THE POLITICAL ECONOMY OF REGULATION

By
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In recent years government regulation has increased, whilst a number of forces have worked to decrease, in real terms, the power of private enterprise to regulate its own behaviour. In this article, Dr Fels explores a number of questions relating to the desirability of, and alternatives to, regulation and examines the relevance of current economic theory to such questions. He discusses which economic interests are served best by regulation and canvasses the main forms which regulation may take. Dr Fels evaluates also the economic and political difficulties that arise as a result of conflicts between different regulatory policies.

I. INTRODUCTION

> . . . the Australian economy is in most important respects a regulated economy. It is not, to quote the 1962 Economic Survey again, "a preponderantly free enterprise economy, in which the great bulk of goods and services are provided in response to demand, local or foreign" — not at least in the traditional sense of such an economy, one in which "normal market forces" determine the direction of resources. It is riddled with controls and interventions, quotas and fixed prices, subsidies and barriers to competition. Above all, it is in many respects, possibly in most important respects, a planned economy — although it may not seem so because the "planning" which takes place is chaotic.[1]

The writer of the above quotation was as concerned with the relatively unconstrained power of many firms to regulate their behaviour as with the effects of government intervention. It is at least arguable that a number of forces have on balance reduced (or led to no net increase in) the power of firms to regulate their own behaviour in the last twenty years. These forces include the enlargement of the Australian market brought about by demographic and economic growth, the greater

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penetration of the manufacturing sector by imports in the 1970's, the abandonment of import controls in 1960 (though re-introduced in some sectors in the mid 1970's), keener scrutiny of tariff protection, and the introduction of trade practices laws.

Government regulation, "the substitution of commands and controls for the economic signals of the market place",[2] has been on the increase in Australia as elsewhere.[3] From 1960 to 1969, Federal and State Parliaments passed 6,928 Acts and Federal and State Governments made 12,420 statutory rules. From 1970 to 1979, 9,703 Acts were passed and 20,131 regulations were made.[4] A recent study suggests that regulatory laws have increased from around 15% to 30% of total Federal enactments during the second period.[5] There has also been a growth in the number of government agencies which have to be dealt with by the private sector.[6] It has been estimated that the proportion of the American GDP being produced in regulated sectors has risen substantially in the last ten years,[7] and there may have been a similar trend in Australia.

The extent and growth of regulation gives rise to a number of important questions:

(a) When is regulation desirable? Has the likelihood of market failure been exaggerated in particular cases? Are there alternatives to regulation? What are the effects and costs of regulation? Does "government failure" replace market failure? In the changed economic environment of the 1980's, with 'slowth' likely, can regulation be afforded? Has government overreached itself in trying to regulate so many economic activities? Should there be de-regulation? What economic and political difficulties arise in deregulating industries which should not have been regulated originally?

(b) Given the existence of regulation, have the best methods been chosen? Has sufficient reliance been placed, for example, on the provision of incentives to achieve desirable results or have less efficient means of achieving regulatory goals been chosen?[8] Having regard to its enforcement costs, has an optimal amount of regulation been implemented?[9] Having regard to its enforcement costs, has an optimal amount of regulation been implemented?

(c) Are there conflicts betwween different regulatory policies, for example, environmental protection and energy conservation? Are there conflicts between regulatory policies and other economic policies, for example, policies which aim to promote more competition?

1 M. Newton, "The Economy" in A. F. Davies and S. Encel (eds.), *Australian Society: A Sociological Introduction* (1965) 247-248.

2 Economic Council of Canada, *Regulation Reference: A Preliminary Report to First Ministers* (November, 1978) Document: 800-91004.

3 M. L. Weidenbaum, *Business, Government and the Public* (1979).

4 Confederation of Australian Industry, *Government Regulation in Australia* (paper 1, 1980) 46, 51. The length of Federal Acts has increased whereas the length of regulations has decreased.

5 *Id.*, 48.

6 Senate Standing Committee on Finance and Government Operations, *Statutory Authorities of the Commonwealth* (first report, 1979).

