td>5,782</td>
<td>6,041</td>
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</table>

**Note:** Dash indicates not applicable.

Business Week reported the same trend in 1977, determining a total regulatory figure of $100 billion—equal to 5 percent of the gross national product and 25 percent of the total federal budget. Of this total, $85 billion is seen as compliance costs, $25 billion of which pays for paperwork and company administrative costs. The need for manpower is so intense that corporations are reorganizing in order to handle the challenge, in many cases establishing and expanding government relations departments and hiring public affairs information managers who deal with the agencies. In 1976, the most labor-intensive reporting requirements were for the Federal Communications Commission (48,076,930 labor hours), the Nuclear Regulatory Commission (4,918,480 labor hours), the Federal Aviation Administration (3,065,138 labor hours), and the Federal Energy Administration (7,845,900 labor hours).

The perception of the business community is that compliance costs became more demanding between 1977 and 1979. According to one survey, 92 percent of executive respondents found compliance costs had increased, 48 percent claiming somewhat more and 44 percent believing somewhat more.

Compliance costs hit small businesses especially hard, and the Carter administration found it necessary to create exemptions. In 1977, the Labor Department's Occupational Safety and Health Administration exempted workplaces with 10 or fewer employees from its jurisdiction. In July 1979, Carter issued a memo requesting that agencies “tailor requirements to fit the size and nature of the businesses and organizations subject to them.” A subsequent memo urged a decrease in paperwork, and Congress followed with the Paperwork Reduction Act of 1980, which cut down substantially on required forms, and the Regulatory Flexibility Act of 1980, which allows agencies to tailor requirements according to the scale of enterprises involved. The Environmental Protection Agency exempts most companies from record keeping if total waste is less than 1,000 kilograms per month; the Federal Trade Commission requires no advance notification of some small mergers; and the Securities and Exchange Commission has reduced disclosure and auditing standards on stock offerings under $5 million.

In the area of tertiary costs, deregulationists state that the compliance costs of regulation compromise productivity and business innovation. They indicate that regulation is related to the decrease in the annual growth rate in the gross national product, which declined from a rate of 6 percent in 1976 to 2 percent in 1979. One analysis concludes that the redirection of investment capital from production to regulation has reduced GNP growth by one-quarter to one-half of a percentage point a year. Although improvements in technology allowed for a continual increase in productivity per labor hour, the rate of labor productivity increase went down for the period 1961 to 1979 compared to 1950 to
1979.\textsuperscript{29} In the area of innovation, deregulationists indicate that technology and research development has become compromised due to intensive regulation. The outstanding example of this, they say, is a "drug lag" in the pharmaceutical industry. During the past 15 years, drug discoveries in less-regulated Great Britain have outpaced American ones, as exemplified in the area of cardiovascular drugs.\textsuperscript{30}

As stated in Chapter 1, the costs of regulation must be measured against the costs of not regulating in order to determine a more balanced measure of costs. A consideration of problems associated with both intensive and less intensive regulation demonstrates that regulation is always a question of balance. There are rarely benefits without accompanying costs, and the full range of costs and benefits must be measured in every specific instance. The search for appropriate levels of regulation is a continual theme in the experience of every federal agency. Just how regulatory agencies have dealt with this challenge is the subject of the next section, which examines the nature and performance of ten major agencies.

\section*{NOTES}


16 Nuclear Regulatory Commission, Memoranda of understanding compiled August 1, 1980, to November 27, 1981.


24 Special tabulation by the General Accounting Office and Office of Management and Budget.


PART III

Federal Regulators
CHAPTER 4
Antitrust Division, Department of Justice

The Antitrust Division of the Department of Justice is unique among federal regulators in that its activities center about the judicial process. Antitrust activity is grounded in law, and although case selection is left to the discretion of the division, outcomes are dependent upon the federal court system. For this reason, we shall address the statutory basis of antitrust activity and major cases interpreting the legislation. We shall also describe the division's organization and functioning, its relationship to the regulatory system, and its importance to the economy as a whole.

EARLY HISTORY AND LEGISLATIVE AUTHORITY

Sherman Antitrust Act of 1890

Senator John Sherman first brought an antitrust bill to Congress in 1888 in response to a coalition of farmers of the South and West, labor unions, and small businessmen, all of whom were hurt by industrial consolidation. In his arguments for the passage of the bill, Sherman referred to inequities of opportunity and condition and the development of economic autocracy.1

In substance, the act is general but represents the first formal statement by the federal government on the necessity of controlling business consolidation. Although divided into eight sections, the major portion of the bill appears in the first two. The first section declares illegal "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce." Section 2 indicates that "every person who shall monopolize or attempt to monopolize, any part of interstate or foreign commerce is guilty of a misdemeanor." The other six sections address themselves to court jurisdictions and procedures, defining
"person" to include corporations and associations, and assigning to the attorney general the right of enforcement through civil proceedings, which led to the formation of the Antitrust Division in 1903.2

Beginning in 1904, Congress passed appropriations for antitrust enforcement each year, but the division began modestly and tentatively, largely due to lack of enthusiasm of the attorneys general. An assistant attorney general headed the Antitrust Division, but the attorney general could determine the basic scope of its operations and indicate the approximate case load considered appropriate. The average antitrust caseload was less than 1.5 between 1890 and 1904, and though it rose to an average of 31 between 1910 and 1914, it dropped to about 11 a year through the 1920s. The case load would not rise until the late 1930s, when Thurman Arnold became assistant attorney general in charge of the Antitrust Division. In one year, Arnold increased the number of attorneys in the division from 59 to 144, added economists to the staff, instituted a section to screen cases in order to focus better the schedules of attorneys, and combined economic with legal analysis in the formation of cases. During the 1950s and 1960s, the division would further increase its caseload, improve the quality of its staff, and go after some huge cases, the outcome of which would affect multibillion-dollar corporations.

The Sherman Act initially failed to achieve its stated purpose due to its scope. Since it was limited to interstate commerce and foreign trade, intrastate commerce remained uncovered by a uniform national law. In 1890, only 13 states possessed antitrust laws, and though by 1900 30 states had passed such laws, state enforcement became lax; in practice, antitrust activity remained the responsibility of the federal government. Second, the act was oriented toward conduct and not structure, that is, it outlawed the act of forming monopolies but not monopolies in themselves.3

Also of significance are the limitations imposed by judicial interpretation, which during the early years after the passage of the act reflected more the interests of big business than the coalition that led to its existence. A major case involving the Sherman Act is United States v. E. C. Knight Co. (1895).4 While producing 65 percent of the nation’s refined sugar, the American Sugar Refining Company purchased the entire stock of the E.C. Knight and Company and three other Pennsylvania corporations by agreement with the stockholders and managements, bringing the company’s total market control to about 98 percent.5 The court ruled that the merger was not in violation of the Sherman Act because it involved manufacturing concerns rather than interstate commerce. Manufacturing, the court added, precedes commerce, and Congress may only regulate trade and commerce between states, not manufacturing within a state.
Yet, several cases did follow that offered judicial legitimization to the Sherman Act. The Addyston Pipe case reached the Supreme Court in 1899. Along with five other corporations, the Addyston Pipe & Steel Company engaged in a pooling arrangement by dividing the United States into three areas, within which exclusive sales territories were arranged. The court ruling supported the Justice Department's application of the Sherman Act by stating that, although the firms did engage in manufacturing, the pooling was illegal because it affected sales and delivery of pipes across state lines. Nevertheless, the message of the Knight and Addyston cases to business was that while independent manufacturing firms could not conspire to fix prices, they could still merge and thereby control the market.

Corporations continued to consolidate, and the Northern Securities Company case came up in 1904. The Northern Securities Company was formed as a holding company with stock in three huge railroads—the Northern Pacific, Great Northern, and Chicago, Burlington, and Quincy. By only a five-to-four vote, the Supreme Court ordered the holding company dissolved for being in restraint of trade.

In 1911, the Supreme Court ordered two major monopolies dissolved. In the Standard Oil case, the court ordered the Standard Oil trust divided into a series of companies, each entity remaining supreme in its own area. In the American Tobacco case, the court divided the American Tobacco Company, which had controlled about 75 percent of cigarette production, into three companies, largely because of its practice of selective price cutting. The trend, culminating in these two cases, did not proclaim the end of trusts, however, but rather established a "rule of reason" that distinguished desirable from undesirable trusts. Size and power was not enough in itself, and the proof of predatory acts became a condition for trust dissolution.

In the Trenton Potteries case of 1927, the court established the rule of per se illegality. According to this concept, acts in themselves rather than acts in specific context are illegal. In the Trenton case, the court found price-fixing agreements to be such per se illegality. An extremely important decision that changed the entire approach to consolidation was the Aluminum Company of America case of 1945. The court went beyond its previous rulings when it held that ALCOA violated the Sherman Act in attempting to control 90 percent of the domestic virgin ingot market in aluminum, even though such attempts did not contribute to exorbitant profits. For the first time, the court finally declared the mere possession of monopoly power in general to be illegal; this amounted to the per se illegality of monopoly. In a famous statement, Judge Learned Hand defined illegal monopoly as control of more than 65 percent of a given market. The ruling should not be misinterpreted as the complete
restoration of competition to the American economy, but rather as the establishment of minimum competitive standards.

Clayton Antitrust Act of 1914

By 1914, and especially in light of the Supreme Court's weakening of the Sherman Act in the Knight decision, Congress acted to prevent specific unfair business practices. Rather than taking the general approach of the Sherman Act, Congress delineated actions that lead to restraints of trade in an attempt to eliminate the uncertainty surrounding the previous legislation. The act referred to many of the practices described in Chapter 2, such as price discrimination, tying agreements, and interlocking directorates. Its provisions may be divided into two categories: prohibition of business practices; and remedies against such abuses. There are five major business practice provisions:

1. Prohibition of the acquisition by one corporation of the stock of a competing corporation. Holding companies could not acquire stock in two or more corporations where competition is thereby lessened or a monopoly is created. An individual, however, could still hold controlling stock in two or more competing corporations.

2. Prohibition of interlocking directorates in competing firms capitalized at over $1 million, where the same individuals serve on the board of directors of two or more competing corporations.

3. Prohibition of tying contracts (making sales conditional on purchasing associated products) and exclusive dealing arrangements, where one firm induces another not to deal with its competitors.

4. Prohibition of price discrimination where the effect lessens competition, such as primary-line discrimination, where discrimination involves geographic price differentials.

5. Exemption of labor unions from prosecution under federal antitrust laws. 12

In terms of remedies, the Federal Trade Commission (see Chapter 6) was given joint authority for enforcing the major areas of the act, including tying contracts, exclusive sales arrangements, and interlocking directorates. In addition, private citizens may initiate civil suits with the potential payment of three times the amount of actual damage. Finally, the U.S. government may initiate suits, and fines and prison terms may be sentenced against individual directors or officers of corporations.

The Clayton Act proved to be more successful in the restraint of unfair business practices than in seriously affecting the pattern of corporate
mergers. The courts proved to allow mergers much more readily than to approve the other practices delineated in the act. It became clear that the Clayton Act held several important weaknesses. First, although companies could not own stock in competing firms, nothing in the act prevented a firm from acquiring other types of assets. Also, the act failed to make agreement to as well as perpetration of an unfair business practice illegal. These problems were addressed in subsequent legislation, which is described below.

The Strengthening of Antitrust Law

In 1914, when Congress passed the Clayton Act it also passed the Federal Trade Commission Act, which established the Federal Trade Commission (FTC) to work along with the Antitrust Division of the Justice Department in matters of fair business practice and antitrust (see Chapter 6). The first major amendment to the Clayton Act was the Robinson-Patman Act, passed in 1936. The Robinson-Patman provisions apply to both buyers and sellers. It becomes just as illegal to receive the benefit from price discrimination, for example, as to offer it as a seller. The statute created three types of price injuries: injury to competitors of the seller; injury to competitors of the buyer; and injury to competitors of the customer of the buyer. Price differences among purchasers could only be justified when based upon proven differences in costs, which the FTC was authorized to investigate and determine. However, sellers could also refuse to give discounts, even when justified by lower costs.

The following year, the Miller-Tydings Act exempted resale price-maintenance agreements from the Sherman Act in states in which they are allowed. By price maintenance, manufacturers attempt to control prices charged by resalers. The act weakened antitrust by raising prices above general market levels, and Congress repealed resale price-maintenance agreements in 1976.

In 1950, the Celler-Kefauver Act was passed to plug the loophole in the Clayton Act. Lenient judicial interpretation of section 7 of the Clayton Act allowed firms to acquire assets (as opposed to stock) in competing firms. Celler-Kefauver amended section 7 to include stock and assets and strengthened the antitrust law to prohibit a merger if it added to a trend toward concentration in an industry, thereby creating a tendency to monopoly.

No new antitrust laws or amendments followed during the 1950s and 1960s, but during the third merger wave of the 1960s, interest in antitrust revived, and the 1970s saw a significant amount of antitrust activity. The fair trade amendments to the Sherman Act, which allowed manufacturers
to control retail prices, were repealed. The Antitrust Procedures and Penalties Act of 1974 set up a system for antitrust consent decrees and changed the penalties for Sherman Act violations from misdemeanors to felonies. Offenses became punishable by fines of up to $1 million for a corporation, and penalties of up to $100,000 and three years' imprisonment for individuals. The Crime Control Act of 1976 authorizes the division to improve the state of antitrust enforcement through the provision of federal funds.\textsuperscript{15}

In 1980, Congress passed the Antitrust Procedure Act, which allows antitrust trials to move more quickly and cheaply through the court system. Judges' discretion becomes expanded in determining the payment of trial costs, and judges are granted discretion on interest charges for penalties. It also grants the Antitrust Division power to order more materials prior to litigation and clarifies the procedures by which the division employs outside data processing services.\textsuperscript{16}

But by far the most important antitrust act in recent years is the Hart-Scott-Rodino Antitrust Improvements Act of 1976.\textsuperscript{17} The act was sufficiently controversial politically that an effort to filibuster it was narrowly defeated. It has three provisions:

1. The Antitrust Division may obtain information relevant to antitrust violations from individuals and third parties as well as from corporations. The information may be in the form of documents as well as oral and written testimony.
2. The federal government must be notified in advance of all mergers of companies with more than $100 million in sales or assets and of the acquisition of all companies with more than $10 million in sales or assets.
3. The attorneys general of the 50 states may sue antitrust violators for triple damages on behalf of injured consumers in their states. The money first goes to the state and is then subject to compensation for individual damages.

Essentially, corporations must notify the Federal Trade Commission and Antitrust Division at least 30 days before an acquisition is consummated. The procedure allows the government to review the plan quickly and to determine whether or not to seek a preliminary injunction to prevent the action. During the first year of the implementation of the program, the Antitrust Division received 859 applications, investigated 101 of them, and challenged 9.\textsuperscript{18}

Although the procedure allows for greater vigilance by the Antitrust Division (and the FTC), the two pages and 2,000 words of the original statute became translated into 100 pages and 100,000 words of regulations,
written by the FTC with Antitrust Division concurrence. The paperwork became a strain for both business and the government, and the government began to allow more than warranted time for reviewing the insignificant cases. Businessmen concerned with the costs of government paperwork requirements note that a higher capitalization limit for notification could significantly cut costs for business. It could also, they suggest, aid the government by keeping the focus on the more significant cases.19

Much of the antitrust law became interpreted in some landmark cases involving the Antitrust Division. The DuPont case of 1956 involved a vertical merger, dating back to 1919, when the DuPont Corporation acquired 23 percent of the General Motors stock.20 Since DuPont supplied General Motors with materials, as General Motors grew in size, the issue became whether the effect was anticompetitive. The Supreme Court determined that the expansion of the corporation did hinder competition, and it ordered DuPont to sell its General Motors stock.

The Brown Shoe case of 1962 is a landmark case involving both horizontal and vertical dimensions. When the Brown Shoe Company acquired the Kinney Shoe Company in 1955, the Justice Department challenged the action on the basis that the resulting 2.3 percent control of total retail shoe outlets would discourage the entry of competitors. Vertically, competitors would hesitate to sell their goods in Kinney retail outlets. On a horizontal basis, in some areas, the market control amounted to 51.8 percent for men's shoes and 57.7 percent for women's shoes, even though the combined companies only produced 5 percent of the total shoe production. Brown was forced to sell Kinney, which was sold to the F. W. Woolworth Company.

After a conspiracy to fix prices and rig bids in the sale of electrical equipment to utilities, the Justice Department brought suit on violations of the Sherman Act. The Electrical Equipment case of 1961 involved 29 different companies, after consumers had paid millions of dollars in inflated utility rates.21 Because of treble damages provided by the Clayton and Sherman Acts, a total of $1.9 million in fines was levied against companies and executives. Since the Sherman Act provides for both fines and jail sentences, seven executives served 30 days in prison.

Two more recent cases illustrate the scope of the economic stakes involved in antitrust matters: the ITT and IBM cases. The ITT case was initiated in 1969 by the Justice Department after an intensive period of merger activity by International Telephone and Telegraph between 1960 and 1970, during which time it increased its assets by about $4.4 billion.22 Conglomerate mergers involved companies in such disparate areas as electrical equipment, automobile rentals, book publishing, construction, baking, chemicals, and insurance.
The ITT case tested for the first time antitrust law on conglomerate mergers. The Justice Department challenged three acquisitions in the areas of vending machines, sprinklers and power plant piping, and fire and casualty insurance. The case addressed the competitive conflict between sprinklers and fire insurance as well as the damages to competition created by geographical market domination and the control of financial resources. The court ordered ITT to divest itself of all interest—direct or indirect—in each of the areas.

The other huge case did not bear such results for the Justice Department. It demonstrates the difficulties in directing protracted litigation in a changing economy. The Justice Department accused IBM of announcing products for delivery far before their availability, creating tying agreements, and engaging in price fixing. It claimed that IBM selectively introduced computers with very low profit margins in order to drive out competitors and offered discriminatory terms in favor of educational institutions. But the case was dropped early in 1982, mainly because of changed market conditions. Foreign manufacturers have recently taken a sizable share of the American computer and business machine market, and many smaller American firms have proliferated recently as well.

ORGANIZATION AND FUNCTIONS

The Antitrust Division is organized along industry lines, with sections in areas such as transportation, consumer affairs, energy, and special regulated industries. In addition, an operations office coordinates trials, litigation, and enforcement, and sections exist for planning and evaluation. These functions are reinforced by field offices in eight major cities (see Figure 4.1).

Case selection involves a process of evaluating premerger notification reports, citizen and consumer complaints, as well as information in the press and leads gathered from personal contacts of staff attorneys and administrators. The staff attorney view is that information is important, and so they claim to be open to a broad range of sources. Because of the stringent requirements of antitrust law, preliminary investigations are often detailed and drawn out, including detailed reports of company histories and market performance.

Section chiefs distribute the areas of investigation, amend briefs and recommendations, recommend salary and promotion changes, and serve as liaison between the attorneys and the upper levels of the organization. The office of the director of operations assigns the work to the proper division. The assistant attorney general (the head of the Antitrust
Antitrust Division, Department of Justice

Figure 4.1

Antitrust Division, Department of Justice

Division), along with his assistants and deputies, plays the same role with the section chiefs as they do with the staff attorneys. The assistant attorney general can alter policy by reorganizing the sections and placing the emphasis upon particular areas, but any attempt to guide operations too much from above typically meets with staff resistance and lowered morale. In part, this is due to the nature of antitrust research, which, in order to be effective, should not be overly restricted in its selection of materials and areas.

A Ralph Nader study group on antitrust enforcement found undue outside influence in the division, citing 32 examples. The Nader group continued to characterize the division as subject to political influence, especially by the practice of attorney general review, whereby the attorney general makes the wishes of the president felt, who may want to filter out politically troublesome cases. The Nader group concluded:

The review given a case is usually brief and ad hoc. Yet why do antitrust cases go up at all? Neither tax nor civil nor criminal cases routinely need attorney general approval. Why just antitrust? Because it’s sensitive. . . . The other reason is that it acts as a control mechanism. At the same time an assistant attorney general, on his own authority, can dismiss a case. Thus, the whole setup is structured against filing cases.

Yet most other critics conclude that the record of the Antitrust Division—the quality of its personnel and its caseload—belies such a conclusion. They respond that occasional presidential intervention is a reflection of the Antitrust Division’s position within the executive office of the Justice Department rather than of its inherent weakness. Although in 1971 President Nixon did attempt to prevent the division from proceeding with its actions against ITT, such, they indicate, is the exception rather than the rule. Most studies of comparative effectiveness of the Federal Trade Commission and the Antitrust Division favor the latter, citing superior decision-making apparatus and better personnel. Antitrust Division attorneys are especially influenced by the professional antitrust bar, which holds high standards of conduct for its members.

It is clear, however, that the division has not been entirely economical. While the number of cases and staff less than doubled between 1970 and 1980, the budget increased over five times (see Tables 4.1 and 4.2). Although much of the funding includes grants to the states for antitrust activity, this only began in 1977 and accounts for only $1 million in fiscal 1977 and $10 million for 1978 and also for 1979.

One important aspect of Antitrust Division functioning is its involvement with other regulatory offices. It is especially involved with the Federal Communications Commission, the Interstate Commerce Commission, and the Nuclear Regulatory Commission. In the case of the
TABLE 4.1

ANTITRUST DIVISION BUDGET AND STAFFING,
FOR FISCAL YEARS 1970–1980

<table>
<thead>
<tr>
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<td>BUDGET $(MILLIONS)</td>
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<td>12</td>
<td>13</td>
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<td>22</td>
<td>26</td>
<td>36</td>
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<tr>
<td>STAFFING</td>
<td>595</td>
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<td>856</td>
<td>907</td>
<td>920</td>
<td>977</td>
<td>939</td>
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</table>

NOTE: Budget figures are for antitrust enforcement and include grants to states for enforcement.


NRC, for example, the Antitrust Division receives a copy of construction permit applications for nuclear power plants for antitrust review. The attorney general then either recommends a hearing or not, so that antitrust issues may be resolved. Another example of interagency activity is the Antitrust Division's enforcement of the Food, Drug and Cosmetic Act. In several instances, the division defended the Food and Drug Administration's regulations of generic drugs and manufacturing practices.

One of the most important ongoing difficulties in the division's functioning is the establishment of clear merger guidelines, so that businesses will have an idea of which of their merger decisions will legally survive and so that the law may be applied with equity. Since 1968, when merger guidelines were objectified, market share acceptability became specified. The division would challenge the following market shares for horizontal mergers, with four-firm concentration ratios of 75 percent or more:

**ACQUIRING FIRM**

- 4 percent
- 10 percent
- 15 percent

**ACQUIRED FIRM**

- 4 percent or more
- 2 percent or more
- 1 percent or more

For vertical mergers, the guidelines indicate that the division would challenge when the supplying firm has 10 percent or more of the market share.
### Table 4.2

#### Federal Antitrust Cases Commenced


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<tr>
<th>Year</th>
<th>TOTAL</th>
<th>CIVIL</th>
<th>CRIMINAL</th>
<th>ELECTRICAL EQUIPMENT</th>
<th>INDUSTRY</th>
<th>OTHER*</th>
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<td>315</td>
<td>60</td>
<td>27</td>
<td>—</td>
<td>228</td>
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<tr>
<td>1961</td>
<td>441</td>
<td>42</td>
<td>37</td>
<td>—</td>
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<tr>
<td>1962</td>
<td>2,079</td>
<td>41</td>
<td>73</td>
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<td>1,507</td>
<td>42</td>
<td>30</td>
<td>—</td>
<td>1,435</td>
<td></td>
</tr>
<tr>
<td>1979</td>
<td>1,312</td>
<td>50</td>
<td>28</td>
<td>—</td>
<td>1,234</td>
<td></td>
</tr>
<tr>
<td>1980</td>
<td>1,535</td>
<td>39</td>
<td>39</td>
<td>—</td>
<td>1,457</td>
<td></td>
</tr>
<tr>
<td>1981</td>
<td>1,434</td>
<td>60</td>
<td>82</td>
<td>—</td>
<td>1,292</td>
<td></td>
</tr>
</tbody>
</table>

**Note:** Despite the overall decline, private antitrust filings rose significantly in the federal district courts in New York City (up 45 percent to 144), Brooklyn (up 89 percent to 51), and Massachusetts (up 50 percent to 51). Private cases pending in all districts totaled 2,749 as of June 30. New York City led the pending list with 207 cases, followed by Chicago (167), Philadelphia (156), New Orleans (137), Houston and San Francisco (130), and Los Angeles (116).

**Source:** *Trade Regulation Reports*, No. 522, 1982.

*Includes antitrust cases transferred under Title 28 U.S.C. Section 1407.
*Includes 26 cases transferred under Title 28 U.S.C. Section 1404(a).
*All cases were transferred under Title 28 U.S.C Section 1404(a).
and the purchasing firm accounts for 6 percent or more of the total purchases of that market, unless there are no barriers created to market entry.

Yet, a study of actual cases indicates that the division does not entirely adhere to these standards. Since 1968, the FTC and Antitrust Division prosecuted cases falling below the guidelines in 21 percent of horizontal and vertical cases of a total case sample of 162.31

During the Reagan administration, the Antitrust Department began to reevaluate the guidelines seriously. William F. Baxter, head of the division, proposes an alternative approach to antitrust, which holds that the emphasis should remain on consumer prices and not on the percentage of market control held by a company. Limits to size, then, are determined by the marketplace and not a government office. Conglomerates become too big when they produce diseconomies of scale, and vertical mergers are considered procompetitive, since they lower costs. Only horizontal mergers are closely watched, but with more leniency than indicated by the current merger guidelines. Baxter indicates preference for the Herfindahl Index, whereby the market shares of the top companies are first squared and then added up. According to current methods, for example, where four top companies each have 15 percent of the market share, there is a concentration level of 60 percent. It also equals 60 percent if one company has 54 percent and the other three each have 2 percent. Four shares of 15 percent according to the Herfindahl method is an index of 900, below the 1,000-level danger point. But if one company has a share of 54 percent, the index is far beyond the acceptable limit.32

Another proposal for new guidelines is specification of not only those mergers the government is likely to prosecute but also of those that are likely to be safe as well. Currently, the division only has been willing “in certain circumstances to review proposed business conduct and state its enforcement intentions.”33

Division changes must be evaluated in light of the competitive functioning of the economy as a whole. To date, the Antitrust Division has managed to mitigate effects of merger “waves” that occurred during the past century. While public awareness is not always keen to the negative potentials of consolidation, the division continues to monitor such plans, set limits on the seemingly continual consolidation drive in a competitive economy, and attempt to set at least general guidelines of acceptability. The division must set a fine balance between the overregulation that could prevent the economic growth of corporations and the underregulation that could allow for firm domination and, ultimately, consumer and general economic hardship. The same basic qualitative criteria for mergers, though, remain: the preservation of competition; the productivity of firms; and the long-term viability of industries and economic growth.
The regulation of business consolidation is shared by the Antitrust Division with the Federal Trade Commission, the subject of Chapter 6. Whether the situation creates redundancy or effectiveness will become clearer with an analysis of the FTC.

NOTES

8 *U.S. v Standard Oil of N.J.*, 221 U.S. 1 (1911).
12 38 Stat. 730.
14 49 Stat. 1526.
17 90 Stat. 1383.

27 Weaver, “Antitrust Division,” p. 149.


CHAPTER 5
Interstate Commerce Commission

In 1980, Congress passed the Trucking and Railroad Deregulation Acts, two major pieces of legislation that substantially altered the impact of the Interstate Commerce Commission on the transportation industry. After tracing the early history, legislative authority, organization, and functioning of the commission in terms of the transportation industry, we will present critiques on the impact of deregulation both on the commission and on the regulated industries it affects.

EARLY HISTORY AND LEGISLATIVE AUTHORITY

By 1880, when 93,000 miles of railroad existed (the number would double by 1900), a history of business abuses had already been established. Railroads engaged in selective rate setting by cutting prices to drive out the competition and then, when they possessed geographic monopoly control, draining communities with high rates. Railroads also discriminated in charges for long hauls and short hauls, deviated from published tariffs, and gave rebates to preferred shippers and localities.

Farmers and small businessmen began to exert pressure for government regulation, and railroad regulation became a part of the platform of the powerful agrarian organization known as the Grange. Beginning in Illinois, the states took action, Illinois creating a warehouse and railroad commission to fix maximum rates for freight and passenger service as well as for storage services within the state in 1871. The same year, Minnesota legislated maximum freight and passenger rates, which were enforced by a state railroad commissioner. Iowa followed with similar legislation in 1874. Munn v. Illinois, in which a grain elevator owner challenged the state's right to control maximum storage charges, established the state's
legal basis for such action, but the railroads exerted a sufficiently powerful impact upon state legislatures (mainly because of their economic power) to gain modification of the regulatory laws. The state approach, too, proved inadequate since it did not cover interstate transport. The case of *Wabash v. Illinois* strictly forbade states to regulate in this area.2 This case, along with the difficulties of some 25 state regulatory apparatuses to effectively control abuses, intensified the pressure on Congress to involve the federal government.3

**The Interstate Commerce Act of 1887**

The nature of the transportation industry tends to confirm the notion that support for the ICC Act was diverse and not simply restricted to small business and farmers. Some businessmen in competing modes of transportation, such as waterway transportation, found the disparate rates confusing and were often hurt by the railroad rate wars and discriminatory pricing. Some large shippers did not receive preferred rates if they happened to be active in noncompetitive areas. In addition, the railroad companies that had lost the rate wars sought increased price stability. Therefore, support cut across various levels of business, depending on the positioning of the individual firms in a relatively chaotic market structure.4

The main provisions of the ICC Act are as follows:

1. Creation of the Interstate Commerce Commission with five members serving six-year terms. Commissioners are appointed by the president and confirmed by the Senate.
2. Prohibition of short-and long-haul rate differentials for shipments on the same line in the same direction.
3. Prohibition of pooling of the market and the division of profits by individual railroads.
4. Required publication of freight and passenger rates, with advance notice of changes (at least ten days).
5. Administration of the law by the ICC, along with the initiation of investigations of common carriers and the hearing of complaints.5

Unfortunately, the commission soon ran into trouble. Entirely dependent on the court system for enforcement of its rulings, the ICC had difficulty obtaining information from company managers and compelling testimony. Throughout the 1890s the Supreme Court observed a narrow interpretation of the ICC Act that minimized the commission's powers and eventually reduced it to a fact-finding body. Of the 16 decisions on rate
cases before the Supreme Court between 1887 and 1905, the Court decided in favor of the carriers in 15 and for the ICC only in 1. More disturbing to the regulatory process is the delay caused by such litigation, since the average case took four years to proceed through the court system. Then came the final blow, when the Supreme Court decided in the Cincinnati case that "Congress has not conferred upon the Commission the power of prescribing rates either maximum or minimum or absolute."7

The Early Amendments: Hepburn and Mann-Elkins

The Hepburn Act of 1906 marks the beginning of effective federal railroad legislation. Partly in reaction to the vigorous support of President Theodore Roosevelt for a law giving the ICC explicit power to fix maximum rates (subject to court review), Congress passed a multifaceted law. The Hepburn Act forbids preferred treatment to individuals by the issuance of free passes, grants the ICC power to declare rates unjust and set maximum levels, allows the commission to prescribe uniform accounting practices, increases the number of commissioners from five to seven, and extends the commission's power to the regulation of certain pipelines. The key clause is on rate making. Railroads were given 30 days to comply with rates set by the ICC. Should a company contest the rates in the courts, they remained in effect until a decision was forthcoming.8

The act strengthened the commission's position, but when rates increased in 1909 and the dockets of the circuit courts became full with carrier appeals, it became clear that a further strengthening of the ICC's legislative authority was necessary.

Although President William Howard Taft introduced a bill more sympathetic to business interests, he eventually supported the bill that emerged from a congressional conference committee known as the Mann-Elkins Act.9 The act, passed in 1910, tightened up the ICC's regulatory powers by further regulating short- and long-haul rate discriminations, by prohibiting predatory pricing against water carriers, and by giving the commission power to suspend a rate increase pending hearings for up to 10 months. It established a Commerce Court to expedite the appeals process and defined telephone, telegraph, cable, and wireless companies as common carriers, and therefore under ICC jurisdiction.

The Pattern of Legislation

The legislation that followed Mann-Elkins indicates a pattern of increased ICC involvement and power. (The implications of this power—whether it served the interests of the carriers or the public—is discussed in the
The Transportation Act of 1920 allows the commission to set both minimum and maximum rates and to approve the "consolidation of existing lines," which brought the ICC into the area of mergers, a field it had previously not entered. This act also required ICC approval for construction and operation of new lines and abandonment of old rail lines.10

During the 1930s, the ICC became involved with the regulation of motor carriers, the Motor Carrier Act of 1935 dividing the trucking industry into three classes of carriers: common, contract, and exempt.11 Certificates describing services and routes became required of common carriers (those available to the public). Contract or specialized service shippers had to obtain permits, and finally, a category of unregulated carriers remained, such as those carrying goods owned by the carrier itself and those in selected industries, such as agriculture.

Activities continued to expand in the 1940s, the ICC now regulating coastal, intercoastal, and inland water carriers and becoming involved in collective rate-making bargaining procedures. During the 1950s, the ICC was given power over more intrastate rate-making. An exception to the expansion of power occurred in the 1960s, when safety issues came under the aegis of the Department of Transportation, but in the 1970s, the commission was given authority to establish minimum standards of adequacy of rail service and to establish a Rail Services Planning Office for regional railway reorganization and development.

The watershed year for the continual expansion of ICC powers, though, is 1976, with the passage of the Railroad Revitalization and Regulatory Reform Act.12 The act reduced the degree of rail regulation by allowing management more leeway in adjusting rates and by imposing time limits on ICC proceedings. Deregulation continued with three acts in 1980 that gave railroads price-setting flexibility, expedited procedures for the abandonment of lines, gave the household-moving industry more flexibility in offering and pricing services, eased entry and exit in the trucking industry, and also gave more flexibility for routes and rates for truckers (see Table 5.1).13

The legislation affecting the ICC mirrors the pattern of legislation for regulatory agencies in general. The commission increased its powers, especially during times of economic difficulties such as the 1930s, and experienced greater controls during the retrenchment phase of the public mood that began during the mid-1970s and that proceeds into the 1980s.

ORGANIZATION AND FUNCTIONS

Technically, there are 11 commissioners of the ICC, nominated by the president and confirmed by the Senate, but functionally there are only 7; 4
## Table 5.1

<table>
<thead>
<tr>
<th>Act</th>
<th>Year Enacted</th>
<th>Statutes At Large Number</th>
<th>Substance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hepburn Act</td>
<td>1906</td>
<td>34 Stat. 584</td>
<td>Prohibition of issuance of free passes, granting of power to ICC to declare rates unjust and set maximum levels, increase in the number of commissioners, and extension of jurisdiction to cover certain pipelines.</td>
</tr>
<tr>
<td>Mann-Elkins Act</td>
<td>1910</td>
<td>36 Stat. 539</td>
<td>Tightening of ICC regulatory powers by further regulation of short- and long-haul rate discrimination, prohibition of predatory pricing against water carriers. Also gives ICC power to suspend rate increases pending hearings for up to 10 weeks.</td>
</tr>
<tr>
<td>Panama Canal Act</td>
<td>1912</td>
<td>37 Stat. 566</td>
<td>Prohibition of railroads from operating or owning water lines where competition is reduced.</td>
</tr>
<tr>
<td>Esch Car Service Act</td>
<td>1917</td>
<td>40 Stat. 101</td>
<td>Authorization of ICC to determine the reasonableness of freight car service rules and granting of emergency powers to direct service under unusual circumstances of need.</td>
</tr>
<tr>
<td>Transportation Act</td>
<td>1920</td>
<td>41 Stat. 474</td>
<td>Power to set maximum and minimum rates and intrastate rates discriminating against interstate levels. ICC given power to approve construction and operation of new lines and rail abandonments.</td>
</tr>
<tr>
<td>Motor Carrier Act</td>
<td>1935</td>
<td>49 Stat. 543</td>
<td>Regulation extended to motor carriers of freight and passengers as categorized by act.</td>
</tr>
<tr>
<td>ACT</td>
<td>YEAR ENACTED</td>
<td>STATUTES AT LARGE NUMBER</td>
<td>SUBSTANCE</td>
</tr>
<tr>
<td>------------------------------</td>
<td>--------------</td>
<td>--------------------------</td>
<td>---------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Transportation Act</td>
<td>1940</td>
<td>54 Stat. 898</td>
<td>Regulation extended to coastal, intercoastal, and inland water carriers.</td>
</tr>
<tr>
<td>Transportation Act</td>
<td>1958</td>
<td>72 Stat. 898</td>
<td>Authorization to determine more minimal railway rates, expansion of ICC role over rail service reductions, exemptions of motor carriers of certain agricultural products from regulation.</td>
</tr>
<tr>
<td>Department of Transportation Act</td>
<td>1966</td>
<td>81 Stat. 224</td>
<td>Creation of Department of Transportation with authority to regulate carrier safety.</td>
</tr>
<tr>
<td>Railroad Revitalization and Regulatory Reform Act</td>
<td>1976</td>
<td>90 Stat. 31</td>
<td>Deregulation of many ICC functions, more discretion to railroad in setting rates, imposition of time limits on ICC activities, establishment of Office of Rail Public Counsel to ensure full consideration of public interest.</td>
</tr>
<tr>
<td>Motor Carrier Act</td>
<td>1980</td>
<td>94 Stat. 793</td>
<td>Relaxing of entry and exit requirements for trucking industry, increased rate-making flexibility for freight carriers, less antitrust immunity for collective rate making, streamlined procedures for appeal of ICC decisions.</td>
</tr>
</tbody>
</table>
### Table 5.1 (continued)

<table>
<thead>
<tr>
<th>ACT</th>
<th>YEAR ENACTED</th>
<th>STATUTES AT LARGE NUMBER</th>
<th>SUBSTANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Staggers Rail Act</td>
<td>1980</td>
<td>94 Stat. 1895</td>
<td>Increase in price-setting flexibility for railroads, limitation of railroad immunity from antitrust laws to set rates collectively, expedition of railway abandonment procedures.</td>
</tr>
</tbody>
</table>


Seats have remained vacant since President Carter concluded that fewer commissioners would function more effectively. The commissioners are responsible for all commission decisions and may review or reverse decisions made at lower levels of the organization. The chairman has the overall responsibility for coordination and organization of the commission's work.

The next tier of the organization consists of five offices. The Office of Special Counsel functions independently and represents the public interest in ICC proceedings. The Office of Governmental Affairs functions as the liaison between the ICC and Congress, as well as coordinating activities with the states. An Office of Communications provides information to the general public and press, and a Small Business Assistance Office is an information source for small businesses, providing advice to those who wish to enter or are already in the transportation industry. Finally, an Office of Legislative Counsel has responsibility for legal matters concerning laws and regulations.

The Office of the Managing Director is the seat of administrative direction and coordination as well as the evaluation of staff performance, both in Washington and in the field. A series of offices handles aspects such
The Uncertain Balance

Figure 5.1


as consumer protection, legal advice to the commissioners, policy making and analysis, conducting hearings (staffed by administrative law judges), maintaining records of commission actions and transportation data, and financial analysis (see Figure 5.1).

As is the case with many regulatory agencies, there is a disturbing rise in the ratio of budget level to staff level (see Table 5.2). In 1951, the average staff level was 2,072.3 persons, with a total budget appropriation of $11,408,200; in 1979, the average staff level rose to only 2,103 but the total appropriation rose to $70,400,000, a rise far in advance of rises in the consumer price index (inflation rate).

PROCESS AND THE TRANSPORTATION INDUSTRY

As is the case with other regulatory agencies, the ICC has specific procedures for dealing with its workload. Administrative law judges hear cases in the formal docket. After the judges issue initial reports following a hearing, the disputing parties may offer objections. If no objections are forthcoming, the judge's report becomes the order of the commission, but if they do, one of the commission bureaus issues the final decision. Appeals are available to the full commission. The commission may also request that the attorney general institute proceedings in the courts. Cease and desist orders and suspension of operating rights are a part of the commission's enforcement arsenal and are issued upon discovery of clearly illegal actions.

An important element of ICC functioning is the monitoring of tariffs, lists of rates and charges for specific services that require mandatory filing 30 days before going into effect. Although the ICC does not directly set rates, it approves or disapproves of the rate schedules, and in this manner adjusts prices. The Motor Carrier Act of 1980 gives an area of leeway in charges, and the Staggers Rail Act allows the ICC to regulate rates only in areas where a railroad has market dominance and the rates are a certain percentage above carrier costs.

Until recent deregulation changes, many criticisms came forth that the ICC served a protectionist function, conservatively protecting and promoting established transportation interest at the expense of the general economic good. There is much merit to these criticisms. A General Accounting Office report in 1978 (before the deregulation legislation) found that often qualified applicants in the trucking field were denied entry because of ICC fear that their rates could lower the prices of established operators. The commission may also be seen as promoting the welfare of unionized as opposed to nonunion drivers, who also benefited by the
Table 5.2

**Budgets and Staffing for Fiscal Years 1951 – 1980**

<table>
<thead>
<tr>
<th>Year</th>
<th>Dollar Appropriation (to nearest million)</th>
<th>Staff</th>
</tr>
</thead>
<tbody>
<tr>
<td>1951</td>
<td>11</td>
<td>2,072</td>
</tr>
<tr>
<td>1953</td>
<td>11</td>
<td>1,849</td>
</tr>
<tr>
<td>1955</td>
<td>12</td>
<td>1,859</td>
</tr>
<tr>
<td>1957</td>
<td>15</td>
<td>2,090</td>
</tr>
<tr>
<td>1959</td>
<td>19</td>
<td>2,268</td>
</tr>
<tr>
<td>1961</td>
<td>21</td>
<td>2,386</td>
</tr>
<tr>
<td>1963</td>
<td>24</td>
<td>2,413</td>
</tr>
<tr>
<td>1965</td>
<td>27</td>
<td>2,339</td>
</tr>
<tr>
<td>1967</td>
<td>27</td>
<td>1,929</td>
</tr>
<tr>
<td>1969</td>
<td>25</td>
<td>1,808</td>
</tr>
<tr>
<td>1971</td>
<td>28</td>
<td>1,731</td>
</tr>
<tr>
<td>1972</td>
<td>31</td>
<td>1,676</td>
</tr>
<tr>
<td>1973</td>
<td>34</td>
<td>1,765</td>
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<tr>
<td>1974</td>
<td>41</td>
<td>1,874</td>
</tr>
<tr>
<td>1975</td>
<td>45</td>
<td>1,986</td>
</tr>
<tr>
<td>1976</td>
<td>52</td>
<td>2,049</td>
</tr>
<tr>
<td>1977</td>
<td>61</td>
<td>2,117</td>
</tr>
<tr>
<td>1978</td>
<td>66</td>
<td>2,110</td>
</tr>
<tr>
<td>1979</td>
<td>70</td>
<td>2,103</td>
</tr>
<tr>
<td>1980</td>
<td>77</td>
<td>1,940</td>
</tr>
</tbody>
</table>


higher prices charged the consumer, which became reflected in higher wages. The GAO report also found regulation to have a negative impact upon the energy and economic efficiencies of trucking companies. Empty backhaul, or those miles traveled by a truck without cargo, became more preponderant due to route regulation and the restriction on leasing out of
backhaul loads to other firms that have goods ready for transport. In its route allocations, the ICC created excess capacity in motor freight by delineating circuitous routes and excluding intermediate points.14

The ICC has also been involved in granting subsidies for the preservation of branch lines, subsidies that provide railway service to communities off the main lines but have questionable economic impact. Critics indicate that this regulatory approach also discourages technological innovation. First, to ensure standard service, any change must be made jointly, and second, outmoded freight cars are guaranteed a certain rate regardless of their service so that incentive for investment in better-designed cars disappears.15

Another analysis of the trucking industry found federal regulation in this area to be promotional, that is, effecting benefit to some at the expense of the total economy. Prices under regulation remained higher than they would have reached in a deregulated situation throughout the 1970s. Over a five-year period in the 1970s, the return on equity of the major trucking firms reached 21.2 percent. As a reflection of the profitability of trucking, truckers' certificates of operating authority became valuable and sold at high prices. In general, carriers became able to earn higher profits on their investments than manufacturers. In New Jersey, where intrastate shipments were not regulated, rates remained 10-13 percent below interstate rates for comparable goods and distances.

Another element this analysis points to is the willingness of the ICC to engage in cost-of-service as well as value-of-service rate making. The cost approach analyzes the cost of supplying the service, whereas the value approach takes into account the willingness of the shipper to pay based on the value of the item transported. Besides determining the cost of doing business, the ICC divides cargo into various classes, determining class rates according to the willingness of the shipper to pay. While the process may help offset large initial costs in the case of railroads or companies that have constructed bridges, it serves to inflate the returns of trucking companies.16

Many believe that the problem with promotional regulation stems from the precedent set by the railroads. While political and economic leverage let railroad interests gain overgenerous subsidies, the nature of the railroad industry does require a certain amount of government intervention. The amount of capital investment is so intensive that some guarantees become necessary. However, such is not necessarily true in other modes of ground transportation, such as trucking and shipping, where the government pays for the roads and provides for the available use of the waterways. Yet, the ICC often proceeded as if these industries remained in as much need of promotion as the railroads had historically.
In favoring the large and established interests, critics say that the ICC misapplied the concept of the economy of scale as well. Large firms become more economically viable in certain areas, such as the railroad, which may decrease unit costs by size. A long train does not take much more locomotive power to pull than one half its length and requires no more track. Such is not the case in trucking, where an independent trucker may haul a ton of goods at the same rate of gas consumption as a large firm with a fleet of trucks.

Several studies point to the pre-deregulated ICC as consistently showing a bias in favor of size. The Nader reports indicate that the Justice Department found the ICC to be the most insensitive of all the regulatory agencies to antitrust matters. The commission served to put a damper on initiative. By 1977, five huge trucking firms were handling 36 percent of all intercity transport of manufactured goods. The president of a smaller corporation complained to Congress that he was denied entry to carry cars and baggage to Florida, despite demonstrated market demand and 400 pages of affidavits and other supporting testimony.

The deregulation effort began to turn the situation in a better direction. In trucking, more independents are allowed to offer their services at competitive rates. Operating grants increased from 6,746 in fiscal 1976 to 29,311 in 1980, and rate discounts began to go into effect from 5 percent to 20 percent. In spite of the warnings of those opposing deregulation, trucking to small communities remained unchanged after the first year under deregulation policies.

The railroads are in a different position than the trucking industry. They are no longer a vital mode of transportation, yet they serve vital functions for certain sectors of the economy (notably agriculture and coal). It is not yet clear whether the increased operating flexibility allowed by the Staggers Rail Act, especially in the areas of rates and abandonments, will sufficiently vitalize the rails. More deregulation might prove necessary along with incentive programs (possibly tax abatements) to encourage technological innovation and the redirection of resources from antiquated methods and equipment.

The case against the ICC before 1980 is summarized by the statement that the economy as a whole suffers when the government seeks to protect one mode of transportation for fear that a competing mode will drive it out of business. This view holds that the natural decay of obsolescence is an essential part of any growing economy.

On the other hand, those defending the ICC point to the need to protect transportation industries. When change is too sudden, jobs are lost and goods are stranded. The transportation deregulation acts represent compromises whereby more flexibility—especially in the areas of entry and rates—is allowed, while the basic structure is preserved.
NOTES

1 *Munn v. Illinois*, 94 U.S. 113 (1877).
5 24 Stat. 379.
8 34 Stat. 584.
9 36 Stat. 539.
10 41 Stat. 474.
11 49 Stat. 543.
12 90 Stat. 31.
CHAPTER 6
Federal Trade Commission

A commission as large and multifaceted as the FTC requires a broad approach. We describe its origins and legislative authority and present its structure in terms of departmental divisions, basic staffing, and budget. We then analyze the way the FTC works, that is, how it functions and how the personnel and structure blend into process. Finally, we evaluate the FTC in terms of its effects on the total economy and compare it with the Antitrust Division of the Justice Department.

EARLY HISTORY AND LEGISLATIVE AUTHORITY

The FTC grew out of a period of intense economic consolidation, during which corporations reached unprecedented size. In 1898, Congress created the Industrial Commission to study corporations, which led to the creation of the Bureau of Corporations in 1903 within the Department of Commerce and Labor. But the bureau had no enforcement powers and was eventually merged into the new FTC in 1915.

Political support for a trade commission came from three distinct groups. Elements of the population, such as small business and farmers, were hostile to big business and expressed interest in a governmental harness over its activities. Another group, spanning over a wide range of business interests, sought guidelines to impose order upon a competitive environment. Finally, the general public, or consumers, were interested in regulations of price and service.