7 P. W. MacAvoy, *The Regulated Industries and the Economy* (1979) 25.

8 It is this kind of question which has been the concern of economists like Schultze. See C. L. Schultze, *The Public Use of Private Interest* (1977).

9 G. J. Stigler, "The Optimum Enforcement of Laws" (1970) 78 J. Pol. Econ. 526.

(d) In view of the widespread existence of regulation, are modifications required of economic theory in order to increase its predictive power and relevance to the real world?
(e) Finally, there are questions which are of special concern in this paper. Which economic interests does regulation serve? Does it serve the general interest (in the sense in which this term is used in economics) or sectional interests? Why has regulation increased so much recently? Why do some industries seemingly desire regulation? What characteristics of the political process lead to producer interests predominating over consumer interests in many cases? Can regulation be modelled?

This last group of questions about the political economy of regulation concerns the distribution of income and wealth as much as, or more than, the efficient allocation of resources.

II. THE MEANING OF REGULATION

Before embarking on a survey of regulation it would be useful to define precisely, and to make an exhaustive multidimensional typology of the kinds of, regulation. However regulation pervades the economy and takes many forms; its definition varies with the purpose of the discussion; it shades into other economic policies; and it is more difficult to generalise about than market phenomena. Accordingly, only two comments are made below about the meaning of the term.

First, the term 'regulation' is often used in different senses. At one extreme, some mean any government law or policy affecting the economy. More commonly, many limit the meaning to direct government control or enterprise decisions concerning prices, the amount or quality of output, the nature of the production process (for example, safety rules) and also include the regulation of entry into an industry by licensing, import controls and tariffs. This narrower meaning is designed to contrast regulation with competition, tax and other policies which merely establish a framework and system of incentives within which enterprises are free to make their own decisions. If the purpose is to contrast policies which are more or less market oriented, then this meaning is appropriate.

When, however, the purpose is to explore regulation as part of the political economy of relationships between government and business, a somewhat broader approach is desirable. The forces which give rise to regulation might also be expected to apply to other business legislation. If they do not, a special explanation is required. For this reason, this paper includes a discussion of trade practices institutions, even though on one view they are not regulatory.

A further point about the term is that much of the economics literature derives from the study of 'traditional' regulation in the United States. Traditional American regulation controls prices and/or entry in interstate transport, communication (telephones and broadcasting), electricity production, pipeline transportation, natural gas field prices in the last twenty-five years, and crude oil and refined petroleum product prices since 1973. Traditional regulation is largely industry specific. It differs from the 'new' regulation which relates to health, safety, quality of environment and conservation. Most of this regulation has originated in the last

twenty years.[10] Generalisations based on traditional regulation are not necessarily applicable to regulation which is functional in character and relates to a range of industries. Nor are generalisations about American regulation necessarily applicable to other countries, with different histories, institutions, attitudes and economies.

III. ECONOMIC INTERESTS SERVED BY, AND HYPOTHESES CONCERNING THE EFFECTS OF, REGULATION

> The central tasks of the theory of economic regulation are to explain who will receive the benefits or burdens of regulation, what form regulation will take, and the effects of regulation upon the allocation of resources.[11]

It is useful to begin by identifying the various interest groups which are affected by regulation. These interests are:

(a) the general consumer or public interest;
(b) particular groups of an industry's customers who receive discriminatory treatment, either favourable or unfavourable, as a result of regulation;
(c) producers, or sub-groups of producers, in the regulated industry itself;
(d) employees or other suppliers of inputs to a particular industry;
(e) producers of substitute or complementary goods;
(f) groups which do not consume the principal output of an industry but which are subject to actual or self-perceived externalities arising from its activities. Examples include persons living near factories which cause pollution, and temperance groups seeking liquor regulation;
(g) the regulators;
(h) the government (for example, where regulation allows the industry to make monopoly profits which the government appropriates for itself through taxation or other means);
(i) politicians and political parties.