President Woodrow Wilson's support of the Federal Trade Commission Act in 1914 is important in that it marks his acceptance of big business as inevitable. Instead of seeking to prohibit the formation of huge corporations, the act is oriented to regulating them. Wilson thereby came around to the view of his Republican and Progressive competitor, Theodore Roosevelt.1
In 1914, the Clayton Act specified some of the unfair business practices that restrained trade and competition that had been only implied by the Sherman Act. During the same year, the Federal Trade Commission Act established an expert body that would not rely on the court system to enforce trade and antitrust rules. An independent commission could also be composed of individuals with expertise in both trade practices and antitrust and have more political insulation than executive department agencies.

The Federal Trade Commission Act has two basic provisions:

1. The prohibition of the use of unfair methods of competition and the use of unfair or deceptive practices by business firms.
2. The creation of the Federal Trade Commission with the power to investigate, regulate, and make reports on trade and commerce.²

Much of the act is vague, however, using language such as "unfair methods of competition in commerce," "unfair or deceptive acts or practices," and the stipulation that the commission shall act in "the interest of the public." In effect, the act described the nature of abuses without specifically delineating them. It creates confusion by declaring an absolute standard (fair business methods) but indicating the commission should act only when to do so is in the public interest.³ Section 6 also allows the FTC to "make rules," but it does not specify what type of rules. The act also provides for consent decrees, whereby the commission negotiates terms of firm behavior, and powers to issue cease and desist orders. The cease and desist is oriented toward specific behavior and does not prevent firms from initiating similar actions with the same negative impacts. The vagueness of the original act leaves the commission's performance more to the individuals who comprise it, rather than ensuring minimal standards as arranged by legislation.

The original FTC Act created a commission with a dual purpose: the regulation of business consolidation; and the regulation of business practices. In antitrust matters, the FTC has become involved in the areas of collusion (agreements among competitors), monopoly, mergers, and distributional restraints (arrangements between suppliers and purchasers).

The important specific business practices regulated by the FTC are summarized as follows:

1. Price-fixing agreements among independent firms.
2. Exclusive dealerships designed to prevent the entry of competitors.
3. Restrictive sales agreements or tying contracts that tend to reduce competition.
4. Price discrimination among the purchasers of a product when such price differences are not justified by cost economies and have the effect of lessening competition.
5. False and/or misleading advertising and warranties.
7. Interference in the business of a competing firm by threats, spying, or the disparagement of its products.
8. The use of scandalous and immoral trademarks, or trademarks that have been fraudulently obtained or that have become a common descriptive name.
9. The holding back of information on service or product qualities and capabilities to the consumer.
10. Overly restrictive licensing requirements that harm the consumer.
11. Improper disclosure of information, granting of application, and collection of funds in the credit industry.

The series of laws that expanded FTC jurisdictions are listed and summarized in Table 6.1. The laws indicate that the FTC has continued its activities in both fair trade practices and antitrust. Despite periodic public and congressional hostility, the commission's programs are intact, and the pattern has remained expansion rather than retrenchment.

ORGANIZATION AND FUNCTIONS

Today, the organization of the FTC mirrors its dual functions of antitrust and consumer protection. However, before 1949, the enforcement staff was divided into a Bureau of Legal Investigation and a Bureau of Litigation. Here, both consumer protection and antitrust were investigated by one staff group and litigated by another. In the early 1960s, the commission organized separate bureaus for the functions of consumer protection and antitrust. When Caspar Weinberger became chairman in 1970, yet another reorganization occurred when he established the Bureau of Competition to replace the Bureau of Restraint of Trade and the Bureau of Consumer Protection to replace the Bureau of Deceptive Practices. Weinberger effected a consolidation process in which some bureaus were abolished, such as the Bureau of Textiles and Furs, a division some critics had indicated received too much attention and resources. The commission now contains offices of policy planning and administrative law judges, as well as a Bureau of Economics, which engages in economic analysis. The commission is headed by five commissioners under a chairman, who has considerable authority over budget recommendations, appointments, agenda, and timing, although
<table>
<thead>
<tr>
<th>Act</th>
<th>Year Enacted</th>
<th>Statutes At Large Number</th>
<th>FTC Involvement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clayton Antitrust Act</td>
<td>1914</td>
<td>38 Stat. 730</td>
<td>Regulation of stock holding of corporations, interlocking directorates, certain sales and price arrangements.</td>
</tr>
<tr>
<td>Export Trade Act</td>
<td>1918</td>
<td>40 Stat. 516</td>
<td>Authorization of FTC to supervise export associations that were exempted from the antitrust laws.</td>
</tr>
<tr>
<td>Robinson-Patman Act</td>
<td>1936</td>
<td>49 Stat. 1526</td>
<td>Prohibition of price discrimination where competition is reduced or monopolies promoted. The FTC supervises all price discounts to determine justification.</td>
</tr>
<tr>
<td>Wheeler-Lea Act</td>
<td>1938</td>
<td>52 Stat. 114</td>
<td>Enforcement strengthened, all FTC orders made final within 60 days. Compliance failures could be punished by fines up to $5,000 per diem for each violation. FTC authority expanded to cover unfair business practices affecting the consumer as well as producer.</td>
</tr>
<tr>
<td>Wool Products Labeling Act</td>
<td>1940</td>
<td>54 Stat. 1128</td>
<td>Requirement that all manufacturers disclose materials used in production of wool product supervised by FTC.</td>
</tr>
<tr>
<td>Lanham Trademark Act</td>
<td>1946</td>
<td>60 Stat. 427</td>
<td>Requirement of registration and protection of trademarks used in commerce, administered by FTC.</td>
</tr>
<tr>
<td>Act</td>
<td>Year Enacted</td>
<td>Statutes At Large Number</td>
<td>FTC Involvement</td>
</tr>
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<td>-----------------------------------------------</td>
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</tr>
<tr>
<td>Textile Fiber Products Identification Act</td>
<td>1958</td>
<td>72 Stat. 1717</td>
<td>Prohibition of the use of false brands or advertising of the fiber content of textile products.</td>
</tr>
<tr>
<td>Fair Packaging and Labeling Act</td>
<td>1966</td>
<td>80 Stat. 1269</td>
<td>Prohibition of unfair or deceptive packaging or labeling of certain consumer products.</td>
</tr>
<tr>
<td>Truth-in-Lending Act</td>
<td>1968</td>
<td>82 Stat. 146</td>
<td>Authorization of FTC to require full disclosure of credit terms to a borrower. It also reduced user liability for loss of a credit card.</td>
</tr>
<tr>
<td>Fair Credit Reporting Act</td>
<td>1970</td>
<td>84 Stat. 1521</td>
<td>Authorization of the FTC to ensure that a consumer’s credit report is accurate, relevant, current, and confidential.</td>
</tr>
<tr>
<td>Equal Credit Opportunity Act</td>
<td>1974</td>
<td>88 Stat. 1521</td>
<td>Prohibition of the denial of credit based upon sex, marital status, age, race, religion, or national origin.</td>
</tr>
<tr>
<td>Magnuson-Moss Warranty – Federal Trade Commission Improvement Act</td>
<td>1975</td>
<td>88 Stat. 2123</td>
<td>Authorization of FTC to establish standards on written warranties. Allows the FTC to establish trade regulation rules with the force of law on an industry rather than case-by-case basis, and allows agency to represent itself in court and to request redress and civil penalties for violations of the FTC Act.</td>
</tr>
</tbody>
</table>
### Table 6.1 (continued)

<table>
<thead>
<tr>
<th>ACT</th>
<th>YEAR ENACTED</th>
<th>STATUTES AT LARGE NUMBER</th>
<th>FTC INVOLVEMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hart-Scott-Rodino Antitrust Improvement Act</td>
<td>1976</td>
<td>90 Stat. 1383</td>
<td>Requirement of certain companies to notify FTC of intention to merge.</td>
</tr>
<tr>
<td>Federal Trade Commission Improvements Act</td>
<td>1980</td>
<td>94 Stat. 374</td>
<td>Lessening of powers of FTC, curtailing publicizing of information, regulation of trade groups by requiring outside party contacts to go on the record, tightening standards on restrictions of advertising. Also places three-year moratorium on existing FTC rules on advertising (with the exception of children's ads) and provides for a two-chamber congressional veto of FTC actions.</td>
</tr>
</tbody>
</table>

technically, concurrence of the other commissioners is necessary for important matters (see Figure 6.1).

Offices

The Bureau of Competition is the seat of antitrust activity and is staffed primarily by lawyers. The bureau director is generally considered the second most influential individual in the FTC. The director decides whether the law has been violated and whether commission action would be in the public interest. In the Bureau of Economics, the emphasis is on specific business practices and actions that will benefit consumers. The bureau is a support office in that it advises the commission on the economic aspects of possible actions, but it also cooperates with the investigations of the Bureau of Competition and Bureau of Consumer Protection. The Bureau of Consumer Protection has the responsibility of investigating, conciliating, and litigating cases of unfairness and deception of the public. The Office of General Counsel offers legal counsel and handles congressional liaison.

The functions of monitoring and evaluating FTC management and making recommendations for commission changes are handled by the Office of Policy Planning and Evaluation. Its purpose is to coordinate the operation of the bureaus of Competition, Consumer Protection, and Economics by engaging in long-term planning so that the commission may gear its resources to the most significant cases. It organizes interbureau task forces based upon an industry or issue that offer recommendations for policy review.

Budget

The budget of the FTC indicates the scope of the agency, its concern, as well as its political relations with Congress. During the past 10 years the budget has more than tripled and the staff increased by about one-fourth (see Table 6.2). Although the Federal Trade Commission Improvement Act of 1980 is mainly a curtailment of FTC powers (see Table 6.1), the budget and activities of the commission have yet to change dramatically. Congressional antagonisms have led to a dramatic increase in FTC appearances before Congress, and during a dispute that resulted in a congressional two-chamber veto over FTC regulations, the commission temporarily ran out of funds. Yet in 1980, from a total budget request of $69,021,000, Congress came through with $67,756,000. The ratio of funds spent maintaining competition and protecting the consumer remains
The Uncertain Balance


Figure 6.1

Federal Trade Commission
TABLE 6.2
FTC BUDGETS AND STAFFING FOR FISCAL YEARS 1970–1980

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</thead>
<tbody>
<tr>
<td>BUDGET ($ MILLIONS)</td>
<td>20</td>
<td>22</td>
<td>25</td>
<td>27</td>
<td>32</td>
<td>39</td>
<td>52</td>
<td>59</td>
<td>63</td>
<td>68</td>
<td></td>
</tr>
<tr>
<td>STAFFING</td>
<td>1,385</td>
<td>1,385</td>
<td>1,390</td>
<td>1,530</td>
<td>1,560</td>
<td>1,569</td>
<td>1,638</td>
<td>1,668</td>
<td>1,650</td>
<td>1,665</td>
<td>1,665</td>
</tr>
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</table>


about the same, with an approximately $2 million difference in funding. Thus, regardless of the deregulation impetus in Congress, the essential organization and structure of the FTC remains the same.

PERSONNEL AND PROCESS

Staff

For any commission as multifaceted as the FTC, the individuals who comprise it are essential to its successful functioning. The backgrounds of individuals reflect the antitrust/consumer protection dual function of the commission, as does its organization. The two major affiliations of FTC personnel are law and economics, and each discipline has its own regulatory orientation.

Attorneys typically comprise about 75 percent of the total staff, which makes them the dominant force. Because attorneys are trained in the law and the adversarial process, they are oriented toward the “attack” of breaches, rather than considerations of economic impact, and look toward results measured in terms of decision and sanction. The lawyers are oriented toward “conduct” cases, the proper behavior of individuals rather than the focus of economic results. Because the commission acts in both proactive and reactive ways, that is, it finds cases by initiating research as well as by responding to unsolicited information, the research skills of the lawyers is essential.

According to interviews conducted by political scientist Robert Katzmann, the economists often feel in conflict with the attorneys. They are likely, Katzmann reports, to be wary of undue government interference with business operations and more tolerant of concentration if there is economic justification. Because of their training in macroeconomics, they are more theoretically minded than lawyers, more willing to base actions based on a model or set of assumptions about the economy. They are also
apt to feel that their government position is more a temporary role until they are settled in a university, whereas the lawyers see their casework as more integrated into the future of their careers. Partly because the economists' role is primarily advisory, they are sensitive about taking direct orders from the attorneys and guard their independence, both for reasons of personal autonomy and to retain a consistently economic perspective.¹⁰

There is little evidence to support conflict of interest between the regulators and their regulatory mandate. One study concludes that of the major regulatory agencies, FTC personnel perceive of few incentives to rule in favor of the regulated industries. Subsequent career opportunities tend to be planned in the areas of consumer protection and antitrust rather than in the regulated industries. In any event, the lawyers perceive that even if they work at a later time in regulated industries, if they are aggressive in their regulatory functions in the FTC, they will be looked upon favorably as dedicated professionals.¹¹

The quality of the staff is affected by two problems: turnover, and emphasis upon political instead of qualification selection criteria for commissioners. The turnover rate of attorneys is close to 20 percent a year, and one 1976 study indicates that 89 percent of attorneys who joined the commission in the period 1972-1975 expected to leave in two years or less, no doubt looking toward more lucrative private jobs after their investment in government experience. Since 1970, Bureau of Competition attorneys have left at rates of from 13 percent to 25 percent a year, and of a total of 200 attorneys whose service dated from 1969, only 20 remained in 1976. Although economists see their work in the FTC as disjointed from the work of their future careers, they have half the turnover of the attorneys, in part due to the relatively poor employment opportunity in universities.¹²

Staff turnover represents a costly expense for the government and a compromise of commission efficiency, especially for an organization involved in complex cases where experience is of prime importance. The commission should seek to determine why the turnover rate is so high and then devise remedies to diminish it. If the reasons for leaving are primarily monetary, raises should be cost-effective if it is proven that the monies spent in additional salaries is less than the expenses incurred in retraining and in mistakes due to inexperience. The matter of personnel tenure involves a delicate balance, as do most matters in government regulation. People who do the same things for too many years tend to become inflexible and set in their ways. However, inexperience holds its own dangers. In sum, the emphasis should be on attracting and keeping highly qualified personnel by making the compensation adequate and creating opportunities for variety and growth within the commission.
The matter of commissioner recruitment is somewhat more difficult since it involves other personnel, that is, the personnel of the executive department, specifically the president and his domestic counsel. A Senate Committee on Commerce study of appointments to the regulatory agencies found that the process is both highly partisan and casual. With the exception of Lyndon Johnson, presidents have not given much attention to the matter, and they have therefore relied on the judgment of their advisors. As a result, competence, experience, and often even regulatory philosophy become secondary to loyalty and a sense of obligation created by those who have previously given political service. The Commerce Committee study summarized the important qualities of those selected to be FTC chairmen: (1) political sponsorship; (2) nonassociation with controversy; (3) lack of glaring philosophical disagreement with the administration; (4) tactical positioning, that is, selection as a way of repaying a political debt or avoiding political antagonisms. The committee concluded that the White House should create an office on regulatory agency appointments with responsibility for recruiting regulators and that Congress should hesitate to confirm nonqualified applicants rather than continue on its present course, which has denied only one nominee confirmation since 1950. In such a manner, individuals who have a substantive interest and background in the FTC and are able to approach the economy with objectivity would more likely come to the fore.  

Case Selection

Case selection is another important aspect of agency functioning. Determining an agenda and priorities is the definition of the commission’s goals and defines the parameters of its potentials. Political scientist Robert Katzmann describes the caseload selection of the 1970s as primarily determined by the interaction of the bureaus of Competition and Consumer Protection and the five commissioners. This view sees the commission as primarily operating with conflict and compromise among its components. Before 1970, the conflict was more pronounced in that commissioners either vetoed or gave the go-ahead for cases presented by the staff. After 1970, the staff could proceed after commissioners voiced reservations as a type of research extension. Should more convincing material later come to light, the commission could then give a go-ahead. One problem with case selection is the entrenchment that develops after resources have been committed. Even though a case may no longer have merit, previous time investment motivates those with a “stake” in the case to continue efforts in the hopes of achieving at least some result.
A powerful dynamic in case selection is the self-interest of the individuals within the commission. The attorneys, for example, do not favor the large “structural” cases. These are cases that are proactive (initiated by the FTC rather than responding to a specific complaint) and involve general issues of principle with long-term implications for the consumer. Because these cases do not reach the courtroom for several years and do not bear results for more protracted periods, the lawyers are denied courtroom experience and could get bogged down in detail.15

The economists, as indicated, do not base their reputation upon courtroom performance or trial outcome. They are more oriented toward long-term objectives and are more satisfied with producing analyses of conditions, or serving as a brake on moving forward with too many insignificant cases.

The commissioners in the FTC do not tend to base their careers on public service, and so they are not under great pressure to “make a name” in a dramatic case that will serve as capital in an election, or get them attention for purposes of landing an appointive office. One general pattern that tends to hold for commissioners, though, is that they prevent the commission from taking radical action in any direction. Commissioners, more than the staff, tend to have dealings with the regulated industries, either directly or as legal representatives or consultants.

There are, of course, elements that affect FTC actions outside of the commission. Mention has been made of the president’s responsibility in the recruitment and nomination process. Congress is responsible for appropriations and oversight and has already reflected the popular mood that regulations should be reduced by the passage of the congressional veto over FTC actions and by curtailed appropriations. Along with the executive branch, which demands economic impact statements, Congress expanded its oversight by requiring additional testimony from the commission; in 1975, the number of hearings increased by more than one-third.

In 1974, the commission announced an openness policy whereby it attempts to publicize as much information as possible and to allow the public a greater opportunity to offer input. The openness policy consists of the issuance of more news releases, public statement of the termination of investigations, public availability of consent orders indicating the commitment of individual firms, an extension of public comment on proposed settlements from 30 to 60 days, and disclosure of staff memos normally after three years. The commission also made more of its activities open to public observation. Such a policy encourages the input of not only industry but public interest groups as well.
Specific Procedures

The FTC engages in several procedures to ensure the proper process of rule making and enforcement. Advisory opinions are offered at the request of a business or individual that define the limits of the law (though they may be overturned by the commission). Industry guides are offered to aid in the interpretation and understanding of FTC requirements.

Adjudicative proceedings have the purpose of resolving complaints. They occur after a commission investigation and issuance of a formal complaint. If the respondent contests the charge of illegality, the case is brought to a hearing in front of an administrative law judge in which judicial procedures such as arguments and examination of witnesses are followed. If neither party files an appeal with the U.S. District Court of Appeals, the decision becomes a commission order within 30 days.

A consent order is an agreement in which a party neither admits nor denies wrongdoing, but agrees to adhere to a specified line of conduct. The trade regulation rules (TRRs), authorized by the Magnuson-Moss Warranty—Federal Trade Commission Improvement Act of 1975, allow the commission to rule on an industrywide rather than case-by-case basis. A period of comment is allowed (usually about 60 days) between the publication of proposed rules in the Federal Register and their enforcement as law.

In the case of failure to comply to either a TRR or a cease-and-desist order, the FTC may obtain a court order for compliance. Failure to adhere to such rulings carries a penalty of $10,000 for each day of truancy.

The FTC has several reporting requirements, including the subpoena of materials it wishes to inspect, questionnaires for FTC quarterly financial reports, premerger notifications, export trade association annual reports, advertisement substantiation reports, compliance reports for companies abiding by consent orders, and line-of-business reports detailing information on business activity and required of nearly 500 of the largest manufacturers.

The emphasis upon disclosure is sound in a highly technological society. Detailed business information allows the government's antitrust and consumer protection activity to be more efficient, since it has a better picture of what is happening within firms as well as their effect upon the economy. The dissemination of information also ultimately helps to rationalize the allocation of resources since stock analysts and investors are better able to make more informed judgments. Economic studies are likewise improved by the availability of more detailed data. Benefits also exist for business, which may spot opportunities and assess the market and the competition.16
EVALUATION

Although the FTC issued some broad directives in the early years of its operation, it soon lost the interest of Congress and attention of the public, and it became extremely inactive in the 1920s and 1930s. The 1940s mark a time of somewhat renewed interest in antitrust activities and unfair business practices, and during this period the commission moved into specific areas such as wool and textiles. In the following two decades, however, the commission can best be characterized as low-key, as attempting to create some regulation, but without unduly disturbing business. A statement by the Hoover Committee in 1949 summarizes the basic criticism of FTC performance up to that time, with its emphasis on trivial cases and ponderous pace:

As the years have progressed, the Commission has become immersed in a multitude of petty problems; it has not probed into new areas of anticompetitive practices; it has become increasingly bogged down with cumbersome procedures and inordinate delays in disposition of cases. Its economic work—instead of being the backbone of its activities—has been allowed to dwindle almost to none. The Commission has largely become a passive judicial agency, waiting for cases to come up on the docket, under routinized procedures, without active responsibility for achieving the statutory objectives.17

The year 1969 is a watershed year for the FTC in that evaluations of the FTC came forth from both Ralph Nader and the American Bar Association.18 The Nader report gained widespread public attention and is an analysis based upon the work of seven Nader volunteers who observed the commission firsthand.

The Nader report criticized the commission in several areas. It indicated that the FTC was far too reactive, waiting for cases to come in rather than delineating policy and proactively finding significant violations. It relied too heavily on voluntary compliance rather than sanctioned enforcement and failed to seek the necessary resources and authority. In addition, recruitment was based too greatly on partisan politics rather than ability. Although more moderate in tone, the ABA report came to similar conclusions. It found the commission too protectionist of specific industries, such as textiles, furs, and wools. The caseload was insignificant and low, and delays all too prevalent.

In terms of recommendations, the Nader report called for more and swifter activity, more complete planning and policy making, information disclosure, and stiffer penalties. The ABA went as far as to say that, if management is not improved, the FTC should be terminated and its functions taken over by other government offices.
Following these criticisms, new FTC Chairman Caspar Weinberger reorganized the commission to reflect better its dual roles of antitrust and consumer protection enforcement. The less important departments were abolished, and a great many of the staff replaced, until eventually about a third of the middle- and lower-level staff was changed. Many of the new staff members adhered more closely to the tenets of consumerism than had the previous employees. The revitalization continued during the 1970s, with several important antitrust cases being initiated in the areas of business machines and cereals and a broader perspective taken in delineating industrywide guidelines after the passage of the Magnuson-Moss Warranty—Federal Trade Commission Improvements Act in 1975. Michael Pertschuk, the chairman appointed by Carter, initiated the regulation of children's advertising.

The increased activity led to a response by business, which lobbied for a curtailing of FTC functions. The Federal Trade Commission Improvements Act of 1980 represents an inhibition of the agency, especially in the creation of the two-chamber congressional veto, which is the first time arrangement for such a veto was made in reference to a federal regulatory agency. The hostility to overactivity is reflected in the Reagan administration, director of the Office of Management and Budget David Stockman on one occasion remarking that "the world would never know the difference" if the FTC were eliminated. When James Miller, Reagan's appointee as chairman, joined the FTC, the Republicans then composed a majority of the commissioners.

The FTC can point to some basic improvements in recent years. It cut down on delays, eliminated some of the more trivial regulations, broadened public participation, improved coordination with other agencies and state activities, strengthened planning functions, and improved the readability of its rules. But more important in the evaluation of the commission is the viability of its essential two-part structure and its role in the total regulatory system, especially in comparison with the Antitrust Division of the Justice Department.

The FTC was established as a means of presenting clearer standards of conduct and organization to business than had previously existed. It also was to complement the Antitrust Division, which sought remedies exclusively in the courts. The existence of an independent regulatory commission could counteract lax antitrust should the Supreme Court grow conservative in its orientation, since the commission decides itself on antitrust matters, although its decisions may be appealed in the courts.

Some critics state there is no justification for a two-pronged commission and call for the assumption of all antitrust duties by the Antitrust Division. Others feel, however, that antitrust is more efficiently regulated by a regulatory thrust from two directions. The Antitrust
Division has the element of greater presidential control, which may work for or against vigorous antitrust activity, depending on who is president. When a president is particularly interested in the area, he may bring considerable weight to the problem by announcing antitrust as a priority and directing resources to it. But in the absence of such interest, the FTC operates regardless. In an organic sense, the commission may be seen in this case as a backup system, ensuring the application of the Sherman and Clayton statutes in an unfavorable political climate. While the FTC may be more dependent on the Congress than is the Antitrust Division, it is, due to its quasi-judicial functions, less dependent on the courts. It may, therefore, have greater control over reducing delays.

What is essential in the context of a coexistence of these agencies is an adequate feedback and communications system. Ralph Nader associate Mark Green quotes Robert Wright, formerly second in charge of the Antitrust Division, as stating that at one time the communication was entirely ad hoc: "We'd get on the phone and say, 'Well, who's got this one? And then we'd argue about it.'" Embarrassing and wasteful conflicts occurred well after June 1948, when a liaison system was established to prevent the duplication of work. In 1966, for example, the FTC began an investigation of an RCA-Whirlpool acquisition shortly after the Antitrust Division had informed the company that there would be no government antitrust action.

However, since that time, the system has improved; liaison officers hold regular meetings and keep more complete files. Usually, one agency concurs with the action of the other, unless it is already involved in a case that holds some conflict with the new proposed action. As a result of greater care in liaison, there have been no instances in recent years of wasted and duplicated efforts.

The biological approach referred to in Chapter 1 lends support to the existence of built-in backups and function sharing for important systems. When a part of the brain, for example, is incapacitated, the properly functioning sectors can take over the processes lost due to the injury. Some strategic redundancy also characterizes a properly functioning organic system. Eyesight regulates movement, but the senses of hearing and smell do so as well. Locomotion is too important to the organism to rely totally upon one sense, for that sense has its own perspective and is subject to confusion, malfunction, and breakdown. Likewise, the areas of antitrust and fair business practices go to the heart of the functioning of the political economy. Two involved agencies, each with their own perspectives and orientations, and subject to different powers and pressures, could ensure more productive system functioning. With continued monitoring and reevaluation, especially by the Congress, coexistence appears viable.
NOTES


8 Clarkson and Muris, *Federal Trade Commission*.


23 Green, *Closed Enterprise System*, p. 428.
CHAPTER 7
Air Transportation: FAA and CAB

EARLY HISTORY AND LEGISLATIVE AUTHORITY

In many respects, the history of airline regulation parallels that of the government's involvement with the railroads. The concept of air travel brought with it the requirement of technological innovation, great capital expenditures, and the assumption of enormous business risks. If the railroads required thousands of miles of tracks, the airplanes required landing facilities, airports, and a new system of rules to guide their safe and efficient operation.

Under the impetus of World War I to develop airplane technology, the U.S. Post Office Department was able to establish eight air mail routes by 1918. Although the government operated the planes in the early years due to lack of private interest, by 1925 enough commercial carriers were in operation to allow the government to contract private companies. The Kelly Act of 1925 authorized the postmaster general to make contracts not exceeding four-fifths of the revenues derived from the air mail. An amendment the following year set fixed rates based on distance traveled and mail weight, which made postal revenues, carrier costs, and carrier compensation all independent of one another. Another amendment was added to the Kelly Act in 1930 with the passage of the Watres Act, which permitted the postmaster general to renegotiate rates and lengthen existing routes without competitive bidding.

The legislative cornerstone for the development of commercial aviation is the Air Commerce Act of 1926. The measure directed the secretary of commerce to foster air commerce, establish and designate airways, establish and maintain aids for navigation (except airports), license pilots and airmen, arrange for research and development affecting air travel, inspect and certify aircraft and aircraft components, and investigate accidents. Thus, in the early years, the Commerce Department became
responsible for the range of activities that today is allocated to the Federal Aviation Administration. In order to administer the act, the Commerce Department created two divisions within its Aeronautic Branch, the Air Regulations and Air Information Divisions. Various other Commerce offices handled other aeronautics-related functions, such as the Bureau of Standards, which conducted aeronautics research.

The period of Commerce and Post Office Department regulation, between 1926 and 1934, when major reorganizations became instituted, held both progress and problems in airway regulation. Air traffic rules, craft registration, and pilot licensing successfully moved forward under the guidance of the Commerce Department, yet the Post Office failed to control air mail traffic adequately. A Senate investigating committee chaired by Senator Hugo L. Black in 1934 exposed a scandal in which collusion occurred in the awarding of air mail contracts instead of competitive bidding. The problem was considered so serious that President Roosevelt invalidated all existing contracts and directed the army to carry the mail.3

The congressional response to the disarray culminated in the passage of the Airmail Act of 1934.4 The measure reduced the postmaster general's involvement with airmail contracts by transferring control over contract rates to the Interstate Commerce Commission. The act also limited the number of contracts each airline could acquire, made airline holding companies unlawful, and created a Federal Aviation Commission to study regulatory problems and report to the Congress by February of 1935. Problems under the new act immediately became evident. The three agencies now involved with airway regulation—the Interstate Commerce Commission, the Post Office, and the Federal Aviation Commission—had difficulty coordinating activities. The unsatisfactory nature of the arrangement became even more evident when the Federal Aviation Commission announced its findings. The commission recommended the institution of an air commerce commission (based on the model of ground transportation regulation), which would have the authority to fix air mail rates and carry out other economic regulations, such as the promotion of sound competition. While the Commerce Department's Aeronautics Branch changed its name to the Bureau of Air Commerce the same year, the commission recommended that the proposed air commerce commission should also take over the regulation of safety currently handled by the Bureau of Air Commerce. Local agencies had the primary responsibility for the development of airports, but the commission also recommended that the federal government should share the costs of the installation of lights and other navigational aids. Because of lackluster economic performance by the private air carriers, the commission sought subsidies in the form of government extra mail pay, which, it felt, would
also encourage better safety performance.\(^5\) Congress went to work on a major new piece of legislation.

**The Civil Aeronautics Act of 1938**

The Civil Aeronautics Act reflects the socioeconomic conditions of the times in which it was written. While airplane technology advanced in the 1920s, financial conditions in the 1930s made it difficult to apply the new information. Between 1935 and 1938, the number of miles flown increased by 46 percent and total revenues grew almost 75 percent, but expenses continued to outdistance revenues. Airline losses came to $150,000 in 1937, and increased to $3.3 million in 1938.\(^6\)

After President Roosevelt announced support of air traffic regulation by a new division created within the Interstate Commerce Commission, Senator McCarran and Representative Lea submitted bills in both houses of Congress reflecting this perspective. In a consistent illustration of the notion that bureaucrats seek to maximize their own influence, the ICC supported the proposal, while the Commerce Department and Post Office, which would lose influence by it, opposed the measure. Seeking to minimize interagency conflict in the face of intense differences, Roosevelt appointed a committee to review the situation and make recommendations to facilitate the passage of federal legislation. Under the influence of its conclusions, Roosevelt changed his position and favored the establishment of a separate agency to regulate the airways. Roosevelt’s support for airway regulation was based on the desire to keep airlines and the railroads on an equal footing, so that both operated in a regulated context.\(^7\)

The Civil Aeronautics Act created a five-member Civil Aeronautics Authority with powers to regulate safety and economic conditions composed of both a civil aeronautics administrator responsible for executive and operational functions and a three-member Air Safety Board authorized to investigate accidents and propose changes to improve air safety.\(^8\) The act contains promotional, economic regulatory, as well as safety provisions. For promoting the air transport system, it grants the authority power to issue certificates of public convenience and necessity, which require carriers to demonstrate that their routes are adequate, necessary, and competitive. Less confusion existed under the requirement that tariffs, regulations, and practices be filed with the authority. A central source of information and protection from rate wars and wasteful competition gave the industry more stability. In addition, the new agency could approve or prevent mergers, so that approved consolidations became exempt from antitrust actions. A grandfather clause in the act gave
16 established carriers permanent rights to routes existing at the time of the act’s passage. Economic regulation proceeded by the prescription of rates and regulations, assignment of routes, inspection of records, suspension of unjust rates, and determination of reasonableness of overseas agreements by the authority. The Air Safety Board served to investigate and make recommendations to the authority, which could then establish rules of safe conduct.

The 1940s and 1950s

A major reorganization of air traffic regulation was carried out in 1940 in order to clarify the functioning of the Civil Aeronautics Authority. By order of President Roosevelt, the five-person Civil Aeronautics Authority was transferred to the Department of Commerce and renamed the Civil Aeronautics Board (CAB), while the Air Safety Board was abolished and its investigatory functions assigned to the new CAB. The new organization functioned within the Department of Commerce; however, it was to exercise considerable independence from the secretary of commerce. In addition, the Civil Aeronautics Administration (CAA) was established, also within the Department of Commerce, to take over the administrative functions previously handled by the civil aeronautics administrator within the Civil Aeronautics Authority. The CAA also took on safety functions, running a Bureau of Safety Regulations and becoming involved in civil air traffic control, aircraft inspection standards, and the training of flight personnel.

The consistent protectionist approach of the CAB and CAA was given exception by the nonregulation of nonscheduled operators, that is, contract-basis air “taxi” services, which continued during and persisted after the end of World War II. Many military-trained pilots took advantage of war surplus equipment to begin such services and offered a competitive service, often priced as much as 35-40 percent below regular airline rates. In a continuation of its protectionist policy toward the larger established airlines, the CAB increasingly regulated the nonscheduled flights.

President Truman organized an Air Policy Commission, which submitted its report on the development of commercial aviation in January of 1948. It recommended placing all civil aviation activities under the secretary of commerce and creating an Airport Advisory Committee to advise on ground facility improvements. Truman responded with Reorganization Plan V in 1950, which placed all airway regulatory agencies within the Department of Commerce under the secretary’s supervision. Yet, the secretary, in turn, responded by redelegating authority and
creating an assistant secretary of commerce for transportation to handle many of the supervisory functions and left the CAA with considerable autonomy. The early 1950s also marks a time of cooperation between federal authorities and localities in the provision of airport facilities, as in the case of Rockford, Illinois.

A second report ordered by Truman, written under the aegis of the Doolittle Commission, handled safety issues. The report took a case-by-case approach and focused on planning and zoning of ground facilities, local responsibilities and federal aid, circling and maneuvering procedures, noise levels, crew training, and air control methods. Budgetary and political considerations in Congress, however, prevented implementation of the major findings.

The airline industry succeeded in receiving consistent protectionist and promotional policies from government regulation. It became an industry in which successful operation was reinforced by most government actions. When profits became too reduced, the government would respond by either direct financial subsidy or by mandating a rise in rates. Under pressure from Congress, the CAB instituted a General Passenger Fare Investigation in 1956, although it was opposed by the airlines, which feared an investigation could result in lowered fares. The hearings, however, resulted in fare increases and the establishment of fair rate of returns of 10.5 percent for the large trunk airlines and 12 percent for smaller trunks.

During the Eisenhower administration, the President’s Advisory Committee on Government Organization recommended a study of transportation regulation, which led to the formation of the Aviation Facilities Study Group. Its report, submitted to the Bureau of the Budget in December 1955, called for a master plan for developing aviation facilities, air traffic control, technology, and financing. A subsequent report directed by Edward P. Curtis focused upon the problems of the CAA in dealing with air traffic control and proposed an independent agency to deal with navigation, communication, and air traffic.

In the Congress, Senator Mike Monroney, chairman of the Subcommittee on Aviation, supported the idea of an independent agency, and the concept became law by the Federal Aviation Act of 1958, which created two independent agencies. Taken out of the Commerce Department, the Civil Aeronautics Board handled economic regulation and investigations of accidents. A newly formed Federal Aviation Agency was responsible for safety.

For the purposes of implementing its regulations, the act specified that the CAB elicit reports from carriers and prescribe their form and content. The CAB became responsible for approval of all mergers and consolidations between air carriers, air carriers and surface carriers, and air carriers and firms engaged in other aspects of aeronautics. Approved
consolidations became immune to antitrust laws. The CAB gained approval powers for all government loans and financial aid to carriers, regulated unfair and deceptive business practices, and approved all carrier agreements in the areas of pooling, sharing of earnings, losses, or equipment, and other such arrangements. In addition, the CAB could exempt selected carriers from economic regulation should their economic condition require it.

The Aviation Act also prescribed the areas of safety responsibility of the new Federal Aviation Agency. Minimum safety standards became necessary in all aspects of production, design, construction, operation, and maintenance of aircraft and aircraft components as well as reserve parts and fuel. The FAA set maximum hours for airmen and other employees and determined practices and procedures connected to safety in air commerce. In addition, the FAA controlled navigable air space, operated air navigation facilities, issued standard certificates for all personnel and craft, operated air navigation facilities, and established grant programs for airport improvements and construction.

The 1960s and 1970s

The most important development of the 1960s for aviation was the passage of the Department of Transportation Act of 1966. The act created a cabinet-level Department of Transportation and transformed the Federal Aviation Agency into the Federal Aviation Administration, which became a division of the new Transportation Department. Accident investigation became the responsibility of a new independent agency, the National Transportation Safety Board.

Before the deregulation effected in 1978, the CAB evolved a set of procedures and applied its regulatory powers. Perhaps the most important aspect of its economic regulation from the point of view of business was its power to regulate the entry of carriers by means of the issuance of certificates of public convenience and necessity. The certificates not only granted the opportunity to enter the market, but specified terminal and intermediate destinations and types of service as well. The application process became complex, involving public notice and formal hearings to determine whether there was a public need for service. The process included a fitness evaluation, in which the applicant demonstrated abilities to finance, initiate, and maintain service.

In addition, carriers filed rate schedules with the CAB, which prescribed categories and levels of charges. The CAB also fixed rates for mail transportation, establishing service rates designed to promote a fair rate of
return on investments, and subsidy rates, designed to preserve the continuance of less profitable service.

The CAB took complaints from any individual and dismissed without hearing those considered to be without merit after preliminary investigation. CAB directives stemmed from complaints as well as agency-initiated investigation and were always subject to judicial review.

A major reorientation of federal regulation of the airways occurred in 1978, with the passage of the Airline Deregulation Act of 1978. The major purpose of the legislation involved increasing the level of competition in the airline industry while preserving service to less-populated areas and preventing anticompetitive practices. Among its major provisions, the act opened up entry by ordering the CAB to grant operating rights to carriers for areas in which only one other carrier served, in addition to allowing generally for the approval of new airlines. Rates also became substantially deregulated by permitting carriers to lower rates 50 percent below or 5 percent above standard industry fares without prior CAB approval. The standard industry fare was defined as the fare in effect on July 1, 1977 (subject to semiannual CAB review). In addition, interstate airlines became explicitly exempt from state regulation of rates and routes. An automatic entry program became instituted, whereby airlines could begin service on an additional route for each year of 1979-1981 without CAB formal approval.

Currently, CAB enforcement actions fall into the broad areas of consumer matters, agreements and antitrust, charter flights, passenger tariffs, and accounting and reporting violations. Consumer matters involve issues of service delivery, and agreements and antitrust concern the relationships between airlines. The Deregulation Act requires the CAB to approve or disapprove of all such agreements if they affect competitive conditions, but the act also put the burden of proof for prohibiting a merger on the objectors to the consolidation. The board seeks court injunctions to those who violate charter agreements as well as rate schedules. Cease-and-desist orders and civil and criminal penalties are assigned by the board for accounting and reporting violations. Service to less-populated communities is preserved by the continuance of CAB subsidies, reviewed semiannually.

Interestingly, deregulation did not significantly affect safety requirements or the functioning of the Federal Aviation Administration. Reflecting the general separation of economic and safety regulation, Congress recognized it could alter one without substantively affecting the other.

Deregulation of air travel, as ground transport, is important both for the functioning of that industry and for its implications for regulation in general. Its effectiveness will be seen in terms of preregulatory conditions
and in the rationales for and effects of deregulation in the years since its initiation.

REGULATION AND THE AIRLINE INDUSTRY

Due to its performance during the 1960s and 1970s, the CAB became criticized as operating according to protectionist principles that did not foster innovation and efficiency, a posture reflected in the areas of rates, entry, and route allocation. The evidence is strong that the CAB became protective and promoted an industry hurt by costs and the general level of the economy. The board's immediate concern for industry welfare overshadowed creative regulation that might have offered incentives for industry change.

In the area of price, rates did not take advantage of the nature of airline travel. Law professor and circuit judge Stephen Breyer points out that three characteristics define the industry in reference to rate making: the existence of a highly competitive array of companies; cyclical demand; and complexity and ambiguity in the valuation of services. These aspects make pricing difficult and require a flexible approach that does not apply rigid formulas over any protected periods of time.

Because the CAB prevented price competition in a highly competitive industry, the airlines turned to competition in the "extras"—food, service, types of planes, convenience of scheduling. During much of the 1960s, the board engaged in negotiation procedures with airline executives rather than formal hearings, and in this more informal way became immersed in the industry perspective and exceedingly well versed in airline problems. In addition, the Domestic Passenger Fare Investigation of the 1960s modified cost-of-service rate making by applying rates on an industry rather than firm-by-firm basis. As a result, the fare hikes reflected the condition of the economy rather than profits of individual firms. Yet, by preventing rate competition, this system, which lasted from 1970 through 1974, fostered competition in scheduling, so much so that the lines became overscheduled and capacity often fell below 50 percent.

In the area of entry and route assignment, the CAB showed little openness to new applicants. Between 1950 and 1974, the board received 79 applications from those wishing to enter the domestic scheduled airline business and granted none. Between 1969 and 1974, less than 4 percent of all applications from existing airlines for new routes were granted. The CAB also created cumbersome procedures, which benefited neither the industry nor the public. In 1975, 40 percent of all applicants had been waiting for over two years and 28 percent for over five years. Airlines remained confused as to the standards and criteria governing route
awards. Since the board had complete authority to grant or deny hearings, the process became unqualified by judicial review or the intervention of non-CAB authorities. Finally, between 1969 and 1974, the CAB refused to hear new applications under a period of route moratorium.\textsuperscript{18}

**The Kennedy Hearings and Reform**

The lackluster performance of the CAB—both for the interests of the airline industry and for the public—prompted an investigation of the Subcommittee on Administrative Practice and Procedure of the Senate Committee on the Judiciary, chaired by Senator Ted Kennedy. The agenda of the 1975 hearings became a series of questions, such as, Does the consumer pay for excess capacity in the airlines? What is the effect of price and entry regulation? Are the arguments against price competition valid?

Among the most significant findings of the hearings is the comparison between certain intrastate unregulated airline performance and the performance of regulated airlines. Intrastate fares in California and Texas remained 50 to 70 percent lower than fares for comparable distances on regulated routes between states.\textsuperscript{19} Although the industry countered that those states presented special cases of low congestion and route suitability, the subcommittee found that such considerations explained only a fraction of the rate differentials.

The subcommittee succeeded in crystalizing industry objections to deregulation. The airlines claimed that community service would be seriously curtailed, smaller communities finding service curtailed or cut off entirely. In addition, the decrease in stability would lead to firm closings and a nonwillingness among surviving airlines to take on additional risks involved with technological innovation. Labor would also be affected, wages decreasing and the general level of services deteriorating.

After an exhaustive presentation of evidence and a highly publicized series of hearings, the subcommittee drew its conclusions and made its recommendations. It found that the increased competition from deregulation would lower prices for the consumer while compelling industry efficiency. The subcommittee recommended that entry policy be liberalized and rate making left entirely open except for a rate ceiling. It also called for less leniency in antitrust action, so that the CAB would allow only those mergers that clearly do not affect competition.\textsuperscript{20}

During the interim between the Kennedy report and the passage of the Airline Deregulation Act of 1978, the CAB concurred with the essential Kennedy perspective. John Robson, chairman of the CAB appointed by President Ford, liberalized charter flight regulation as an experiment in deregulation and indication of the willingness of the CAB to change its
ways. The board also liberalized discounts for certain classes of tickets sold in advance. When economist Alfred Kahn replaced Robson as chairman in 1977, he espoused a deregulation position and further liberalized price and entry policy. As a result of price reductions, demand rose and passenger levels increased over 16 percent from June of 1977 to October of 1978.21

The Deregulation Act of 1978, then, may be seen as a continuance of the policies initiated in the CAB during 1975. The events serve as a contradiction to the theory of the self-perpetuation of bureaucracy since the act, supported by the CAB, calls for the termination of the CAB by 1985.

THE EFFECTS OF DEREGULATION

The early experience of airline deregulation indicates that the policy is a sound one. Despite rising fuel costs, a strike that grounded nearly 24 percent of the domestic air fleet in 1979, several serious crashes, an air controllers' strike, and a recessionary economy, the airlines have performed fairly well. During the first year of deregulation in 1979, the airlines held profit levels at the same rate as during regulation years while offering lowered fares and an increased volume of service. The increased volume, of course, is a reflection of the decrease in prices, which made flying available to more people, in spite of a reduction in discretionary income due to the recession.22 Passenger traffic grew 16 percent in 1978 and another 12 percent in 1979, and aircraft orders increased from 246 in 1977 to 410 in 1978.

Another area in which the early experience of airline deregulation indicates clear benefits is service to small communities. In spite of industry claims that less-populated areas would become vulnerable to service cuts, such has not proven to be the case. Where airlines did decrease service in the smallest airports, the commuter lines took up the slack. In 1982, the CAB released a report that indicated service to small communities actually improved under deregulation.23

Deregulation has also fostered a more rational policy concerning size and mergers. Under the new policy, the CAB is more oriented toward approving end-to-end mergers, that is, mergers involving two carriers that meet at common airports but do not compete over the same routes. These mergers allow for greater efficiency of service without reducing the competition between destinations. Ease of entry has allowed smaller airlines to offer competitive service, often demonstrating an economy of small scale. Comparatively small operations such as Midway Airlines and People Express offer low-price service by the availability of no-frills
flights. By operating according to the purpose of transporting an individual between two points rather than competing as a restaurant or a leisure activities service, the small airlines have gained a foothold in the market. In sum, a recent statement by Marvin S. Cohen, chairman of the CAB, indicated that "domestic deregulation has proceeded rather smoothly despite the unprecedented turbulence caused by the rapid escalation of fuel prices and the erratic course of the economy." All of this is not to say, however, that the airline industry is not in trouble. While profits on investment reached a high of 14 percent in 1978, they have continually declined since that time due to fuel increases and the condition of the economy. The bankruptcy of the first major airline under deregulation, Braniff International, manifested the problems affecting many carriers. Braniff found that a recessionary economy resulted in tighter credit practices and a squeeze on available operating and investment funds. Airlines have become a poorer credit risk for both banks and insurance companies, especially since it is difficult for investors to identify the secure areas of the industry.

Competition has become particularly intense. In 1982, 33 airlines carried passengers before deregulation, and 70 airlines had regularly scheduled passenger flights. The largest companies possessed an 86 percent share of domestic traffic in 1981, whereas they had had a 92 percent market share only two years earlier. Increased competition has driven up advertising costs. The Air Transport Association has estimated that the 16 major airlines spent $560 million on advertising and promotion in 1981, compared with $475 million in 1980 and $322 million in 1977.

The verdict on the deregulation measures is not yet entirely in. It is probable, though, that most of the airlines' problems relate to the condition of the economy as a whole, rather than to the loss of federal protection due to deregulation. The federal government, though, should not conceive of the present policies as permanent. When sectors of the economy are functioning well, they might not be in need of regulation; but when they falter, an adequate regulatory mechanism should go into effect. Firm closings may indicate a desirable flushing out of the less-efficient companies, but should they intensify to the point that service and prices are affected negatively, increased regulatory activity will again be called for.

Safety and Deregulation

The rationale for the present deregulation involves the assumption that economic and safety regulation may be separated so that the deregulation of the former does not compromise the standards of the latter. Generally, the Federal Aviation Administration has continued to function effectively.
It is continuing to establish and enforce safety rules and regulations, promote the expansion of airport facilities, operate and maintain the air traffic control network, establish international safety standards, and administer an air security program designed to inhibit criminal acts in airports and in the air. It has become a highly reliable source of data concerning aircraft, forecasts of aviation activity, systems plans to meet anticipated airway needs, and general aviation news. In addition, the administration proved itself able in handling the major air traffic controllers' strike, when it coordinated military controllers and its own staff in keeping the airways open.30

Yet, the persistence of serious aircraft accidents and malfunctions indicates that there is room for improvement. The areas that may be improved, however, do not relate to economic deregulation, but rather are methods employed by the administration in the enactment of its two major functions of air traffic control and air safety certification. Air traffic control could be improved by the work rotation of controllers, so that high-pressure tower work could be offset by some other duties, which could add more time to the length of service and the continued availability of experienced personnel.