This enumeration suggests that many hypotheses concerning the effects of regulation are possible. Empirical studies of regulation only sometimes conclude that regulation serves one interest exclusively at the expense of all others. Nevertheless for the limited expository and analytical purposes of this paper, it is desirable now to outline in their simplest forms, and to offer a brief critique of, the chief hypotheses in the literature.[12] The theoretical basis, often implicit, of these hypotheses is not set out. In the following sections of the paper, however, the theoretical basis of a particular version of one such hypothesis by Stigler is examined in greater detail.

The *consumer protection hypothesis* states that regulation is intended by legislatures to, and in fact does, protect consumer interests by securing improved

economic performance. Regulation is a response to actual or potential market failure, and leads to an improvement in performance, compared with an unregulated situation.

Difficulties with this thesis include:

(a) regulation is not restricted to highly concentrated industries where the danger of monopoly abuse is greatest nor to the industries generating substantial external costs. Such restriction is certainly not observed in the United States where some potentially very competitive industries are regulated, for example, trucking.[13] In other cases, regulation has little connection with the externalities to which the industry's production or consumption give rise;

(b) regulation is not a costless activity. There may be massive government failure in place of market failure. Many studies claim to show that the costs of intervention, including side-effects, exceed the benefits;

(c) in many regulated areas, the likelihood of market failure may have been exaggerated through superficial analysis. There is, for example, reason to believe that markets might work well (or, at least, better than regulated markets) even in such fields as medicine, drugs and the law, if given the opportunity.

The *perversion hypothesis* states that, although the intended purpose of regulation is to protect consumers, the regulated industries have managed to pervert their regulators until the regulators become the protectors of the regulated rather than the customers. Regulators come to identify with industry interests because life is easier if they do so. In some cases particular weaknesses in regulatory procedures or personnel may explain the failure of regulation. On this view, there is nothing inherent in the failure of regulation; weaknesses may be remedied as society gains experience of regulation.

A possible theoretical basis for this hypothesis has been advanced by Bernstein,[14] who proposed a life-cycle theory of regulation. Regulation is created to serve the general interest but eventually is captured by, and comes to serve the interests of, the regulated. Initially the agency is established after the will of a public interest minded majority of legislators prevails over the opposition of a minority. The minority, however, lives on to develop a working relationship with the agency. The interest and support of the majority begins to wane, and the minority interest comes to prevail.

This hypothesis can be criticised because:

(a) the theoretical underpinning of the hypothesis, to the extent that there is one, is questionable. Why should a general interest prevail initially and then wane? If an interest group is strong enough to capture an agency, why is it not able to fend off regulation in the first place?;

(b) it ignores that much regulation is desired, and often principally brought about, by the regulated, for example, hotel and taxi licensing. This is not to say that they do not voice public interest conditions with the aim of achieving regulation that serves their own interests;

13 Trucking regulation is not a response to possible externalities generated by this industry either.

14 M. Bernstein, *Regulating Business by Independent Commission* (1955).

(c) the evidence often does not accord with the theory, and in some cases the opposite circumstances to those postulated by Bernstein occur. Some regulatory agencies serve the interests of a regulated industry initially, but in later life become reinvigorated and begin to serve a wider interest.[15]

(d) evidence of actual mismanagement by regulatory agencies is weak. Rather, they are reasonably efficient in the pursuit of questionable goals set by the legislature, for example, the Victorian Liquor Licensing Commission is not usually accused of inefficiency. Its fault is perhaps a zealous pursuit of statutory goals that are not in the public interest.

Despite these criticisms a virtue of Bernstein's hypothesis is that it draws attention to the dynamics of regulation and to the fact that the interests served by regulation may alter over the course of time.

A common weakness of both the consumer protection and perversion hypotheses is that they both fail to trace through adequately the process by which the general interest is translated into legislative action. For these hypotheses to be acceptable, a theory of political behaviour would be necessary to show that legislatures in fact act in the public interest. At best, these hypotheses contain an implicit theory of 'benevolent' government in which legislation is always in the public interest.