A more serious problem is delineated by Robert W. Poole, Jr., an engineer and public policy analyst.31 Poole determined that, although FAA inspectors are in theory involved in the supervision of aircraft design and production, in practice many functions are left to the manufacturers. The system of delegation-option authority allows the manufacturer to carry out inspections under a type of honor system, which accounts for 70 percent of the inspection of large aircraft and 90 percent of the inspection of light aircraft. Another indication of inadequate regulation is the fact that the safety standards for the operation of the FAA's own fleet of planes are more stringent than those governing commercial airline flights. FAA pilots need at least 48 hours of piloting time within the past 12 months to legally fly, but there is no such requirement of the airlines. FAA pilots must have made five takeoffs and landings within 90 days, but commercial pilots need make only three within that time period.

There is indication that deregulation may have at least some impact upon safety. While the major carriers require from 10 to 20 years' experience in noncaptain cockpit positions, a smaller company such as the People Express will hire pilots as captains from the first day of employment.32 The pressure of competition and the drive to enter the market could potentially compromise the meticulous care required for consistent air safety. Again, the only answer lies in performance, and although, to date, there is no correlation between danger in the skies and deregulation, the situation should be carefully and continually monitored.
NOTES

1 43. Stat. 805.
2 44. Stat. 568.
4 48 Stat. 933.
7 Behrman, “Civil Aeronautics Board,” pp. 84-85.
13 72 Stat. 731.
14 80 Stat. 931.
15 92 Stat. 1705.
18 Breyer, *Regulation*, pp. 207-08.
20 Committee on the Judiciary, *Civil Aeronautics Board*, pp. 177-82.
130

The Uncertain Balance


CHAPTER 8
Nuclear Regulatory Commission

Nuclear power generation is the one industry that no analysts seriously consider deregulating. Given the unique hazards of nuclear energy—its intensity and the hazards of its waste products—nuclear regulation should not be compared with the railroads, air travel, business consolidation, or business practices. Rather, it must be considered on its own.

The hazards of underregulation of nuclear energy are far greater than those associated with overregulation in this area. Although the accident rate to date is low and more individuals lose their lives on average in mining coal and drilling oil, there has been a series of nuclear accidents with the potential of great damage, and the line between disaster averted and disaster is difficult to specify, though in some cases it appears to be extremely thin (see Table 8.1).

In this chapter, the desirability or nondesirability of nuclear power is not addressed, but rather, the regulatory issues are presented as they exist. The facts indicate that nuclear power generation is an established institution, at least for the foreseeable future. Nuclear energy accounted for only 1.5 percent of the contribution to electrical power generation in 1971, but by 1980 it accounted for 11 percent, and some estimates hold that by 1985 the percentage could expand to 19 percent. Orders for nuclear generating capacity proceeded from 1975 until 1979 (see Table 8.2). Although no new applications for NRC construction permits came forward in 1980 (after the Three Mile Island accident), it is unlikely that existing plants will go out of business. However, considering the skyrocketing costs of plant construction, the future of nuclear power generation may be in doubt for the next decade.

EARLY HISTORY AND LEGISLATIVE AUTHORITY

The Atomic Energy Act of 1946 created the Atomic Energy Commission (AEC), which remained essentially unchanged for the next 20 years. Five
Table 8.1
Nuclear Accidents

<table>
<thead>
<tr>
<th>Location</th>
<th>Date</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Three Mile Island, Pennsylvania</td>
<td>March 28, 1979</td>
<td>Pump failure caused large radioactivity releases. Young children and pregnant women were evacuated; the surrounding population was almost evacuated.</td>
</tr>
<tr>
<td>Browns Ferry, Alabama</td>
<td>March 22, 1975</td>
<td>Use of a candle to check for air leaks caused a serious accident with a potential meltdown in two large reactors.</td>
</tr>
<tr>
<td>Traverse Bay, Michigan</td>
<td>January 1971</td>
<td>A B-52 bomber flying over a Michigan reactor crashed a mere two miles from the site.</td>
</tr>
<tr>
<td>Hanford, Washington</td>
<td>September 30, 1970</td>
<td>A short circuit caused a new electrical circuit to form, cutting the reactor off totally from its scram (immediate shutdown) mechanism. Disaster was averted because the reactor was equipped with a backup scram system of a different design, which did lower the 87 control rods into the reactor's guts.</td>
</tr>
<tr>
<td>Enrico Fermi, Michigan</td>
<td>October 5, 1966</td>
<td>The first commercial breeder suffered a partial meltdown when a last-minute safety addition worked loose and blocked the coolant flow. A nuclear explosion could have resulted.</td>
</tr>
<tr>
<td>Shippingport, Pennsylvania</td>
<td>1964</td>
<td>Replacement steam generators, heavier than the original, were installed with faulty supports. They fell as they were being filled with coolant, preparatory to reactivation of the reactor.</td>
</tr>
<tr>
<td>Idaho Falls, Idaho</td>
<td>January 3, 1961</td>
<td>Three men were killed during a nuclear runaway at a small test reactor.</td>
</tr>
<tr>
<td>Idaho Falls, Idaho</td>
<td>November 1955</td>
<td>A core meltdown at a small experimental breeder reactor. The reactor came within a half-second of exploding.</td>
</tr>
</tbody>
</table>


Commissioners headed an organization that remained entirely separate from the military. Oversight of the commission consisted of a joint committee composed of nine members from each house of Congress and staffed with people from the AEC; the act provided for closer congressional scrutiny than is the case in other industrial affairs.

Due to political tensions, however, the Joint Committee on Atomic Energy failed to take an active oversight role during the years 1947-1948, and the newly appointed chairman of the AEC, David Lilienthal, kept
### Table 8.2

**Nuclear Power Generation, 1973–1982**

<table>
<thead>
<tr>
<th>Year</th>
<th>Billion Gross Kilowatt-Hours</th>
</tr>
</thead>
<tbody>
<tr>
<td>1973</td>
<td>88.0</td>
</tr>
<tr>
<td>1974</td>
<td>104.5</td>
</tr>
<tr>
<td>1975</td>
<td>181.8</td>
</tr>
<tr>
<td>1976</td>
<td>201.7</td>
</tr>
<tr>
<td>1977</td>
<td>263.3</td>
</tr>
<tr>
<td>1978</td>
<td>292.7</td>
</tr>
<tr>
<td>1979</td>
<td>270.7</td>
</tr>
<tr>
<td>1980</td>
<td>265.5</td>
</tr>
<tr>
<td>1981</td>
<td>288.6</td>
</tr>
<tr>
<td>1982 (January)</td>
<td>44.2</td>
</tr>
</tbody>
</table>


### Table 8.3

**Net Orders for Nuclear Generating Capacity, 1975–1979**

<table>
<thead>
<tr>
<th>Year</th>
<th>Orders</th>
<th>Cancellations</th>
<th>Net Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>NO. OF UNITS</td>
<td>CAPACITY (MWe)</td>
<td>NO. OF UNITS</td>
</tr>
<tr>
<td>1975</td>
<td>2</td>
<td>1,948</td>
<td>12</td>
</tr>
<tr>
<td>1976</td>
<td>3</td>
<td>3,790</td>
<td>3</td>
</tr>
<tr>
<td>1977</td>
<td>4</td>
<td>4,975</td>
<td>8</td>
</tr>
<tr>
<td>1978</td>
<td>2</td>
<td>2,240</td>
<td>11</td>
</tr>
<tr>
<td>1979 (August)</td>
<td>0</td>
<td>0</td>
<td>9</td>
</tr>
<tr>
<td>Total</td>
<td>11</td>
<td>12,953</td>
<td>43</td>
</tr>
</tbody>
</table>

relations with Congress at a minimal level. After 1949, the committee's activities increased, especially after the detonation of an atomic bomb by the Soviet Union.

With the successful generation of electricity in 1951 at the Argonne Laboratory in Idaho, the prospect of a private nuclear power generation industry became a possibility. Previously, only the military had engaged in nuclear power generation, but in 1953 the joint commission awarded a contract to Westinghouse to build a reactor and to the Duquesne Light Company to build and operate a generating plant.

A civilian nuclear power generation industry required additional legislation, which took the form of the Atomic Energy Act of 1954. This act provided for a relationship between public and private power generation that is identical to that established for conventional electrical power. While private power became the chief form, public generation coexisted and received preferential treatment in the licensing process. The Federal Power Commission would regulate rates. While nuclear fuel would continue to be the property of the government, it would be leased to the private companies on the basis of need. Licensing was the function of the AEC and consisted of experimental licenses for research and development as well as commercial licenses for power generation.

The first serious compromise of safety involved the mining of uranium. When the AEC became concerned that 85 percent of the United States' uranium needs were supplied by the Belgian Congo as of 1949, it fostered an American uranium mining industry. Evidence surfaced that safety precautions were inadequate, and miners began to manifest lung damage from the radiation, but the AEC did not pursue the problem and discouraged investigations. The Colorado Health Department managed to communicate the importance of the problem, and the Joint Committee on Atomic Energy eventually held hearings in 1959. Yet, partially as a reflection of the Cold War emphasis upon nuclear power and a hesitancy to curtail its development, no major overhaul of mining procedures ensued.

Only an Idaho accident in which three men were killed in 1961 halted Consolidated Edison's plan to build a nuclear plant right in New York City. Still, in 1967, the AEC relaxed its siting requirements for reasons of economic efficiency, deciding that it was possible for engineering to compensate for the safety disadvantages inherent in locations near populated areas.

In an effort to reorganize the safety and economic regulation of atomic energy, Congress passed the Energy Reorganization Act of 1974, which created the Nuclear Regulatory Commission (NRC) as a replacement for the Atomic Energy Commission.3
ORGANIZATION AND FUNCTIONS

Offices, Staffing, and Budget

The NRC is headed by five commissioners who are appointed by the president and confirmed by the Senate. In order to ensure bipartisan orientation, no more than three commissioners may be members of the same political party. Commissioners serve five-year terms, and the chairman is appointed by the president.

The Energy Reorganization Act of 1974 provided for three major divisions. The Office of Nuclear Reactor Regulation is responsible for licensing nuclear reactors that are used for testing, research, and power generation. The Office of Nuclear Material Safety and Safeguards regulates safety, both in the areas of health and security as well as in theft and sabotage. The Office of Nuclear Regulatory Research administers the research programs. Since 1974, two additional offices have been created, the Office of Standards Development and the Office of Inspection and Enforcement. The Office of Standards Development prepared standards for plants and protection of the environment and merged its functions with the Office of Nuclear Regulatory Research in 1980. The Office of Inspection and Enforcement is responsible for the inspection of nuclear facilities and also investigates accidents and allegations of improper construction and operation.

Staff offices include an Office of General Counsel, which provides legal information and advice as well as providing legal analysis and drafting legal documents. The Office of Policy Evaluation serves the purpose of commission self-evaluation. Inspection, public affairs, and congressional offices handle, respectively, staff monitoring, public information, and congressional liaison. In addition, numerous support offices are involved with the administration and operation of the commission (see Figure 8.1).

In 1980, Congress instituted President Carter's reorganization plan, which gave the chairman of the NRC increased authority for responding to nuclear emergencies. It also made the director of agency operations directly report to the chairman in order to facilitate intra-agency communications and give the chairman increased control over staff operations.

Budget levels for the NRC significantly increased over budget appropriation levels of the AEC, reflecting the proportional increase in importance of nuclear power to total energy production as well as the increased sensitivity to safety issues. The staff level nearly doubled between 1974 and 1980. The staff level rose from 3,041 in 1980 to 3,336 in 1981, a change that is primarily reflective of the improved regulatory requirements instituted after the Three Mile Island accident in 1979 (see Table 8.4).
Table 8.4

NRC Budgets and Staffing for Fiscal Years 1970–1980

<table>
<thead>
<tr>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>BUDGET ($MILLIONS)</td>
<td>12</td>
<td>16</td>
<td>27</td>
<td>45</td>
<td>80</td>
<td>180</td>
<td>231</td>
<td>271</td>
<td>309</td>
<td>378</td>
<td></td>
</tr>
<tr>
<td>STAFFING</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>1,538</td>
<td>2,006</td>
<td>2,289</td>
<td>2,499</td>
<td>2,666</td>
<td>2,472</td>
<td>3,041</td>
<td></td>
</tr>
</tbody>
</table>


Of NRC resources, nearly half go toward research into new methods, processes, and means of obtaining safer and more efficient nuclear energy. Inspection and enforcement has recently taken 12-13 percent of the budget, reactor regulation about 16 percent, and program direction and administration between 8 percent and 9 percent (see Figure 8.2).

Licensing and Siting

The licensing process is necessarily complex since it is connected to matters of efficient operation and safety. A company wishing to operate a nuclear facility must first obtain an NRC construction permit. The NRC has devised a series of requirements that translates into the provision of approximately ten or more volumes of application materials, which describe safety and environmental factors. The second phase consists of safety and environmental evaluation as well as antitrust review by the NRC. Prelicensing antitrust reviews generally involve a hearing, when one is recommended by the attorney general, in order to determine if the issuance of a license would violate antitrust regulations. Antitrust review is repeated before a firm goes into operation to determine whether the pattern of competition had changed since the construction phase. The third aspect of the licensing process involves a safety review by the independent Advisory Committee on Reactor Safeguards (ACRS). Fourth, a public hearing is conducted by the three-member Atomic Safety and Licensing Board, which makes an initial decision as to whether or not to grant the permit. Their decision may be appealed to the Atomic Safety
**Figure 8.2 Nuclear Regulatory Commission**

NRC RESOURCES
FY 1980*

Personnel -3041

Funds—$396 Million

*Includes FY 1980 Supplemental Authorization
RESOURCE ALLOCATIONS

NRC RESOURCES
FY 1981

Personnel—3336

Funds—$466 Million

and Licensing Appeal Board, and finally to the commissioners of the Nuclear Regulatory Commission. The licensing process, then, involves three independent units outside of the NRC.

When the initial application has been accepted by the NRC, a notice is published in the Federal Register along with a notice of a public hearing. In the meantime, NRC safety, safeguards, environmental, and antitrust reviews proceed. The applicant's preliminary safety analysis report is scrutinized, and a safety evaluation report is prepared by the NRC staff and published. The ACRS reports the evaluation findings to the chairman of the NRC. While this process is continuing, the NRC may grant a limited work authorization to allow an applicant to do some initial work at the site, which may save as much time as seven months.

The environmental review begins when the applicant submits an environmental report. The NRC completes a draft environmental statement, publishes it, and distributes it to various federal, state, and local agencies. The NRC then writes a final environmental statement, which is taken into account in the final licensing decision.

Two to three years before the scheduled opening of the plant, the applicant files for an operating license. A similar process to the construction permit is followed, and a safety evaluation report as well as an updated environmental report are issued. After the plant is operational, it remains under NRC inspection and surveillance throughout its operating life.

Some critics claim that the licensing process is too long and costly. They point out that the time involved between the planning and operational stages of a plant is now at least 10 years, over twice that of a decade ago. Federal and state requirements may repeat or contradict each other. Reformers call for complete public participation before the submission of an application to build a plant, site evaluation early in the process, and the elimination of duplications between state and federal authorities.4

Protracted licensing procedures are extremely expensive. Figures presented to the Congress indicate that if the design and construction durations could be reduced from an average of 11 years to an average of 8 years, the average family's electric bill would be reduced about $40 a year for a 30-year plant life. The cost of many units would be reduced from $450 million to $260 million, and demand on capital markets would be decreased by $27-47 billion during the next several years.5

These arguments are persuasive on one level of economic analysis, but a broader approach should be taken. The risks involved are so acute and the potential losses so great that extreme caution should be taken in any reduction of licensing procedures. There is merit to reducing redundancies between state and federal regulations, but the proposals to settle issues of site selection and public input early in the process are not sound. In an area
of technological complexity in which years of planning are required even without the licensing process, conditions—social and physical—continually change. The amount of information required is too great to disallow submission of evidence at the latter stages of decision making.

Improvements have been made in the licensing process. In 1980, a reorganization of the NRC Office of Nuclear Reactor Regulation allowed for a more interdisciplinary approach to licensing. It also created a division specializing in the human factors involved in safety, including control room design, emergency procedures, initial test programs, and technical competence.

Licensing goes to the heart of safety regulation since it involves the entire framework—the facilities and the procedures—that defines the nature of the plant. It is not surprising that it is expensive. But there is justification to the view that one of the major costs, if not the major cost, in nuclear power production should be safety. The issue is so crucial that any change should be gradual and a high priority concern of the Congress.

An important safety issue is the selection of site location (see Figure 8.3). This is important not only because of the danger to populations surrounding the plant should a reactor problem occur but because of the proximity of people to the transportation of highly toxic nuclear wastes. The policy that the lack of remote siting may be compensated for by improved engineering is ill-founded. Enough accidents have occurred to establish that nuclear plants are not likely to become accident-proof. The mere reliance on human judgment indicates that problems will occur in the future. In 1978, an NRC Siting Policy Task Force stressed that requirements for site approval should be independent of site design, in other words, engineering improvements cannot compensate for plants located in densely populated areas.6

Waste Management

One of the most serious dilemmas in nuclear energy production is the problem of radioactive waste. The creation of large quantities of manmade radioactive materials is an unavoidable aspect of the fission process. Since these wastes remain dangerous for hundreds and in some cases thousands of years, the problem becomes one that intensifies as the industry develops.7

Waste management is a two-pronged problem. The NRC must set regulations both for the transportation and for the storage of radioactive materials. The General Services Administration found that a number of unknowns make the situation particularly dangerous. Due to geological
Figure 8.3
NRC Regional Offices and Commercial Nuclear Power Reactors in the United States

difficulties such as the possibility of earthquakes and tornadoes, storage locations are difficult to select. The behavior of materials and containers is likewise uncertain over long periods of time, especially in the areas of material solidification and container stress cracks.

The regulation of the transportation of wastes is shared between the Nuclear Regulatory Commission and the Department of Transportation. In 1979, the General Accounting Office indicated that the NRC should amend its regulations to better screen the delivery of packages for leakage. Although no serious trucking accidents have yet occurred, it is still not clear whether packaging standards would adequately protect the contents under the impact of a severe collision. Since the materials are transported through urban areas, a risk of unknown degree is continually being taken.8

In 1982, a U.S. Court of Appeals ruled invalid an NRC method of determining nuclear waste hazard. The NRC guidelines liberalized waste control requirements on the grounds that waste management will ultimately be a federal responsibility, since it has pledged someday to bury nuclear waste permanently far below the earth's surface. The court found that since Congress had instituted no timetables, the NRC could not proceed under the assumption of federal responsibility.9

**Inspection and Enforcement**

The NRC's Inspection and Enforcement Program is directed by the Office of Inspection and Enforcement (IE), headquartered in Bethesda, Maryland, with five regional offices. The IE staff reached 846 in fiscal 1980 and conducted 5,416 inspections during that year.10 Inspections are either routine or reactive. Routine inspections include observation, review, interviews, checks, and where possible direct measurement of licensee equipment, functioning, and personnel. Reactive inspections occur in response to specific reports. Increased monitoring vigilance became expedited by the resident inspector program, whereby inspectors remain full time at selected nuclear power sites.

The NRC has several modes of enforcement actions. It may serve written notices of violation, consider civil penalties, or order cease-and-desist directives. In 1980, the commission imposed 49 civil penalties on licensees representing total fines of $1.4 million and issued 26 cease-and-desist orders in order to gain compliance to NRC rules.

**State Coordination and Public Information**

Under the States Agreements Program, the NRC enters into arrangements with individual states for the regulation of byproduct and source
materials involved in nuclear power generation. The NRC also offers technical assistance to the states in licensing matters, health physics, environmental analysis, proposed regulation review, and guidance for state inspection and enforcement. In addition, the agency offers training for state personnel in the field of nuclear regulation. Because of the close working relationship between the NRC and the states, in 1980 there were 51 state liaison officers assigned to the NRC. As required by legislation passed in 1980, the agency now requires licensees to notify governors in advance of shipments of hazardous materials through their states.

Although state action is a necessary complement to federal regulation, the federal level should remain responsible for the ultimate setting of standards. Without such supremacy, nuclear regulation would become uneven throughout the nation, some states operating according to safer standards than others. Federal regulation should represent the highest level of regulation achieved by an individual state.

Because the costs and dangers of nuclear power are so extensive, the area is a public issue, and information should be made as available as possible. As held by the government in the Sunshine Act and Freedom of Information Act, commission deliberations are a matter of public record except where matters of national security or corporate secrecy are involved, and materials are placed in a Public Documents Room. In 1980, the commission conducted three-quarters of its meetings in open session.

**THREE MILE ISLAND**

March 28, 1979, marks the most publicized nuclear reactor accident to date. A Metropolitan Edison Company reactor near Harrisburg, Pennsylvania, on the Three Mile Island malfunctioned when a pump failed. Operators, misled by a faulty instrument, made the error of turning off the emergency cooling system. As a result, the reactor heated up dangerously and threatened to melt to the core.

A combination of the potential hazards of a meltdown, the release of some (but later determined safe) radiation, and media attention turned the incident into a means of evaluating the entire nuclear industry and the functioning of the NRC. President Carter, who had served on a nuclear submarine and had a background in nuclear engineering, personally visited the site of the accident to allay the fear of the public and appointed a commission to evaluate fully the circumstances and implications of the accident.

The Kemeny Commission, chaired by president of Dartmouth College John Kemeny, analyzed the nature of the accident and made 44 specific recommendations and 77 supplemental suggestions. The report
concluded that the training of the operators was deficient in that they were not prepared to deal with extraordinary circumstances. Emergency preparedness was sadly lacking as well, since reaction time was slow and procedural confusion rampant.

Among the more important recommendations of the Kemeny Commission is that the five-member Nuclear Regulatory Commission be abolished and replaced by a new executive agency under a single administrator. In this manner, communication within the agency would be improved and reaction to unusual circumstances facilitated. A policy of remote siting should be instituted to the maximum extent possible. It also called for serious consideration of shutting down plants located near Chicago and New York City. Licensing requirements, in general, should be made more stringent. Equipment should be reviewed more frequently and greater applications made of computers. Accident investigations should be more extensive and emergency planning entirely overhauled, with the states better involved in systematic public information provision.

The report was useful in illuminating the emphases and biases in NRC actions. It found that emergency planning had a low priority in the commission. The NRC had not made the existence of a state emergency or evacuation plan a condition for plant licensing. Nor was it crisis-oriented, as it took the NRC about two days to determine and understand the seriousness of the accident, even though representatives were on the emergency site within hours of the declaration of the emergency. Communications between these individuals and the upper levels of the commission remained fragmented and unclear. While the NRC had required emergency planning for an area of only two miles about Three Mile Island, the state of Pennsylvania actually had more stringent requirements and prepared for an area covering five miles. In addition, based on poor information, NRC scientists drew incorrect conclusions about the behavior of a hydrogen bubble in the reactor vessel.12

A special inquiry group within the Nuclear Regulatory Commission came forward with conclusions similar to those of the Kemeny Commission. It concurred that the major problems in nuclear energy involve management rather than hardware and recommended more stringent licensing procedures as well as an overhaul in training and operating processes. It also called for placing more resources in the inspection area.