The *'no effect' hypothesis* states that regulation has no significant effect, other than imposing certain administrative costs. The only costs are the bureaucratic costs (for example, the budget cost of the regulation) and any costs the process imposes on the regulated (for example, filling in forms, having lawyers, and diverting management time from productive activities).

There is no well developed theory on this, but some American studies claim to demonstrate that the performance of monopolies which are regulated in some States but not others differs little.[16] However, it seems that this evidence is not beyond question.[17] Jordan has also suggested that much of the evidence purporting to show that regulation has no effect can be accommodated within the producer protection hypothesis, once proper account has been taken of the market structure prevailing before regulation.[18]

The *producer protection hypothesis* states that the effect of regulation is to increase or sustain the economic power of an industry. Producer protection hypotheses enjoy the support of some odd bedfellows, including Marxists, Ralph Naderites and Chicago economists. The first two of these groups differ from the Chicago economists however, in tending to limit the applicability of the thesis to big business producers. The Chicago economists emphasise the applicability of the theory to small businesses as well. Producer protection hypotheses also enjoy the support of some political science interest group theorists who see regulation as being captured by interest groups but who do not advance explanations of which interest groups are successful and when.

15 The Australian Tariff Board is a possible example.

16 The classic study is G. J. Stigler & C. Friedland, "What can Regulators Regulate? The Case of Electricity" (1962) *5 J. Law & Econ.* 1.

17 MacAvoy, note 7 *supra*, surveys the studies and finds "traditional" regulation has many effects which vary from one period to the next.

18 W. A. Jordan, "Producer Protection, Prior Market Structure and the Effects of Government Regulation" (1972) *15 J. Law & Econ.* 151.

The foregoing are the most widely cited hypotheses concerning regulation. Yet it is apparent from the enumeration of interests which regulation might serve that further hypotheses could be advanced. The possibility that the chief beneficiaries of regulation, and the main forces in the maintenance of regulation over the course of time, are the regulators themselves, for example, has considerable appeal as a possible hypothesis.[19] In addition, the foregoing hypotheses mostly reduce regulation to serving, or predominantly serving, single interests. Up to a point, it is an acceptable and useful simplification to reduce hypotheses to such specific forms, but in reality regulation often involves a complex balancing of multiple interest which any single factor hypothesis is of limited value in explaining. Moreover, the above hypotheses relate mainly to the question of the interests which regulation serves. There may be other influences on the introduction or retention of regulation. Scherer points out that regulation may be imposed because, no matter how efficiently the market is working, those who hold political power are displeased with the results or consider some good or service too important to be priced and allocated by market means. This is the 'governmental habit'.[20] Ideology may also be important.

Sometimes regulatory legislation exists principally for symbolic reasons, and is not well explained by economic interest group theories. Income politics have sometimes been introduced as a symbol of government concern with inflation at a time when other policies which are bound to be inflationary are introduced.[21] It has not been intended in such cases that the policies should have any substantial effect. The same suggestion about antitrust policies has been made by Thurman Arnold.[22] Regulation of the 'oldest profession' has also largely amounted to a symbolic expression of public disapproval, whilst not intended to stamp out prostitution.

There are also frequent conflicts and even contradictions in regulation. Governments have anti-smoking campaigns but take steps to encourage farmers to grow more tobacco; they help the liquor industry with licensing laws but hinder it with trade practices laws and with measures against drink-driving; conflicts occur between energy conservation and environmental protection laws; tariffs are introduced to allow firms to raise prices, while price control bodies prevent this. This is only to refer to conflicts at one level of government. Conflicts between governments at different levels are even more obvious. Up to a point, conflicts in regulation are the product of rational behaviour by politicians. In the tobacco example above, the politician may be able to satisfy both the tobacco grower and the anti-smoking lobby. However, it is doubtful that all such examples can be so explained and theories which point to government actions as being the result of the demands of interest groups do not provide a very adequate explanation of such complexities and compromises.

19 The bureaucratic empires associated with the licensing of taxi-cabs in most states and with the licensing of builders in New South Wales suggest the applicability of this.

20 F. M. Scherer, *Industrial Market Structure and Economic Perfomance* (2nd ed. 1980) 482. See also J. R. T. Hughes, *The Governmental Habit: Economic Controls from Colonial Times to the Present* (1977).

21 M. Edelman & R. W. Fleming, *The Politics of Wage-Price Decisions* (1956).

22 "In order to reconcile the ideal [industry is made up of small competing concerns] with the practical necessity, [of bigness of firms] it became necessary to develop a procedure which constantly attacked bigness on rational legal and economic grounds, and at the same time never really interfered with combinations." T. Arnold, *The Folklore of Capitalism* (1937) 207.

IV. STIGLER'S THEORY OF ECONOMIC REGULATION

> The interest of the dealers, however, in any particular branch of trade or manufactures, is always in some respects different from, and even opposite to, that of the public. To widen the market and to narrow the competition, is always the interest of the dealers. To widen the market may frequently be agreeable enough to the interest of the public; but to narrow the competition must always be against it, and can serve only to enable the dealers, by raising their profits above what they naturally would be, to levy, for their own benefit, an absurd tax upon the rest of their fellow-citizens. The proposal of any new law or regulation of commerce which comes from this order ought always to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous, but with the most suspicious attention. It comes from an order of men whose interest is never exactly the same with that of the public, who have generally an interest to deceive and even to oppress the public, and who accordingly have, upon many occasions, both deceived and oppressed it.[23]

Stigler's theory of economic regulation[24] has its general antecedents in the classical writings of Adam Smith and Karl Marx and in the more recent work of Downs, Becker and Buchanan and Tullock, who have formulated economic theories of politics, though not with reference to regulation.

Prior to Stigler, a number of empirical studies had concluded that in certain cases regulation served sectional rather than general interests. These studies, however, were simply observations of particular situations and did not advance generalisations as to why or under what conditions regulation might so operate and gave no basis for predicting whether in other cases regulation would work in the sectional or general interest. Stigler's contribution is to attempt to go beyond observations without theory and to devise an operational theory of regulation.

A central thesis of Stigler's paper is "that, as a rule, regulation is acquired by the industry and is designed and operated primarily for its benefit".[25] It is only in exceptional cases that regulation has an onerous effect upon an industry.

The machinery and power of the state, in particular its unique power to coerce, is a potential resource or threat to every industry. The legal power of the state to seize money by taxation and to give it to others; the power to ordain the physical movements of resources and the economic decisions of households and firms without their consent; and the power to prohibit or compel, all provide the possibility for industry to harness the state in order to increase profitability. The state is a potential input in the productive process.

Accordingly, there will generally be a positive demand by industry for the resource of state power. There are four main policies which an industry may seek: a direct subsidy of money; control over entry by new rivals (for example, by licensing, or protective tariffs); policies which affect substitutes and complements; and price fixing. Of these, subsidies are not in widespread demand. They will be dissipated among a growing number of rivals, unless entry to the industry can be controlled.

23 A. Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (1920) Vol. 1 231-232.
24 Note 11 *supra*.
25 *Id.*, 3.

State control over entry may be more efficacious than any controls the industry itself can erect. In addition, controls may be designed to retard the rate of growth of new firms, for example, by prohibitions on price-cutting. The benefit of tariff may be dissipated by the entry of new domestic producers and would ideally be accompanied by domestic entry controls (although this is rare in practice). A tariff is most effective if there is a specialised domestic resource necessary to the industry, for example, a class of raw materials. As to policies affecting complements and substitutes, two Australian examples are provided by railways which seek laws which limit the carriage of certain products by road, and taxi interests which attain laws prohibiting car pooling for profit. On occasion, the defensive power of various other industries affected by regulation must also be taken into account by the industry seeking regulation. As to price-fixing, a publicly operated and enforced cartel is often cheaper and easier to run, and more effective than a private cartel. A private cartel often is not feasible because of the cost of participants agreeing on prices and outputs and of enforcing agreements (especially to prevent free riders gaining benefits).[26] The setting of a minimum retail price for packaging in Victoria was impossible until the Victorian Government passed the necessary legislation (quite apart from difficulties under the Trade Practices Act 1974 (Cth)). Many other forms of regulation, for example, uniform shopping hours, could not easily be achieved by private agreement.