The Senate became involved in investigating the accident and established a special Senate investigation of the TMI accident under the sponsorship of the Senate Committee on Environment and Public Works. This investigation cleared the operators of any willful concealment of their handling and involvement of the accident. Acknowledging the gravity of the situation, the report discussed the viability of evacuating sectors of the
population. The General Accounting Office issued its own report to the Congress on the Three Mile Island in September of 1980. This report called for skepticism about the effectiveness of emergency backup systems and the necessity of emergency planning at all levels of government, it endorsed increased power for the chairman of the NRC and called for the delineation of goals and standards for a definition of safe conditions.\textsuperscript{13}

President Carter rejected the Kemeny Commission's proposal for the establishment of an administrative agency within the executive branch to replace the NRC. Instead, he successfully instituted the expansion of the chairman's powers described earlier in this chapter. The chairman, in effect, became a chief executive officer rather than the facilitator of a deliberative committee.\textsuperscript{14}

SAFETY

The experience of Three Mile Island, more than any other single incident, points out that the central theme in the regulation of nuclear power is safety. Each year, the Nuclear Regulatory Commission lists what it euphemistically terms \textit{abnormal occurrences}. In 1979 and 1980 many of these accidents took place. In Palisades Nuclear Power Station in Michigan, valves were left open for more than a year; at Uranium Mill, New Mexico, a dam failed and contaminated solutions poured through a break into a catchment area below the dam; and Nuclear Fuel Services, Inc. showed inventory discrepancies for uranium in its records. At a facility in Pennsylvania, a worker inhaled plutonium, and in 1980 an incident similar to the Three Mile Island problem occurred at Crystal River in Florida during which electrical indicators failed and coolant was subsequently lost. Heat removal capability was lost at Davis-Besse in Ohio, and 76 control rods failed to function at Browns Ferry in Alabama.\textsuperscript{15} It is clear that concern over nuclear power safety is rational, and not alarmist, as some social scientists claim.\textsuperscript{16}

The fact is that we still know relatively little about nuclear power. The extent of the imponderables in the nuclear area was dramatically illustrated when the research scientists who enacted the first nuclear explosion in the 1940s addressed the question of whether a nuclear explosion could explode the entire atmosphere. The long-term effects of radiation exposure are not precisely known, though a sufficient dose is definitely carcinogenic. The possibilities of terrorism are difficult to contemplate, but an attack upon a nuclear reactor or even the attempted construction of a nuclear bomb is not an impossibility.\textsuperscript{17}

No new licenses were granted after the Three Mile Island accident, and in March of 1982, the NRC reported that utilities were considering canceling
or delaying 19 nuclear power plants then under construction.\textsuperscript{18} An Associated Press survey of the previous month indicated that of the 72 licensed plants in the United States (not including three plants shut down indefinitely), 25 were out of service as of February 6. Although 10 were shut down due to scheduled maintenance or refueling, the remaining 15 had technical problems.\textsuperscript{19}

One result of technical difficulties and construction costs is higher utility charges. Many estimates indicate higher rates for nuclear-generated electricity than for that from coal. The performance of nuclear power in France is likewise questionable. Production costs have remained high, and public opposition has mounted during the past several years. Yet, there is no talk of dismantling the nuclear energy industry in the United States, and it is likely nuclear power will play a role in the economy at least for the foreseeable future.

Few people are entirely comfortable with nuclear power. Such discomfort was dramatically illustrated by Admiral Rickover in testimony before the Senate. The admiral, who was among the foremost supporters of the introduction of nuclear-powered submarines, stated:

I'll be philosophical. Until about two billion years ago it was impossible to have any life on earth. That is, there was so much radiation on earth you couldn't have any life. . . . Gradually, about two billion years ago, the amount of radiation on this planet and probably in the entire system reduced and made it possible for some form of life to begin. . . . Now when we go back to using nuclear power we are creating something which nature tried to destroy to make life possible.\textsuperscript{20}

\textbf{NOTES}

2 60 Stat. 775.
14 “A New Call for Abolishing the NRC,” *Science* 207 (February 8, 1980), pp. 624, 626.
EARLY HISTORY AND LEGISLATIVE AUTHORITY

The Securities and Exchange Commission owes its birth to the intensive need felt during the early 1930s to regulate corporate securities. Prior to that time, the major task of corporate securities regulation had rested with the states, which, in competition to attract businesses, usually established lenient requirements.

The outstanding examples of such leniency are New Jersey and Delaware. In 1896, New Jersey's revision of corporate laws allowed for unlimited market size and concentration, while leaving it up to the corporations to set the value of newly purchased companies. Following New Jersey's lead, Delaware liberalized its conditions in the General Corporation Law of 1899, which allowed for the dilution of shareholder voting rights and made it difficult for them to sell their shares back to the corporation before a merger. The cumulative effect of these laws made it difficult for the investor to know the true status of corporations and to base investment decisions on solid data.

Some periodic state efforts were made. The 1879 state constitution of California prohibited the margin trading of securities, which involves the purchase of securities paid in part by a loan using the same securities as collateral. In 1911, a Kansas law established a state securities commission to judge upon the merit of securities offered for sale within the state and suspend the sales of those deemed fraudulent. The practice expanded until every state except Nevada had established such laws. Other state securities regulatory efforts included the licensing of dealers, the registration of stock, and the establishment of sanctions for those involved in fraudulent practices.

Before the 1930s, federal involvement had been minimal. The only statutory protection of cheated investors was the fraud clause of the U.S.
Postal Law, the enforcement of which was not effective. In 1913, the House Committee on Banking and Currency under A.J. Pujo publicized abuses such as bank officers borrowing their own bank’s assets for personal investment purposes, insiders with special information manipulating prices, the separation of banking from investment operations, and outright misrepresentation by securities dealers. However, bills requiring registration of data with the secretary of the treasury and authorizing the U.S. attorney general to determine the validity of securities offers and prosecute violators failed to gain passage.

Abuses continued throughout the 1920s. Investment proceeded—at times at a feverish pace—as the prospect of “get rich quick” took hold of the imagination of many following the trauma of World War I. Under the unrealistic assumption of massive industrial growth and business success, credit was granted on the easiest of terms and margin trading proliferated. Within the context of a bullish market, corporate managers misrepresented the nature of business plans, and dealers and brokers pushed highly questionable and even worthless securities in the pursuit of commissions. Pools of investors colluded to manipulate stock prices in order to make large profits, at times making use of inside information.

In addition, banks, which had participated in nearly two-thirds of all new stock and bond issues, lent money on favorable terms to their own investment affiliates. Banks, in return for underwriting business, often considered corporate loan requests more favorably. The same banks also favored the purchase of securities in their trust departments or securities written by their corporate affiliates. Congressional hearings discovered that Chase National had absorbed $10 million in questionable securities to aid its securities affiliate, and National City had offered its subsidiary about $25 million in speculative loans paid out of new stock issues.3

While individuals continued to be hurt, it took the crash of 1929 and the first few years of severe economic depression to alert the public that the securities industry suffered from underregulation. The Securities Act of 1933, originally administered by the Federal Trade Commission, required the filing of financial and other data about the issuer and the securities for sale in interstate commerce or through the mails with the federal government.4 Exemptions were made in the areas of small investments, offerings restricted within states, government securities, and those of charitable organizations. Accomplishment of public disclosure is obtained by registration statements, including publication of prospectuses. Registration statements generally contain information on the registrant’s property and business, a description of securities, management information, and public accountant-certified financial statements.

Liability is also delineated. Execution of the registration statement lies with the principal executive officer, financial officer, controller or
accountant, and a majority of the board of directors. Liability for fraud lies with each of these parties as well as every person consenting to be named as being or about to become a director. Liability also extends to experts who have prepared or certified any part of the statement, as well as every underwriter of the security. These individuals are subject to civil liabilities and criminal penalties for crimes of omission or commission. The law is based on the “full disclosure” model espoused by Louis D. Brandeis rather than the state “blue sky” statutes, which allowed regulators to judge the merits of new security offerings.

The Securities and Exchange Commission (SEC) was created by the Securities and Exchange Act of 1934. Registration as well as annual and periodic reports are made to the commission detailing the performance and health of the registered companies. Additional requirements include the complete detailing of information to be voted on in proxy matters, the provision of full information to stockholders concerning tender offers to buy up stock in a company, the requirement that corporate officers or insiders and those holding over 10 percent of the total company stock report changes in their holdings, and the registration of all national exchanges, brokers, and dealers who conduct business over the counter.

The principle of disclosure is considered to benefit the consumer and the economy in several ways. It reduces the likelihood of fraud to investors who would otherwise be misled, as well as the inadvertent misrepresentation of financial statements. Such reporting reduces the possibility of price manipulation that is made possible by the inadequate disclosure of information. The publication of information encourages greater efficiency and sophistication in investment decisions, which can only benefit the economy. Finally, a feeling of public confidence is fostered, which encourages economic stability.

While the laws of 1933 and 1934 form the foundation of securities regulation, several laws have been passed since that time to deal with specific problems and expand the scope of SEC regulation. The Public Utility Holding Company Act of 1935 requires public utility holding companies in the areas of gas and electricity to register with the SEC and file reports, and the Bankruptcy Act of 1938 has the SEC aid the courts during bankruptcy proceedings. The Trust Indenture Act of 1939 requires that trust indentures, arrangements where trusts are formed for the purpose of offering securities for sale in order to finance debts, must demonstrate a lack of trustee conflict of interest; the Investment Company Act of 1940 requires investment companies to register with the SEC and subjects them to regulation; and the Investment Advisers Act of 1940 requires similar regulation of investment advisors.

The next significant piece of securities legislation did not appear until 1970, with the passage of the Securities Investor Protection Act, which
came after a series of adjustments in the securities industry during the 1960s. The Report of the Special Study of Securities Markets, authorized by Congress and published in 1963, recommended more stringent requirements for those wishing to become brokers and dealers, which led to the Securities Act Amendments of 1964. During the 1960s, the SEC had ruled concerning dealer eligibility and set standards concerning the activities of specialists. But the Securities Investment Protection Act served as a systematic authorization to develop new standards of financial responsibility for brokers and dealers, and to establish a broker-dealer examination program in cooperation with an independent nongovernmental Securities Investor Protection Corporation, with the continuance of surveillance of self-regulatory efforts within the industry.

Finally, the Securities Acts Amendments of 1975, an extremely important piece of legislation, authorizes the SEC to develop a national system of buying and selling stocks; the Foreign Corrupt Practices Act of 1977 gives the SEC authority to prevent the improper gaining of influence with foreign governments by means such as bribery; and the Small Business Investment Incentive Act of 1980 exempts certain small and medium-sized businesses from registration requirements.

The 1975 Securities Acts Amendments are especially important because they provide for a national market system that links communications and data processing for all markets. The central market is composed of systematic trading rules and composite quotation systems to facilitate transactions. It also provides for a consortium of organizations under the authority of the SEC to administer the system. As of 1982, the system gained application on a limited basis. The amendments also affect competition in the securities industry since the commission is to eliminate the rules of exchanges that are anticompetitive, such as the establishment of fixed rates of broker commissions. In sum, the amendments provide for the extension of SEC authority over automated systems, unjustified competitive restraints, exchange trading and unlisted securities, rates of commission, and trading by institutions. This increased scope of activities amounts to a major overhaul of the 1934 act.

**ORGANIZATION AND FUNCTIONS**

The SEC is run by a five-member commission, no more than three of whom belong to the same political party, who are nominated by the president and confirmed by the Senate for five-year terms. The commission is responsible for holding hearings and issuing rules as well as evaluating evidence to decide upon prosecutions. The Office of Administrative Law Judges conducts hearings, subject to commission
review, which may be appealed in the U.S. Court of Appeals. An Office of Opinions and Review aids the commission in preparing decisions and opinions. Offices of economic policy and analysis, corporate regulation, investment management, market regulation, consumer affairs, public affairs, and applications administer specific acts and conduct research in their respective areas. Support and executive functions are offered by an executive director, a general counsel, and offices of data processing, administrative services, and personnel (see Figure 9.1).

The work of the SEC begins with the initial public offerings of securities of a company. The Division of Corporation Finance reviews registration statements for compliance with disclosure requirements. If no action is taken to correct shortcomings, the commission may suspend the issuance of the securities and a hearing may be held. Stop order actions are revoked when the inadequacies are rectified. Various divisions survey required reporting materials concerning proxy (corporate voting) reports, acquisition plans, and inside trading information.

The commission’s regional offices, under the direction of the Division of Enforcement, are primarily responsible for matters of investigation and enforcement. Most of the investigations are performed privately, utilizing informal interviewing and record examinations, but the commission may subpoena testimony and records. The commission reacts to complaints and inquiries from the public as well as initiating its own investigations. It may look into matters of sale and registration of securities, misrepresentation, mispledging of funds, market manipulations, unreasonable price transactions, and secret profit taking by trusted broker-dealers.

The commission has several courses of action and remedies upon the determination of a violation: (1) civil injunctions, U.S. district court orders preventing acts or practices alleged as violations of laws of commission rules; (2) criminal prosecution, Justice Department court actions referred by the SEC; and (3) administrative remedies, SEC orders following hearings suspending or revoking privileges or censuring individuals.

The data indicates that the SEC has remained on a consistent level of efficiency, if costs of agency operation are compared with the quantity of work accomplished and the amount of fees collected. Increases in broker-dealer commissions, which reflect the quantity of security trading activity, roughly parallel the net cost of commission operations and the fees collected for the registration of securities, securities transactions on national security exchanges, and miscellaneous filings, reports, and applications. The commission is unusually cost-effective in its operations in that in fiscal year 1980 it collected $49 million in fees, which represents 68 percent of its appropriated funds.13
COSTS AND BENEFITS OF DISCLOSURE

As is the case with every regulatory agency, there are those who believe the SEC has overstepped its purpose and creates costs that are greater than the benefits it delivers. The most elaborate case is made by George J. Benston, a professor at the University of Rochester's Graduate School of Management. He concludes that voluntary disclosure would be an effective means of guarding the rights of investors in honest corporations. Since prospective shareholders demand information, which will be produced by market demand by independent financial accountants, the corporations will fully cooperate in order to establish their own credibility. In reference to dishonest corporations, Benston argues that regulated disclosure of the SEC is of limited value since auditors stand at a distance from the market data and only create a subset of information needed by investors to make decisions. Disclosed information also involves artificially imposed time frames that could distort the long-term performance outlook of a firm. Second, companies attempt to mislead investors more in the area of future outlook rather than past performance, floating false rumors and distorted upcoming prospects. Third, dishonest corporations engaged in voluntary disclosure would be subjected to the rigors of independent certified public accountants seeking to preserve their own reputations.

Benston proceeds to divide the current costs of mandated disclosure into direct and indirect costs. Direct costs include the costs of record keeping, auditing, report preparation, and administration involved in filling out forms such as the 10-K (annual report), 10-Q (quarterly report), and 8-K (monthly report). For fiscal 1976, annual direct reporting costs for 9,784 regulated companies came to $213.5 million. The SEC’s requirements for new-issue registration is estimated to add up to $2.70 per $100 raised in some cases. Indirect costs are mainly opportunity costs, which are the advantages lost due to SEC requirements. For example, the SEC disallows the inclusion in prospectuses of forecasts, which might attract investors.

Next, the rationale for security regulation is addressed by Benston in its specific aspects: the prevention of fraud, misrepresentation, price manipulation, and nonavailability of data. In the area of fraud, Benston argues that there is no evidence that fraudulent financial statements were common before 1934, since very few cases reached the courts. Misrepresentation, or the selection of facts with the purpose of distorting the full picture, is not an effective means of fooling investors. Price manipulation has little to do with information disclosure, and information availability would emerge due to investor demand in an unregulated context. Benston concludes that the beneficiaries of government-mandated disclosure are the government agents who use and administer the data, securities analysts and firms that process the data for sale to the public, accountants, and lawyers.14
Another critic is a former SEC commissioner, Roberta Karmel. In a speech in 1979, she stated, "I believe that a skeptical attitude toward government-mandated disclosure is the best antidote for unwarranted extensions of disclosure policy into areas beyond reasonable investor concern." Her book holds the provocative title, *Regulation by Prosecution: The Securities and Exchange Commission vs. Corporate America.* Her thesis is that the SEC became overzealous, and by resorting too often to prosecution, it served to impede the crucial processes of capital formation.

Karmel traces the shape of the history of the SEC, its activist posture in the 1930s, but nonactivist approach in the 1940s and 1950s, which resulted in a major stock fraud scandal in the 1950s, its resurge of energy in the 1960s, when it expanded its functions under Kennedy appointee William L. Carey. Karmel argues that the SEC functioned effectively through the late 1960s and early 1970s, but by the middle of the decade had become overextended. The amendments of 1975 expanding the scope of the SEC's regulatory realm, and the climate of antibusiness opinion that built before that time, infused the commission with an adversarial ethic. Rather than interpreting its mandate as one of disclosure for investor and shareholder benefit, it sought to alter the conduct of corporate management. It became involved with regulating corporate governance, the sharing of corporate power with shareholders through their input into corporate decision making. Karmel seeks a reduction in the number of regulatory agencies with power over capital markets and financial institutions and a spirit of cooperative effort with business over compulsion for adversity.

Karmel also feels that technology allows for greater deregulation:

Securities regulation and government regulation of business generally must place greater responsibility on the private sector for developing and following appropriate standards of conduct. Since communications technology is so much more advanced today than it was when New Deal agencies like the SEC were created, the marketplace is capable of a greater degree of self-policing than formerly was the case. Both government officials and the public must develop greater appreciation for the links between capitalism, freedom, and prosperity, and we must make those links stronger. Accordingly, regulation designed for the purpose of achieving greater social justice through increased prosperity must enthusiastically endorse private enterprise and administrative due process.

Those more enthusiastic about the performance of the SEC respond that critics such as Benston and Karmel manifest too much confidence in self-regulation. They state that regulatory history indicates that regulations are established not in reference to businesses with the highest standards of efficiency, quality, and ethics but to those with the lowest. Just as a manufacturer of a product with high-quality ingredients welcomes rather than fears labeling requirements, the management of a solid company will not be hindered by open securities disclosure.
The application of the biological model stresses that the channeling of capital is a crucial aspect of economic functioning. The sale of securities is analogous to the channeling of energy in the body, capital representing the impetus for action. This energy, capital, is used to optimal effect when it serves to generate more energy, or, in terms of capital, profits that allow for expansion. Capital is best used when it is awarded to the ablest companies. The mandated disclosure of information can only help the ablest companies to gain the public exposure necessary for informed investment. The direction of capital is then more likely to be guided by analysis, rather than by rumor, pressure sales tactics, and groundless optimism.

The regulatory response continues that Benston's arguments for deregulation do not follow from the experience of underregulated periods, such as the 1920s. Karmel's view that technology is conducive to deregulation also is seen as overly optimistic. Computers are not fraud-proof, and they bring with them a new set of regulatory issues. Do they provide all parties with the same information and at the same time? Will a national market system remain standardized, or will some find ways to obtain special advantage? What are the liabilities of electronic equipment and the procedures during malfunctions? Do individual exchanges depart from standard practices? Regulationists continue that, if anything, computers offer the opportunity for increased regulatory surveillance. The SEC is developing a computerized market oversight surveillance system, for example, to allow it to keep an eye on all the nation's stock and option exchanges. Former commissioner of the SEC Andrew Loomis, Jr., indicates that regulation fosters a climate of expectation within corporations, so that they remain precise and detailed in their reporting, given an awareness of SEC involvement.

In the early 1980s, however, some deregulatory efforts were made. The commission's budget declined $188,000 in fiscal 1982 from 1981, and Chairman John S. R. Shad, Reagan's nominee, announced a commitment to easing requirements in a limited manner. Budget cutbacks made it necessary for the SEC to concentrate on the most important cases, and Shad instituted a policy of easing pressure on companies to disclose on unsubstantiated charges. The commission raised the ceiling to $100,000 for the amount a small business may raise through the sale of securities without registering with the SEC. While the agency's top officers vetoed violation enforcement in .9 percent of the cases in 1980, in 1981 they vetoed 2.5 percent of the cases. The agency also considered easing requirements on utility disclosure and the private sale of stocks. In general, there is now a greater presumption of innocence.

These changes are relatively minor adjustments designed in reference to recessionary economic conditions. Since the main thrusts of the SEC efforts continue, it appears unlikely that major abuses in the security industry will ensue.
NOTES

9 84 Stat. 1636.
CHAPTER 10

Protection: OSHA, FDA, and EPA

The agencies discussed in this chapter are engaged in what is commonly termed new-style or social regulation. Whereas old-style regulations tend to be economic and regulate the means of doing business, such as entry requirements, rates and obligations, new-style regulations tend to address the conditions of economic activity and the quality of its products. They also tend to have a broader scope and penetrate more sectors of the economy.¹

The Occupational Safety and Health Administration (OSHA) and the Food and Drug Administration (FDA) seek to protect the individual directly by regulating the immediate workplace and substances ingested into the body. The Environmental Protection Agency (EPA) takes a broad approach to the environment and attempts to modify those elements of land, sea, and air that affect the well-being of persons and physical resources. This chapter presents the structure and functioning of these agencies, as well as critiques of their efficiency and effectiveness.

OCCUPATIONAL SAFETY AND HEALTH ADMINISTRATION

Early History and Legislative Authority

The motivation for a federal agency to regulate the safety of the workplace partially stemmed from the persistence of problems that did not significantly decrease under regulation by the states. In 1970, Congress was faced with 14,000 worker deaths, nearly 2.5 million disabled workers, and an estimated 300,000 new cases of occupational disease.²

In 1970, Congress passed the Occupational Safety and Health Act, which both created OSHA as a division of the Labor Department and described its purpose, applicability, organization, procedures, and standards.³
The act directs OSHA to encourage companies to improve and implement safety and health programs, provide relevant research, establish responsibilities and rights of employers and employees, maintain reporting and record-keeping systems, establish training programs, develop and enforce mandatory health and safety standards, and aid in the development, approval, and evaluation of state occupational safety and health programs. The act extends to the employers and their employees of the United States, but exempts the self-employed, state and local government employees, family farms, workplaces especially exempted due to regulation by other authorities, and since 1979, most businesses with fewer than 10 employees.

Organization and Functions

OSHA is organized into a series of offices under an assistant secretary of labor, who is responsible for direct supervision and control of them all. Departments handle matters such as internal equal opportunity employment, field coordination and experimental programs, public information, policy legislation and interagency programs, training, health standards, safety standards, and technical and administrative support.

Among the agency's most important functions are standards development and standards enforcement. The mechanics of standards development follows the rules of the Administrative Procedure Act, which provides for the publication of proposals in the Federal Register and allows for hearings. The National Institute for Occupational Safety and Health, an executive branch agency that is separate from both OSHA and the Labor Department, plays an important role in recommending regulations and summarizing the literature. Advisory committees are usually brought into play before proposals are published and are composed of representatives of management and labor, as well as the public. Executive orders of Presidents Ford and Carter require that OSHA make statements concerning the environmental and economic impact of its proposed rulings. Any individual or group may present oral or written testimony at public hearings. After the hearings, posthearing comments are accepted, and the final regulation is published in the Federal Register, along with its rationale.

Enforcement of standards is the second crucial function of the agency. The system is based upon OSHA inspections and investigations, which require a warrant should the employer refuse admittance, according to a 1978 Supreme Court ruling. The inspections are almost always unannounced and are based upon a system of priorities. First priority goes to situations of imminent danger, conditions or practices where there is
certainty of danger that would cause death or serious injury. Second priority is given to investigations of fatal accidents and catastrophes that result in the hospitalization of at least five employees. These situations must be reported to OSHA by the employer. Third are employee complaints of alleged violations. Next are the programmed high-hazard inspections, which are aimed at specific industries; and finally are the random inspections, which function as a form of quality control. Due to their health and safety record, five industries are given particular priority: meat and meat products, lumber and wood products, longshoring, roofing and sheet metal, and transportation equipment. In addition, work environments involving carbon monoxide, silica, lead, asbestos, and cotton dust are also given attention.

The employer has the right to accompany an inspector during the tour, as does an employee representative. The inspector explains the nature and the extent of the tour, examines the appropriate health and safety records required of the company, and gives employees the opportunity to meet with him privately to report violations. Employees are protected by law against employer discrimination based upon this participation.4

The outstanding characteristics of penalties levied for violations are the absence of a trial process as well as the imposition of fines upon the discovery of first violations. An area director evaluates inspector reports and determines the citations at the worksite (subject to the director's review and assignment of penalties). Penalties are categorized according to the seriousness of the violations and may rise to $10,000 for each violation. Employers may contest these rulings and bring their case to the Occupational Safety and Health Review Commission, which is independent of OSHA and staffed by administrative law judges. Further appeals go to the U.S. Circuit Court of Appeals.

The success of the inspection process is dependent upon the quality of the inspectors. A recent study found inspectors to be reasonably well trained and resistant to corruption.5 Assistant secretary of labor for OSHA, Thorne G. Auchter, testified to Congress about some changes made in 1982. An internal study of follow-up inspections determined that almost all violations had been rectified. Based on this information, follow-up inspections were reduced to compose less than one-fifth rather than more than one-fourth of all OSHA inspections. Another change involved the increased reliance upon informal conference between employers and area OSHA directors intended to clarify the basis of agency decisions. The policy resulted in a reduction in case contestations from one-fourth of all cases in 1980 to one-twelfth in 1981. Another innovation in inspections is the use of preliminary surveys to determine whether more thoroughgoing surveillance is needed; such a method allows for a more efficient allocation of resources.6
The effect of all these changes, however, is not entirely clear. Should the number of inspections be reduced too greatly, compliance may deteriorate. The reduction of contestations likewise entails some problems. The process whereby, to use Thorne Auchter's words, the parties "arrive at settlement agreements under which the employer agrees to comply," has an element of plea bargaining. While plea bargaining facilitates the adjudication process, it is possible that fines will be too greatly reduced so that an employer will be less vigilant in attempting to avoid violations in the first place.