A minority of industries will not have a positive demand for regulation where, for example, control of entry, substitutes, or prices, is not feasible. Moreover, the calculus of profitability of regulation of an industry is affected by three political limitations upon the exercise of cartel policies by an industry. First, the distribution of control among the firms may be changed to reflect differences in the political as opposed to economic influence of firms. Small or rural or domestically owned enterprises may benefit relatively more. Secondly, costs associated with the procedures of regulation may be substantial. In the case of hotel regulation in Australia, there are also significant costs in providing accommodation and catering of a sufficient standard to satisfy State liquor control commissions, since an important ostensible justification of liquor control is to maintain high standard premises. Thirdly, powerful outside interests are admitted to the industry's councils, for example, in the allocation of television licences in Australia, rural interests have gained a disproportionate allocation, and union groups, chiefly Actors Equity, have gained a share of the monopoly rents by means of heavy Australian content requirements.

Regulation of the above kinds is often against the interest of the majority of the population in democratic societies. If a well-informed national population voted by referendum on each single political issue, one might expect *prima facie* that many forms of regulation would be rejected. What characteristics of the political process ensure that there is a supply of regulation? What is the cost to an industry of acquiring legislation? What form of cost is involved?

26 This point is developed by Posner, note 12 *supra*.

The availability of a supply of regulation is explained by an 'economic' theory of politics which cannot be fully set out in a paper of this length. In essence, political voting is not usually on single issues but occurs in relation to many groups of issues simultaneously. In addition, the whole community votes or can vote, not just those directly concerned with the issue. To cope with these and other characteristics of the political process, there are elected representatives organised in political parties.

The benefits from regulation of an industry tend to be concentrated in favour of a relatively small number of beneficiaries, each of whom stands to gain substantially. The stake of the individual consumer in any one product is small, and consumer interests are diffused across the whole range of goods and services. It may pay a firm to spend a great deal of money in relation to a regulatory matter, while an individual consumer, confronted by the prospect, say, of a small increase in price to him, will find it is worth only a miniscule amount to obtain information and to protect his interests even though, in aggregate, consumer interests equal those of the regulated industry.[27] Moreover, there are sizeable transaction costs in organising coalitions of consumers. There may also be free-riders prepared to share the gains from interest-group activity, but not prepared to contribute. Concentrated groups of beneficiaries suffer much less from these problems. The prospective benefits are large, the costs of organising a group are less, and free-rider problems can be more easily limited. As Peltzman explains,[28] Stigler asserts a law of diminishing returns to group size in politics. Beyond a point it is counter-productive to increase the size of an interest group, while spreading the benefit from its activity more widely, as costs per head rise faster than benefits per head. This limits the size of groups seeking regulation.

In order to acquire a supply of legislation, an industry must offer a political party votes and resources, principally of a financial kind. Hence the amount and kind of the resources of State power which is made available to an industry for its benefit depends upon the interaction of the various supply and demand factors enumerated by Stigler.

In summary, the theory predicts that regulation tends to convert formerly competitive or oligopolistic industries into cartels: that is, regulation helps previously independent producers to form what is, in effect, an agreement to act together. This increases the effectiveness of an existing cartel, and maintains an existing monopoly (or cartel) where rival firms would otherwise enter to provide competition in response to the growth of markets or the development of new technology. On the basis of this hypothesis regulation can be expected to increase prices, promote price-discrimination, reduce or prevent the entry of rival firms, prevent price-cutting and increase or preserve industry profits.

27 M. J. Trebilcock, "The Consumer Interest and Regulatory Reform" in G. B. Dearn (ed.), *The Regulatory Process in Canada* (1978) 102.

28 S. Peltzman, "Toward a More General Theory of Regulation" (1976) *19 J. Law & Econ.* 211, 213.

29 See Posner, note 12 *supra*, for one survey.

The chief virtues of Stigler's contribution seem to be:

(a) it establishes a model of regulation which is an alternative to those which assume that regulation serves consumer interests. As such it is a strikingly effective way of demolishing the assumption (often implicit) in economic theorising that regulation will automatically overcome market failure;

(b) it focuses attention on the fact that the central tasks of the theory of regulation are to explain who will receive the benefits or burdens of regulation, what form regulation will take, and the effects of regulation upon the allocation of resources;

(c) it suggests that the political process which creates regulation is capable of modelling;

(d) it identifies the particular benefits as well as costs to industry of regulation.

Stigler has thus injected real content into the theory of regulation. His theorising represents an advance on crude hypotheses which simply state that regulation, and other forms of government activity, is influenced by interest groups without saying under what circumstances and why.

V. THEORETICAL EVALUATION

This section of the paper discusses a selection of theoretical difficulties with Stigler's views, mainly taken from within the paradigm of the economic theory of politics. No attempt is made to raise all the difficulties.[29]

1. An attempt by Peltzman[30] to formalise and generalise Stigler's theory without significantly changing its assumptions should be noted. The general effect of Peltzman's paper is to modify Stigler's conclusions. Peltzman establishes that even if a single economic interest obtains all the benefits of regulation, these must be less than the group could obtain if its economic advantages were fully exploited, that is, a rational, vote-maximising regulator will limit the gains from regulation, for example, by controlling the price of a cartel. A rational vote-maximising regulator will also exploit differences *within* groups that win and lose from regulating as a whole. Thus, although a group of customers as a whole may lose from regulation, some will lose less or even benefit from cross-subsidisation enforced by regulation. Rural customers in remote areas, for example, may be supplied with uneconomic air transport services. Expressed more generally, Peltzman establishes that the constituency of the regulator cannot be limited to one economic interest: "even if groups organize according to an economic interest (producers v. consumers), political entrepreneurship will produce a coalition which admits members of the losing group into the charmed circle".[31] The importance of these modifications is an empirical matter, but they are potentially far reaching. The ultimate logic of Peltzman's argument is that it is not clear which coalition of interests will win in the competition to control regulation. This also makes it difficult to test Stigler's theory empirically.

30 Note 28 *supra*.
31 *Id.*, 222.

2. Stigler, and Peltzman especially, assume that the goal of regulators is to maximise election majorities. This seems an inadequate approach to the motivation of regulators. The attainment of election majorities is only one aim of politicians. The motivations of those employed as regulators must also be considered. These motives could include the maximisation of the budgets of regulatory bodies (as Downs and Niskanen suggest);[32] the survival of the organisation; or, the enjoyment of a quiet life by the minimisation of conflicts and responsibilities. The motivation of regulators may also vary depending upon, for example, whether their careers are associated with the regulatory agency, whether they have longer-term political or other aspirations in other fields, or whether they belong to a profession, the maintenance of whose esteem is all important.[33] Regulatory agencies may also attract individuals with a personal commitment to the public interest goals of the agency.

3. The "economic theory of politics" approach to identifying factors relevant to the demand for and supply of regulation is rather narrow. The industry demand for the establishment and, more particularly, the continuation of regulation, is influenced not only by profit-maximisation but also, very importantly, by a quest for economic security or protection against the changes which an unregulated market may impose.[34] The political supply of regulation is also influenced by factors other than the votes or political contributions which regulated industries can offer political parties. A government is judged by the electorate according to the performance of the whole economy in relation to such goals as employment, price-stability, growth and income-distribution. Yet it is business which is largely responsible for the achievement of those goals. A major concern of all government policies, therefore, is to encourage businessmen to perform well and it does this by the provision of numerous incentives which cannot be analysed in such narrow terms as vote delivery or financial contributions.[35] In addition, actions in one industry may have an important symbolic value across a range of industries. The recent attempt to protect the interests of small, independent service station owners may have been motivated by a Commonwealth Government wish not to appear unconcerned at the plight of small businessmen generally.