Another area of OSHA functioning involves monitoring state plans. The enabling legislation provided for OSHA to encourage the development of these plans, which must be at least as effective as OSHA, and 23 had come into existence by mid-1982. After approval of the state program, OSHA pays up to 50 percent of the operation costs and retains discretionary enforcement authority for at least three years, during which time OSHA may revoke it for inadequate effectiveness. The initial intention was a gradual relinquishment to state authority, but this has not occurred due to court rulings requiring federal enforcement of minimum levels of protection.

The complete decentralization of occupational health and safety would be unwise, since then it would become next to impossible to enforce uniform standards. The shared federal and state approach holds the advantages of centralized standards, data, and research, along with the input of state funding and the more immediate government of localized control. Effective coexistence requires a continual federal monitoring to reduce redundancy of efforts.

Costs and Benefits

Recent controversies involving OSHA are an indication of its controversial position. In 1980, Senators Richard Schweiker and Harrison A. Williams cosponsored a bill, which failed to gain support, that would have further reduced OSHA powers. It would have targeted for OSHA annual inspections only those firms with poor safety records and effectively exempted 90 percent of the nation's small businesses and 85 percent of all businesses from surveillance. The bill likewise called for reduced penalties.

Another area of extreme controversy is OSHA's cancer policy. The agency divided materials associated with cancer into two categories: those that represent a clear and present danger; and those that show a suggestion of cancer-causing properties. The policy required the lowest possible levels of substances in the first category once the significance of the risk is
determined, but business opposition remained intense and forced the agency to ease somewhat the stringency of its standards.

Recent decisions of the Supreme Court have both supported and dampened OSHA activities. In 1980, the court ruled that benzene exposure requirements were invalid because of insufficient evidence supporting its dangerous properties. While in 1978 the court had required search warrants of OSHA inspectors denied admission to a plant, in 1980 it ruled that workers may refuse to perform tasks that are clearly unsafe without fear of employer recrimination.

Reagan's appointment of Thorne Auchter indicates a decision to limit the activities of the agency. Auchter, known for his dissatisfaction with programs that overregulate business, felt the 928 standards eliminated by OSHA during the Carter administration to be insufficient. Auchter continually searched for ways to reduce compliance costs, while at the same time acknowledging that a complete dismantling of the agency was not in order.

Economic realities forced the application of cost-benefit reasoning to the issue of worker safety. Auchter delineated a procedure of decision making that he felt could integrate economic realities with safety issues. He conceived of four steps. First is the determination of a significant risk, demonstrated and tangible. Second, an OSHA standard must be shown actually to reduce the demonstrated risk. Third, it is up to the agency to show that the standard is economically and technically feasible for the entire industry to which it applies; and fourth, economic as well as social consequences of the rule must be taken into account. As a result of these more stringent requirements for standard making, OSHA modified some of its requirements. For example, it simplified worker electrical safety standards, gave businesses more flexibility in achieving hearing conservation standards, and modified requirements for hazardous materials labeling in the workplace so that estimated initial compliance costs are $581.75 million as opposed to the $2.6 billion estimated cost of the Carter administration proposal.

Reagan policies have affected the agency's budget and staffing. In 1982, the budget was sufficiently reduced so that 250 jobs had to be eliminated, 150 from the field and 100 from headquarters. Plans were made in 1982 to disconnect federal enforcement efforts from the state plans, once legislation in Congress is prepared to allow for the separation. In April, OSHA carried out a consolidation of field units, closing 9 district offices and 20 field stations, as well as downgrading 6 area offices to district office status. In addition, in 1982 OSHA considered a major reduction in safety records in order to reduce compliance costs. Companies would have to keep records only on cases of significant exposure to hazardous substances.
and would be able to dispose of medical records at the termination of an individual's employment.9

It is impossible to come to an objective conclusion concerning the relationship of costs to benefits in the area of worker health and safety. For one, the ethical question of the value of an individual's life or health is in itself subjective. Society can only make decisions based on the "reasonableness" of costs. If the prevention of a case of lung cancer in one worker, for example, costs society $20 million, it could be rationalized that funds become diverted from other lifesaving activities, such as medical care and other social services. But there is no single cutoff, no absolute number or cost level that falls strictly between acceptable and unacceptable expense. Therefore, a type of social triage comes into play whereby society leaves some to the hazards in order to protect a greater number in another area based upon broad conceptions of policy and shared responsibility within the Congress, the workplace, the federal executive branch, and state and local governments.

The nature of social and productivity statistics belies attempts to draw cause and effect analyses. For example, Tables 10.1 and 10.2 present figures on price and productivity. It is clear that the period 1973-1975 represents a severe recession characterized by increases in prices and decreases in output. But how much of the problem is directly attributable to the compliance costs of health and safety regulations? It is clear that in some industries the percentage of capital spending marked for employee safety and health actually peaked before 1973. Costs for mining are estimated at 3.5 percent of capital spending for 1972 and 3.1 percent for 1973. In retailing and other commercial businesses, the level is 3.5 percent for 1972 and 2.4 percent for both 1973 and 1975. Airline expenses were reduced from 2.2 percent in 1972 to 1.5 percent in 1975, and iron and steel decreased from 12.3 percent in 1972 to 1.9 percent in 1975.10

OSHA has yielded real results, though not all entirely positive. Reported injuries and accidents were significantly reduced from 1970 to 1976. They declined from 17 per 100 employees in 1971 to 13.5 in 1976.11 Yet, the rate of accidents and health problems has not improved since 1976.

However, most critics believe that complete reliance on state regulation would be unwise. When the responsibility remained with the states, between 1960 and 1970, the accident rate in manufacturing rose 26.7 percent.12 Studies indicate that worker carelessness accounted for only one-third of all these industrial accidents, whereas unsafe working conditions contributed to 60 percent of them. It is also difficult to assess the situation during this time because of the lack of comparability of state data due to differences in eligibility for workers' compensation, varying quality of statistics, and differences in coding systems.13
### Table 10.1

**Price and Productivity Changes in Industries Subject to Health and Safety Regulation**

<table>
<thead>
<tr>
<th>Industry</th>
<th>Price Changes</th>
<th>Production Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Automobiles</td>
<td>0.9</td>
<td>14.2</td>
</tr>
<tr>
<td>Mining</td>
<td>9.3</td>
<td>8.7</td>
</tr>
<tr>
<td>Construction</td>
<td>10.2</td>
<td>7.4</td>
</tr>
<tr>
<td>Paper</td>
<td>1.8</td>
<td>10.6</td>
</tr>
<tr>
<td>Chemicals</td>
<td>1.2</td>
<td>9.0</td>
</tr>
<tr>
<td>Stone, clay, and glass</td>
<td>4.4</td>
<td>8.3</td>
</tr>
<tr>
<td>Primary metals</td>
<td>4.5</td>
<td>13.8</td>
</tr>
<tr>
<td>Other manufacturing</td>
<td>2.8</td>
<td>7.9</td>
</tr>
</tbody>
</table>

**Note:** Figures are average annual rate of change in percent.  

### Table 10.2

**Comparative Performance During Inflationary Periods of Industries Subject to Health and Safety Regulation**

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Automobiles</td>
<td>7.6</td>
<td>8.4</td>
<td>-0.3</td>
<td>4.8</td>
<td>6.4</td>
<td>-14.1</td>
</tr>
<tr>
<td>Mining</td>
<td>16.3</td>
<td>6.4</td>
<td>3.8</td>
<td>8.5</td>
<td>13.3</td>
<td>-6.9</td>
</tr>
<tr>
<td>Construction</td>
<td>9.2</td>
<td>15.7</td>
<td>6.4</td>
<td>11.4</td>
<td>10.6</td>
<td>-7.4</td>
</tr>
<tr>
<td>Paper</td>
<td>14.9</td>
<td>-8.7</td>
<td>17.8</td>
<td>6.9</td>
<td>21.0</td>
<td>-13.1</td>
</tr>
<tr>
<td>Chemicals</td>
<td>-3.7</td>
<td>26.4</td>
<td>12.6</td>
<td>6.8</td>
<td>15.5</td>
<td>-6.5</td>
</tr>
<tr>
<td>Stone, clay, and glass</td>
<td>8.3</td>
<td>7.9</td>
<td>5.9</td>
<td>7.5</td>
<td>10.8</td>
<td>-10.7</td>
</tr>
<tr>
<td>Primary metals</td>
<td>11.7</td>
<td>1.9</td>
<td>6.3</td>
<td>20.6</td>
<td>20.5</td>
<td>-10.0</td>
</tr>
<tr>
<td>Other manufacturing</td>
<td>6.9</td>
<td>4.7</td>
<td>12.5</td>
<td>5.4</td>
<td>10.8</td>
<td>-5.7</td>
</tr>
</tbody>
</table>

**Note:** Figures are average annual rates of change in percent.  
But improvements in the operation of OSHA are clearly in order. Michael Levin, an OSHA attorney, summarized the areas that may significantly be improved: greater efficiency of inspection returns; reduction of the adversarial nature of standard setting and enforcement by working closer with management; creation of incentives for change such as tax credits for companies with good health and safety records; and required notification of such records to investors and stockbrokers. Increased flexibility in obtaining safer conditions facilitates the process. For example, headgear could be both more effective and efficient for the protection of worker hearing than the costly redesign of machinery. Congress could both monitor and evaluate worker health and safety statistics in its appropriations and reform of OSHA functioning. Incremental rather than sudden, major change is likewise indicated, with each adjustment matched by a corresponding evaluation of results, in order to effect optimal protection without sacrificing health and safety under the pressure of difficult economic conditions.

Evaluations of reform proposals that seek to find alternatives to agency regulation indicate that they would not likely be effective. Relying on increased employer liability approaches the problem after the fact, after the injury or health problem has occurred, and assumes that each worker would have the time and the resources to seek remedies in the courts. Relying upon increased information for the workers assumes a high level of vigilance on the job, when concerns other than safety usually fill the individual's mind.

It is possible that the decrease in OSHA effectiveness since 1979 compared with the period 1971-1975 relates to a safety “threshold.” Initial reductions in worker accidents and sickness may reflect environmental improvements, but reductions beyond that level could involve the impact of the individual, such as the area of industrial psychology, or even other factors more difficult to control. In addition, the elimination of regulations under Carter and then Reagan could also be responsible for the leveling off of results. It should not be assumed that the gains effected by an activist OSHA would remain in a deregulated context.

FOOD AND DRUG ADMINISTRATION

Early History and Legislative Authority

Since King John of England issued laws concerning the proper content of bread in thirteenth-century England, the regulation of food and drugs has been a concern of government. By the 1640s, the government of Massachusetts was regularly inspecting food imports, and in 1668 it passed
a food additive law, which banned a particular type of salt. During the 1770s, states such as Massachusetts and New York passed laws concerning the ingredients of foods. In 1848, the first federal drug law was passed, which concerned the misbranding of drugs.\textsuperscript{16}

The beginning of modern regulation is marked by the appointment of Harvey W. Wiley to the Bureau of Chemistry within the Department of Agriculture. As a result of his lobbying, Congress passed laws regulating the inspection of animals intended for human consumption. The 1906 publication of Upton Sinclair's \textit{The Jungle}, which graphically exposed the sanitary conditions of the meat-packing industry, made the subject of food quality a national issue. The momentum was furthered by a series of articles in the \textit{Ladies Home Journal} and \textit{Collier}'s describing abuses in the manufacture and sale of medicines. In 1903, Wiley had initiated a "poison squad" composed of men who agreed to eat foods treated with additives to determine whether they were dangerous.

The federal government responded with the passage of the Pure Food and Drug Act of 1906, which prohibited interstate commerce in adulterated or misbranded food and drugs and called for a Food and Drug Administration to administer and enforce the act.\textsuperscript{17} Adulteration was defined as the hiding of inferiority by means of artificial color or coating or the addition of harmful ingredients or decomposed or diseased organic substances. Misbranding involved false or misleading labeling. Violations were made criminal offenses carrying fines of up to $200 for a first offense and $300 or one year's imprisonment for subsequent violations.

The inadequacies of the 1906 law became evident over the following 30 years. False claims for patent medicines escaped regulation when Congress passed an amendment in 1912 outlawing such claims but requiring proof that the promoter intended to commit fraud. The courts could not find justification in the law for FDA standards on purity and content.

Yet another wave of consumer sensitivity to the issue came forward in the 1930s, and the book \textit{Your Money's Worth} by Stuart Chase and F. J. Schlink, became the Depression's version of \textit{The Jungle}. But attempts by Assistant Secretary of Agriculture Rexford Tugwell (with the full support of Franklin Roosevelt) to gain support for a new bill in Congress gained little headway in face of industry opposition, already bridling from difficult economic conditions. Only the death of more than 100 people as a result of the "elixir of sulfanilamide" motivated Congress to act, which resulted in the passage of the Federal Food, Drug, and Cosmetic Act of 1938.\textsuperscript{18} The new act regulated cosmetics and therapeutic devices for the first time. Proof of fraud was no longer required to stop false claims for drugs, and drug manufacturers were required to submit proof of the safety of new products before putting them on the market. Regulation increased for the use of poisonous substances and levels authorized for residues of
some of these substances, such as pesticides. Regulation of food labeling (for both substitutions and content) and food containers became more stringent. In addition to product seizures and criminal prosecutions (the penalties of which were increased), federal court injunctions could be brought against violators. Another area of enforcement became the inspections of factories, also authorized by the act.

The 1938 law did not prove detrimental to the pharmaceutical industry, which prospered during the 1940s and introduced many new drugs. However, the very technological advancement that made the food and drug industry more complex also created the need for additional legislation. Although a law required the market pretesting of drugs, consumers still served as guinea pigs for drug introductions, the long-term effects of which were unknown. The research needed to determine the safety of the increased selection of foods and drugs greatly surpassed the resources of the Food and Drug Administration. Three amendments followed as a result: the Pesticide Amendment of 1954, the Food Additives Amendment of 1958, and the Color Additive Amendments of 1960. These amendments extended the scope of regulation so that no type of substance could be introduced without a prior determination of its safety. The 1958 amendment, known more generally as the Delaney Amendment, is important for its inclusion of the clause, "No additive shall be deemed to be safe if it is found to induce cancer when ingested by man or animal, or, if it is found, after tests which are appropriate for the evaluation of the safety of food additives, to induce cancer in man or animal." The clause created difficulties since it did not specify dose levels, and subsequent research determined that many relatively harmless substances may be carcinogenic if forced into animals in sufficient quantities.

Another important addition to food and drug laws appeared with the passage of the Federal Food, Drug, and Cosmetics Act Amendments of 1962. This amendment, following closely the deformation and death of infants of mothers taking the drug thalidomide in Europe, sought to tighten control of new drugs of dubious value and possible danger. These amendments required manufacturers of food and drugs to prove the effectiveness as well as the safety of their products before marketing them. Patenting laws had allowed companies to market drugs that were essentially minor modifications of existing remedies and make extravagant claims in their promotions. The expense of the packaging, management, and advertising of the new products was passed on to an uninformed consumer and therefore did not represent the true value of the products. Manufacturers now had to prove their claims to the FDA and receive its approval prior to marketing. In addition, the FDA could take a product off the market if evidence indicated ineffectiveness. Other important food and drug laws include a Federal Hazardous Substances
Protection: OSHA, FDA, and EPA

Labeling Act (1960), requiring warning labels on hazardous household chemical products, a Fair Packaging and Labeling Act (1966), requiring uniformity and accuracy in labels on food, drugs, cosmetics, and medical devices, and the Radiation Control for Health and Safety Act (1968), which set radiation performance standards on televisions, microwave ovens, X-ray machines, and other products that produce and emit radiation.

In addition, a Drug Listing Act (1972) required the registration of producers of drugs and medical devices with the FDA and the filing of lists of drugs and devices, the Medical Device Amendments (1976) authorized the FDA to ban risky medical devices and set performance standards for those it allows, and the Infant Formula Act (1980) set standards for the production and content of infant formulas.

Organization and Functions

The FDA is headed by a commissioner, who is actually the administrator of the agency. The commissioner is responsible for all final FDA actions taken against the food and drug industry. Because the FDA is a part of the Department of Health and Human Services, the commissioner is subject to review and revision by the secretary of that department. An Office of Regulatory Affairs serves as the coordinator of compliance to FDA rules as well as the coordinator of the rule-making process. An Office of Health Affairs develops guidelines for research, training, and evaluation. Other departments handle policy coordination, management and operations, planning and evaluation, legislative affairs, and consumer affairs. A Bureau of Drugs handles the promulgation of standards and regulations for drugs as well as applications for the marketing of new drugs and testing programs. Bureaus of Medical Devices, Veterinary Medicine, Radiological Health, and Biologies (i.e., serums and vaccines) perform similar functions in their respective areas.

The FDA increased its budget from 1970 to 1980 by five times, as well as nearly doubling its staff during that same time period. By far the greatest single expenditure is in the food area, with drugs remaining as the second priority, food accounting for 27 percent and drugs 22 percent of total FDA funds in 1980. Program management accounted for 14 percent of the budget, and medical devices 11 percent (see Tables 10.3 and 10.4).

Enforcement, as with all regulatory agencies, is an essential function. For this purpose, the FDA employs inspectors and chemists, who work out of regional offices and who may inspect manufacturing centers for food, drugs, cosmetics, medical equipment and substances, and radiation-emitting devices. They may also examine company records. When
Table 10.3

FDA Budgets and Staffing for Fiscal Years 1970–1980

<table>
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<tr>
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<th></th>
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<tbody>
<tr>
<td>Budget ($ millions)</td>
<td>68</td>
<td>85</td>
<td>105</td>
<td>143</td>
<td>165</td>
<td>201</td>
<td>218</td>
<td>245</td>
<td>276</td>
<td>300</td>
<td>326</td>
</tr>
<tr>
<td>Staffing</td>
<td>4,152</td>
<td>4,360</td>
<td>5,431</td>
<td>6,751</td>
<td>6,116</td>
<td>6,206</td>
<td>6,362</td>
<td>7,340</td>
<td>7,483</td>
<td>7,656</td>
<td>7,419</td>
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Note: Budget figures are for antitrust enforcement and include grants to states for enforcement.

Table 10.4

Allocations of FDA Funds for Fiscal Years 1978–1980

<table>
<thead>
<tr>
<th>Program</th>
<th>1978</th>
<th>1979</th>
<th>1980</th>
</tr>
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<tbody>
<tr>
<td>Food Safety</td>
<td>$ 81,625</td>
<td>28</td>
<td>$ 84,699</td>
</tr>
<tr>
<td>Food Economics</td>
<td>3,114</td>
<td>1</td>
<td>1,822</td>
</tr>
<tr>
<td>Cosmetics</td>
<td>2,979</td>
<td>1</td>
<td>2,044</td>
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<tr>
<td>Human Drugs</td>
<td>65,321</td>
<td>23</td>
<td>68,863</td>
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<tr>
<td>Animal Drugs and Feeds</td>
<td>17,158</td>
<td>6</td>
<td>18,264</td>
</tr>
<tr>
<td>Medical Devices</td>
<td>25,883</td>
<td>9</td>
<td>32,144</td>
</tr>
<tr>
<td>Biologics</td>
<td>19,923</td>
<td>7</td>
<td>20,867</td>
</tr>
<tr>
<td>Radiological Health</td>
<td>20,262</td>
<td>7</td>
<td>21,028</td>
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<tr>
<td>NCTR</td>
<td>13,866</td>
<td>5</td>
<td>14,175</td>
</tr>
<tr>
<td>Program Management</td>
<td>37,120</td>
<td>13</td>
<td>39,893</td>
</tr>
<tr>
<td>Total</td>
<td>$287,251</td>
<td>100</td>
<td>$333,799</td>
</tr>
</tbody>
</table>

Note: The 1980 figures are estimates.

violations of agency rules and standards are discovered, the agency has six basic recourses: (1) recalls, whereby products and substances are called back from the marketplace; (2) regulatory letters to management stating that legal action will be taken if a violation is not corrected; (3) injunctions, whereby civil actions are taken against individuals or companies; (4) citations, leading to hearings in which decisions concerning future actions are taken; (5) seizures, the apprehension of goods as directed by the courts and carried out by a U.S. marshal; and (6) prosecutions, criminal actions taken against individuals or companies charged with violating laws administered by the agency.

The Food and Drug Industry and Consumer Protection

The question remains whether the FDA is doing its job. The balance in the regulation of food and drugs lies between the underregulated danger of unsafe products and the overregulated prevention of the delivery of adequate food and innovative and effective drugs.

In the area of drugs, William Wardell, director of the University of Rochester's Center for the Study of Drug Development, presents the argument that the FDA has overregulated. Wardell points to a "drug lag" that emerged during the early 1960s and continued into the 1980s. When the United States is compared with Great Britain in nine therapeutic areas, Britain made three to four times as many new drugs available from January 1962 through March 1979. Of those drugs eventually introduced by both countries, twice as many were introduced earlier by Britain. A similar pattern holds for much of Western Europe as well.

A second part of the drug lag is the area of drug applications, those conditions for which a drug may be prescribed. U.S. policy is much more restrictive, so that a physician has a smaller range of options in the treatment of disease.

Wardell points to some specific areas. In the field of cardiovascular drugs, no new antihypertensive substances were approved between 1963 and 1973, even though heart attack and stroke remained the leading cause of death. Only two antiarrhythmic drugs were approved between 1962 and 1975. The FDA prevented a research project by E. R. Squibb and Sons to determine whether aspirin in normal doses is useful in the prevention of heart attacks, yet five years later the National Institute of Health carried out essentially the same investigation using public funding. In the area of respiratory drugs, four important medications available in Europe were denied asthma sufferers, and the same holds true for central nervous system drugs and gastrointestinal medications. Another study found that the average annual rate of new chemical entities (new compounds not
previously marketed) proceeded at 17 from 1962 to 1975, but reached 56 for the period 1950-1961.25

Others have pointed to the economic impact of overregulation. The period of drug development escalated from an average of two years between 1958 and 1962, four years between 1963 and 1967, and five and a half to eight years between 1968 and 1972. The average time for regulatory approval increased from 6 months in 1962 to 40 months in 1969, expanding the cost of ultimate production geometrically. The average time required for filing a new drug application rose from six years in 1974 to nine years in 1976. One study indicates the cost of introducing a new chemical entity to the point of marketing approval between 1963 and 1975 averaged $93 million in 1982 dollars.26 The effect upon management decisions resulted in a general shift of dollars away from research and development, a reduction in the variety of similar but not identical drugs, which aid the physician in avoiding allergic reactions, an increased emphasis on the important diseases to the detriment of attention to more peripheral diseases, and an increased emphasis on short-term-usage drugs, which involve fewer safety risks and liabilities for the manufacturer.27

Claims for the loss to consumers are sometimes dramatic. One authority believes that the drug alprenolol, useful in preventing heart attacks and coronary death, and available in Sweden since 1976 but not available in the United States, could prevent as many as 10,000 deaths a year in this country.28

The FDA counters these criticisms with a series of arguments. It holds that the reasons for the drug decline are embodied in both the nature of research and issues of safety. It cites a "knowledge plateau" in the field of pharmaceuticals, indicating that scientific progress is never upwardly linear, that breakthroughs come in intensive periods of activity. The 1970s simply represent a time when scientific efforts were regrouping and preparing for future breakthroughs. The FDA claims that although in a few specific areas Europe has more new introductions, in general the decline of introductions is worldwide. The FDA also argues that the safety standards of the United States are higher than in other countries, such as the European democracies, where there might be a somewhat greater rate of drug innovation. It cites higher death rates in specific diseases, such as asthma, where there are more drugs available for treatment.29

The FDA sees its drug approval process as embodying the highest standards of scientific practice and minimizing external influences such as political and economic pressure. While the agency had difficulty attracting top-notch scientific personnel because most scientists prefer to engage in rather than evaluate research, and because industry pay scales remained higher than that of the government, the FDA initiated the use of an advisory system to overcome such difficulties. Advisory committees
composed of leading scientists provide sophisticated input to the agency, so that it may match its safety efforts with the most advanced expertise.\textsuperscript{30}

Given the fact that the agency has regular contact with representatives of industry continually lobbying for more liberal drug approval policies, but relatively fewer contacts with consumer spokesmen, the FDA believes that it has been able regardless to retain its objectivity and emphasis upon safety. The FDA also counters arguments concerning its overregulation by citing the efforts of Congress, which often sees FDA regulatory policies as lax, especially according to various oversight efforts conducted by Senators Edward Kennedy, Estes Kefauver, and Gaylord Nelson and Representatives Lawrence Fountain and Paul Rogers.\textsuperscript{31} The FDA also sees active federal regulation as necessary because of inconsistent and varying levels of standards in the regulatory efforts of the individual states, which must be superseded by an overall protection agency.\textsuperscript{32}

The FDA considers its safety standards to be high partly because of formal drug approval procedures. In 1963, the agency initiated a process that first requires the submission of a new drug application that includes all data on preclinical testing on animals, data on pharmacology and toxicity, as well as plans for clinical testing. If the FDA gives a go-ahead, periodic reports during the testing phase must be made. In phase 1, a small amount of the drug is tested on healthy subjects; in phase 2, controlled studies are made involving a small group of patients for treating a specific disease; and in phase 3 a substantial number of patients are treated in a clinical setting. If the results are favorable, the drug sponsor submits a new drug application. A detailed classification for the effectiveness of drugs became instituted in 1966. Institutional review boards became established in the early 1970s to monitor carefully all testing research. In 1975, the FDA called for postmarketing studies in order to continue drug effectiveness surveillance more thoroughly. In addition, new drug applications now involve strict regulation as to what may be claimed about a drug. Another indication of the agency’s safety orientation is its consideration of evidence. It requires at least two controlled trials in the United States, regardless of data collected abroad.

Recent efforts of the FDA involve stricter labeling requirements, and the agency is considering the required listing on prescription drugs of possible side effects. It is also making the public more aware of the implications of food, such as the effects of caffeine on pregnancy and the effects of sugar consumption.\textsuperscript{33} The agency counteracts the criticism that it is completely unconcerned with economic issues by its involvement with the maximum allowable cost program placing ceilings on Medicaid drug costs and by its interest in encouraging smaller companies to manufacture less expensive generic versions of brand-name drugs.
The central criticism of the FDA remains that it does not apply a more practical version of risk and benefit analysis. For example, the proposal to ban saccharin met with public opposition, which prompted Congress to enact a moratorium preventing the FDA from taking it off the market for at least 18 months. After vacillating, the FDA finally allowed saccharine to remain on the market. The problem related to the application of the 1958 Delaney Amendment, which holds that foods are not safe if they can induce cancer in man or animals, regardless of the quantities or incidence.

The sweeping requirement of the Delaney Amendment ignores the analysis of risk. For one, it assumes that what is harmful in animals will also be harmful in humans. It does not take into account that what may be harmful in massive doses may be harmless in small doses, and it ignores individual variation of response. This example illustrates that it would be far more practical for the agency to consider the levels of risk rather than the mere existence of a problem under extraordinary circumstances.

Others point to the fact that, while recent FDA actions regulating infant formulas, products involved with toxic shock syndrome, and increased research into the possible harmful effects of caffeine in pregnancy are justified, the banning of certain tranquilizers without any known harmful effects, is unwise.

It is clear that some reorientation of policy is in order for the FDA. The agency has an impressive safety record, but it is possible for it to rearrange its priorities. The evidence is strong that a less conservative posture in reference to drugs for treatment of life-threatening illnesses such as heart disorder and cancer makes sense in a risk and benefit framework. All drugs have side effects; their administration always involves a judgment in terms of risks and benefits. The physician decides whether the negative side effects are less important than the positive results of ameliorating the disease. In cases of serious illness, when the possibility of death exists, a drug that could have a serious side effect but is short of lethal may be in order and could allow the physician greater effectiveness.

In areas where the benefits outweigh the risks, the FDA could selectively make more options available to consumers, at the same time increasing product liability of manufacturers and improving the information available to the public about both benefits and risks.

ENVIRONMENTAL PROTECTION AGENCY

In recent years, the public has become sensitized to the ways in which problems in the environment may affect the health and well-being of individuals. In many respects, the problem of environmental control is even more complex than the more direct protection of individuals in such
areas as worker safety and food and drugs. This is true because the problems have their origins not only in individuals, but also in companies and natural processes.

**Early History and Legislative Authority**

A major social awareness concern of the 1960s was the impact of American industry upon the environment. By 1969, federal control had proved itself to be unfocused and ineffective, water quality regulation becoming the responsibility of the Department of the Interior while responsibility for air pollution remained with the Department of Health, Education, and Welfare. The approach relied heavily upon state action, with the federal government supplying grants to those states with established pollution standards. The Federal Air Quality Act of 1967 went somewhat further in that the states were given the opportunity to develop air quality standards and enforcement mechanisms based on federal criteria, but the federal government would take over those functions in the event of state failure. However, no deadlines were specified, so that the federal government was placed in the passive position of waiting for state action. As of 1970, over two years after the law was passed, the states had presented none of the mandated criteria documents specifying unacceptable levels of pollutants, and no state had adopted a full set of standards or implementation plans.

In the meantime, public interest in the problem had intensified. A Ralph Nader organization, the Center for the Study of Responsive Law, criticized the vagueness of the environmental legislation. Books such as John Esposito's *Vanishing Air* (1970) and David Zwick and Marcy Benstock's *Water Wasteland* (1971) graphically demonstrated the extent of pollution and the inadequacy of existing remedies. A major "Earthday" demonstration in April 1970 provided a dramatic forum for public expression as well as serving as a means for capturing the attention of the government.

Senator Edmund Muskie, whose subcommittee was responsible for the 1967 act, came forth in favor of strict statutes with specific goals and timetables as the most practical means of effecting real results. The first of the new antipollution laws was the National Environmental Policy Act of 1969, which established a Council on Environmental Quality with the purpose of establishing a national policy on the environment, but it was not until 1970 that substantive statutes came forth.

Concern with the environment coincided with a considerable impetus for the consolidation of presidential power. President Nixon had instituted an Advisory Council on Executive Organization under former Litton Industries executive Roy Ash, along with an Environmental Protection Group in the White House. Ash called for a Department of Natural
Resources, which would maximize presidential power by consolidating various departments and by reducing the number of officials reporting directly to the president. This department would be one of four super-departments, reducing the size of the Cabinet and therefore allowing for a narrower point of view, more reflective of the president's policies. But the Environmental Protection Group argued that such a department would not be able to combine all the existing government programs into a consolidated unit and that it would be a type of holding company, large, diverse, and not sufficiently connected to its range of operations. The Environmental Protection Group argued that a separate agency could have an explicit pollution control mission so that the control of pollution and the promotion of economic development would be separated. Such an organization could also deal with wastes, regardless of their form or origin, in the air, water, or land.

Within Nixon's Cabinet, opposition to the Department of Natural Resources was strong, but neither was there much support for an Environmental Protection Agency (EPA). However, a coalition began to develop within the administration among groups such as the Council on Environmental Quality, the Department of Health, Education, and Welfare, and the Environmental Protection Group. A compromise emerged that satisfied Nixon's fears that an EPA would be too antibusiness. While the president supported the establishment of the EPA, he at the same time strengthened environmental programs of the probusiness Commerce Department and added to it a National Oceanographic and Atmospheric Administration. Nixon also provided for White House involvement by the establishment of liaison functions within the Domestic Council and the Council on Environmental Quality. The Environmental Protection Agency came into being by an executive order submitted to Congress July 9, 1970, by Richard Nixon as part of Reorganization Plan Number 3.

Shortly after approving the new agency, Congress passed some major environmental legislation embodying specific goals and agendas. The Clean Air Act of 1970 is considered one of the most important pieces of environmental legislation yet passed. The act is most notable for the ambition and stringency of its requirements. It created a comprehensive programmatic and regulatory scheme for controlling air pollution by the establishment of uniform federal ambient air quality standards of two types: primary standards directed to the protection of public health; and secondary standards intended to ensure the public welfare. Each state was required to meet the federal standards by the development of state implementation plans approved by the EPA by 1975. The act also required that by 1975 new cars be all but pollution-free, and emissions of hydrocarbons and carbon monoxide gases reduced to 90 percent below permissible levels in 1970. With respect to six pollutants—particulate
matter, sulfur dioxide, carbon monoxide, photochemical oxidants, nitrogen oxides, and hydrocarbons—the states had to establish and enforce programs meeting federal standards within a period of four to six years. Willful polluters became subject to fines of up to $50,000 a day and to jail sentences of up to two years. The act provided for class action suits, in that any individual or group could sue in the federal courts to prevent pollution practices. The act also authorized $1.1 billion to state agencies for a three-year period of air pollution research and established a Federal Office of Noise Abatement and Control.

The ambition embodied in the 1970 act became expressed in other environmental legislation during the first half of the 1970s. A Water

### Table 10.5
### Major Air Pollutants And Their Health Effects

<table>
<thead>
<tr>
<th>Pollutant</th>
<th>Major Sources</th>
<th>Characteristics And Effects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carbon monoxide (CO)</td>
<td>Vehicle exhausts.</td>
<td>Colorless, odorless, poisonous gas. Replaces oxygen in red blood cells, causing dizziness, unconsciousness, or death.</td>
</tr>
<tr>
<td>Hydrocarbons (HC)</td>
<td>Incomplete combustion of gasoline; evaporation of petroleum fuels, solvents, and paints.</td>
<td>Although some are poisonous, most are not. Reacts with NO₂ to form ozone, or smog.</td>
</tr>
<tr>
<td>Nitrogen dioxide (NO₂)</td>
<td>Industrial processes, vehicle exhausts.</td>
<td>Causes structural and chemical changes in the lungs. Lowers resistance to respiratory infections. Reacts in sunlight with hydrocarbons to produce smog. Contributes to acid rain.</td>
</tr>
<tr>
<td>Ozone (O₃)</td>
<td>Formed when HC and NO₂ react.</td>
<td>Principal constituent of smog. Irritates mucous membranes, causing coughing, choking, impaired lung function. Aggravates chronic asthma and bronchitis.</td>
</tr>
<tr>
<td>Total suspended particulates (TSP)</td>
<td>Industrial plants, heating boilers, auto engines, and dust.</td>
<td>Larger visible types (soot, smoke or dust) can clog the lung sacs. Smaller invisible particles can pass into the bloodstream. Often carry carcinogens and toxic metals; impair visibility.</td>
</tr>
</tbody>
</table>

Source: Environmental Protection Agency.
Quality Improvement Act of 1970 made oil companies partially liable for oil spills (to a limit of $14 million) and outlawed the flushing of raw sewage from boats. In addition, higher standards were created governing thermal pollution from nuclear power plants.\textsuperscript{41} The Water Pollution Control Act of 1972 required manufacturers to monitor discharges (the records are inspected by the EPA), extended federal water pollution control to all navigable waters, and provided for stiffer penalties for polluters.\textsuperscript{42} The same year, a Federal Environmental Pesticide Control Act required the registration of pesticides and gave the EPA power to ban pesticides it deems dangerous; a Marine Protection, Research and Sanctuaries Act outlawed ocean dumping without an EPA permit and zoning designation; and a Noise Control Act gave the EPA the power to set national noise standards for commercial products.\textsuperscript{43}

In 1974, the Safe Drinking Water Act set water purity standards in public drinking water systems.\textsuperscript{44} In 1976, the Resource Conservation and Recovery Act set standards for safety concerning the handling and storage of hazardous wastes and required permits; the EPA was authorized to make grants to states for hazardous waste treatment programs.\textsuperscript{45} The same year, the Toxic Substances Control Act authorized EPA to require testing of substances that present a risk to human health.\textsuperscript{46}

Unfortunately, as these acts became law, it began to appear that the original Clean Air Act was not realistic. The complexity of air pollution became manifest once the federal government was committed to its improvement. During the first six years of the act's application, much litigation proceeded concerning problems such as stationary and mobile
sources of pollution, the definition of hazard, and long-distance transmission and transformation of air pollutants. By 1975, almost 70 percent of the 247 air quality control regions did not meet primary health standards.

The Clean Air Act Amendments and the Clean Water Act of 1977 represent a compromise of standards that proved unrealistic. They are also a watershed, in that since 1977 only two major environmental protection measures became law, the Aviation Safety and Noise Abatement Act of 1979, assigning additional authority to the EPA for aviation noise control, and the Comprehensive Environmental Response, Compensation and Liability Act of 1980, establishing liability of up to $50 million for natural resource damage due to the release of hazardous substances.

The new pollution control amendments contain six basic provisions:

1. The 1970 healthy air goals set for 1975 becomes extended to 1982 and in some cases to 1987.
2. The EPA is given discretion to extend deadlines for control of auto emission pollution of carbon monoxide and nitrogen oxides (but not for hydrocarbons) for up to two years.
3. The EPA must file economic and employment impact statements for all new regulations and make adjustments in requirements for technological innovations.
4. Water pollution control deadlines are extended if industries acted in "good faith" but did not achieve the best practicable technology deadlines.
5. The best available technology (BAT) requirements intended to be achieved in water pollution are likewise extended. The concept of BAT is replaced by the best conventional pollution control technology (BCPCT), with goals set for 1984.
6. The goal of zero-discharge into navigable waters by 1985 is retained. But the technology requirements effectively make any possibility of nearing zero during the 1970s impossible.

The 1977 clean water amendments create three categories of pollutants: toxic, conventional, and nonconventional. The BCPCT requirements are mainly applied to conventional pollutants, which are biochemical, oxygen-demanding, and generally considered the least immediately harmful. Because the nonconventional category involves more unknowns, in general BAT is applied, although the EPA has some discretion in altering requirements. Finally, the toxic pollutant category retains original strict BAT requirements, with the tightest and least flexible deadlines.
The Uncertain Balance

Costs and Benefits of Environmental Protection

The specificity of the antipollution legislation of the past decade is, in part, a response to the critics of vague enabling legislation that marked the appearance of agencies such as the Federal Trade Commission. The legislation contained not only specific goals but timetables as well. The agency created to administer the laws is action-oriented, an independent office headed by an administrator assisted by a deputy and six assistant administrators nominated by the president and confirmed by the Senate. Various offices handle enforcement, regulations and standards, research, and specific areas of pollution. The agency engages in enforcement, and when violations are contested, administrative law judges conduct open hearings, the outcomes of which may be challenged in the U.S. district courts. Fines for violations of the Clean Air Act may range up to $25,000 a day, and breaches of the Safe Drinking Water Act may be penalized up to $5,000 a day. Other acts hold similar penalties.

The agency is geared for results. Extensive media coverage allowed for the EPA to gain credibility and publicize its mandate. Lawyers and research scientists gained dominance over the economists concerning goal formation, and the emphasis remained on reducing pollution rather than maximizing and protecting the returns of firms.

Critics of EPA point to the enormous compliance costs involved in cleaning up the environment. They argue that a 95 percent effluent reduction over 25 years would cost about $119 billion, and near-zero discharge levels would amount to a cost of nearly $200 billion over the same period. In 1976, it is estimated that families with incomes over $11,410 paid an average of $549 a year for pollution control. Some studies indicate that in the late 1970s, 20,000 employees lost their jobs because of antipollution costs and plant closings, and pollution control raised the rate of inflation from .3 percent to .5 percent.53 Others estimate that at 1979 compliance cost rates, by 1988, cumulative costs will balloon to $735 billion in 1979 dollars (see Table 10.7).

Others point out that costs may be even greater than they at first appear. Antipollution costs could delay the construction of new plants, and the operation of antipollution devices may take a total of from 5 percent to 10 percent of a plant’s total energy. Some processes, such as the wet-scrubbing of coal, use large quantities of water.53

The EPA countered its critics with a series of arguments. It stressed that estimates of compliance costs are not accurate and are often inflated. In the case of water effluent guidelines for petroleum refineries, industry and even the EPA overestimated the actual compliance costs by 140 percent.54

The agency likewise points to the costs involved in not regulating. Based on the situation in 1976, a governmental task force estimated the following
## Table 10.7
### Estimated Total Pollution Abatement Expenditures, 1979–1988
(Billions of 1979 Dollars)

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td></td>
<td>OPERATION AND MAINTENANCE</td>
<td>ANNUAL CAPITAL COSTS</td>
<td>TOTAL ANNUAL COSTS</td>
</tr>
<tr>
<td>Air pollution</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public</td>
<td>1.7</td>
<td>.4</td>
<td>2.1</td>
</tr>
<tr>
<td>Private</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mobile</td>
<td>3.2</td>
<td>4.9</td>
<td>8.1</td>
</tr>
<tr>
<td>Industrial</td>
<td>2.5</td>
<td>2.9</td>
<td>5.4</td>
</tr>
<tr>
<td>Electric utilities</td>
<td>6.3</td>
<td>3.5</td>
<td>9.8</td>
</tr>
<tr>
<td>Subtotal</td>
<td>13.7</td>
<td>11.7</td>
<td>25.4</td>
</tr>
<tr>
<td>Water pollution</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public</td>
<td>3.7</td>
<td>8.2</td>
<td>11.9</td>
</tr>
<tr>
<td>Private</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industrial</td>
<td>4.4</td>
<td>3.2</td>
<td>7.6</td>
</tr>
<tr>
<td>Electric utilities</td>
<td>.4</td>
<td>.5</td>
<td>.9</td>
</tr>
<tr>
<td>Subtotal</td>
<td>8.5</td>
<td>11.9</td>
<td>20.4</td>
</tr>
<tr>
<td>Solid waste</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public</td>
<td>1.7</td>
<td>.3</td>
<td>2.0</td>
</tr>
<tr>
<td>Private</td>
<td>4.5</td>
<td>.7</td>
<td>5.2</td>
</tr>
<tr>
<td>Subtotal</td>
<td>6.2</td>
<td>1.0</td>
<td>7.2</td>
</tr>
<tr>
<td>Toxic substances</td>
<td>.1</td>
<td>.2</td>
<td>.3</td>
</tr>
<tr>
<td>Drinking water</td>
<td>.3</td>
<td>.4</td>
<td>.7</td>
</tr>
<tr>
<td>Noise</td>
<td>&lt;.05</td>
<td>.1</td>
<td>.1</td>
</tr>
<tr>
<td>Pesticides</td>
<td>.1</td>
<td>&lt;.05</td>
<td>.1</td>
</tr>
<tr>
<td>Land reclamation</td>
<td>.4</td>
<td>1.3</td>
<td>1.7</td>
</tr>
<tr>
<td>Total</td>
<td>29.3</td>
<td>26.6</td>
<td>55.9</td>
</tr>
</tbody>
</table>

*Interest and depreciation.


Impacts of oxidants by 1980: 1.7-1.8 million cases of eye discomfort; 33,000-36,000 aggravated heart and lung diseases in the elderly; 510,000-570,000 cases of coughing; and 50,000-55,000 excess cases of chest discomfort. And such figures do not account for the possible long-term effects on the creation of cancer, or damage to property, materials, wildlife, and aesthetics.55

Another argument lies in the extreme danger involved with hazardous wastes. The Love Canal dump site is one of the more publicized incidents that holds immediate health danger. Although Hooker Chemical Corporation began to bury industrial wastes during the 1940s, it was not until 1978 that residents of the Love Canal area began to smell odors in
The Uncertain Balance

their basements. Subsequent tests indicated the presence of dioxin, an extremely dangerous chemical that can cause cancer, liver, and heart disease. An EPA study indicated that a high proportion of the Love Canal residents may have suffered chromosome damage. By mid-1980 the EPA found approximately 100 of more than 600 inspected sites to pose health threats.\textsuperscript{56} The costs of just correcting the conditions at Love Canal and relocating the residents, without the medical expenses involved in any contracted illnesses, is estimated at $23 million.\textsuperscript{57} The EPA is also involved in protecting the environment from nuclear wastes and played a prominent role during the Three Mile Island accident.\textsuperscript{58} With the procession of an ever-increasing number of new chemicals, there could be a growing gap between the number of carcinogenic chemicals identified and the number regulated.\textsuperscript{59}

The politics of the Reagan administration are oriented toward tempering environmental protection efforts. By 1979, the Justice Department and the General Accounting Office had indicated that EPA enforcement had not reached an adequate level. A GAO report indicated that between 1972 and 1978, 98 percent of 2,473 enforcement actions were administrative, in which violators agreed to compliance schedules, and that only 2 percent involved court action.\textsuperscript{60} Yet standards have been relaxed regardless. A “bubble” policy calls for air standards over areas of land rather than placing strict requirements on the emissions of each smokestack. Environmental Protection Agency Administrator Anne M. Gorsuch went into the fiscal 1983 budget negotiations with the Office of Management and Budget prepared to accept an 18 percent reduction in the agency’s budget.\textsuperscript{61} Questions of leniency in the enforcement of environmental standards, as well as deep personnel and budget cuts, would eventually lead to Congressional pressure and the resignation of Gorsuch.

Nonagency regulation of the environment holds similar problems to nonagency regulation of worker safety. One such proposal is a pollution tax, but such a tax would come into effect after the fact and would likely involve a reduced monitoring system. Given the difficulties within the Internal Revenue Service with collecting more conventional forms of taxation, such a practice could produce a relaxation of environmental standards. Likewise, the suggestion that consumers should exercise their influence by not purchasing products that create undue pollution assumes a high degree of public awareness and cooperation. It would do little to protect the minority of individuals who are especially vulnerable, such as those living near dump sites or extremely congested areas.

The records of the Occupational Safety and Health Administration, Food and Drug Administration, and Environmental Protection Agency mirror the difficulty of reconciling the need for safety with economic realities. Analysts indicate instances of both underregulation and
overregulation and make the point that regulation in the area of protection, as in other concerns, involves readjustments to changing circumstances. Rather than simple formulas for safety, critics stress that the key words are evaluation, reevaluation, and flexibility. Whether the future brings more or less individual and environmental protective regulation largely depends on the continuing degree of worker disability, dangerous foods and drugs, and environmental contamination.

NOTES

3 84 Stat. 1590.
6 Thorne G. Auchter, Statement before the House Education and Labor Committee, March 30, 1982. Transcript provided to the authors by the Department of Labor.


34 Stat. 768.
52 Stat. 1040.
72 Stat. 1784.
76 Stat. 780.


Protection: OSHA, FDA, and EPA

38 83 Stat. 852.
39 A complete description of the political background to the establishment of the EPA appears in Alfred A. Marcus, Promise and Performance: Choosing and Implementing an Environmental Policy (Westport, Conn.: Greenwood Press, 1980).
40 84 Stat. 1676.
41 84 Stat. 94.
42 86 Stat. 819.
44 88 Stat. 1661.
45 90 Stat. 95.
49 94 Stat. 50; 94 Stat. 2767.
50 Marcus, Promise and Performance, pp. 167-68.
52 Marcus, Promise and Performance, p. 165.
Change and Values in Technological Society

The study of regulation should generate as many questions as it answers. This is in part due to the relationship among change, values, and regulation. The American system is a complex political economy that is in the process of change, change that reflects political, economic, and social values. Regulation, rather than being an objective process about which everyone can agree, serves to reflect and express values and influence the direction and pace of change. The impulse to intensify regulation during the early 1970s expressed values of guaranteeing equality of opportunity and conditions in environmental protection, workplace protection, and employment practices regulation. Yet the impulse to deregulate during the late 1970s and early 1980s reflects values as well, such as an emphasis on freedom of action, individual choice, and the association of material reward with economic effort and responsibility.

It is important to note that while regulationists and deregulationists often disagree about the means of economic development, and about the values that lie behind these means, they often agree upon ends or goals. Most people agree that the American economy will not return to the simplicity of the past. Industrialization, technology, and innovation seem to be permanent ingredients in the modern era. America will never return to the Jeffersonian agrarian ideal. Nor will it again resemble the nineteenth century, when land was plentiful and natural resources seemingly unlimited.

Regulationists and deregulationists agree upon worthy economic goals. A healthy economy is characterized by low unemployment and minimal inflation, an expanding gross national product, and an increasing proportion of individuals living well above subsistence levels. There should be competition between firms, as well as an elimination or less severe occurrence of recessions.
But questions remain as to the role of government and private initiative. What are the boundaries of responsibility between individuals, companies, and the government in various areas of economic activity? Where does or should economic power lie, with the "general interest," the largest corporations, or specific branches of government? What problems are created by government intervention, and what problems are created or exacerbated due to the lack of it? How is government and private action justified, and what constitutes a sufficient rationale?

It is unlikely that these questions can ever be entirely answered, since they involve issues of values and opinion, as well as more objective economic and scientific analysis. It is hoped that the study of regulation deepens the meaning of such questions and that it demonstrates that the balance between government and private action is uncertain, an open issue subject to continual reevaluation.
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