4. A fundamental criticism is that the political basis of Stigler's theory collapses when regulation takes forms other than the conferring of concentrated benefits on groups and the imposing of diffused costs.[36]

The table below sets out some of the main forms which regulation may take. It is possible to imagine forms of regulation which correspond to each element in the matrix.

32 A. Downs, *Inside Bureaucracy* (1967). W. A. Niskanen, *Bureaucracy and Representative Government* (1971).

33 J. Q. Wilson, "The Behaviour of Regulatory Agencies" in J. Q. Wilson (ed.), *The Politics of Regulation* (1980) 374.

34 T. J. Courchene, "Towards a Protected Society: the Politicisation of Economic Life" (1980) 13 *Canadian Journal of Economics* 556, 558.

35 See C. E. Lindblom, *Politics and Markets* (1977) Ch. 13.

36 Note 34 *supra*.

REGULATORY IMPACTS ON PRODUCERS AND CONSUMERS

		Impact on Regulated Industry				
		Concentrated Benefit	Diffused Benefit	No Effect	Diffused Cost	Concentrated Cost
Impact on Consumer	Concentrated Cost					
	Diffused Cost					
	No Effect					
	Diffused Benefit					
	Concentrated Benefit					

There are at least three important forms of regulation which Stigler overlooks. In the first form of regulation overlooked, costs to be regulated may be concentrated and benefits (or perceived benefits) to the public diffused. A significant component of the "new" regulation falls into this category. Examples include car safety requirements, food and drug safety laws, meat inspection laws, drink-driver laws, regulation of cigarette advertising and consumer finance regulation. Stigler's theory implies that regulation of this kind would not exist.[37]

A second form of regulation may involve diffused costs to the regulated and diffused benefits (or perceived benefits) to the public. Possible examples are consumer and environmental protection laws, and occupational safety laws. An economic theory of politics would not necessarily predict that this kind of regulation would operate in the interests of producers and there is in fact ample evidence that the "new" general regulation has not so operated.

A third form of regulation involves a narrow concentration of costs and benefits between organised groups. American trucking regulation has reflected the struggle between rail and trucking interests. Employer/employee conflicts over labour law, margarine production restrictions, contests between large and small enterprises in an industry, and between manufacturers, wholesalers and retailers, provide further examples. It is difficult to predict in such cases which interest, if any, will predominate.

The above are not the only possible categories. They do not take account of all the interests listed in Section III of this paper, nor the full range of cost and benefit possibilities. They may focus too sharply on the extremes of "concentrated" and "diffused" in the cost/benefit spectrum, and ignore intermediate possibilities.

37 It may often be, however, that after the initial legislation has been passed, the regulated industry succeeds in largely neutralising the impact of the legislation. Yet even this is not obvious from the above examples.

The general significance of these other forms of regulation is that there is no reason, based on the economic theory of politics, to expect all of these forms to serve producer interests. The reformulation of a more general theory of regulation derived from an economic theory of politics is, however, a possibility, providing that account is taken of the different forms of regulation.

5. Stigler's theory overlooks the tendency of legislatures to establish regulatory bodies which are largely independent of the political process in order to avoid undue sectional pressures being applied to themselves. This is especially the case with bodies which are not industry specific. Australian examples, which include the Industries Assistance Commission, the Trade Practices Commission, and the Prices Justification Tribunal, are considered later in this paper. Although it is concluded that these bodies do not serve industry interests directly, it could be that in some cases they lend a respectability and legitimacy to processes which, taken as a whole, do serve the interests of industry. Thus, it might be contended that the Industries Assistance Commission, for all of its criticisms of protection, has had little effect on tariff policy.

6. Stigler has little to say about the dynamics of regulation. No doubt in a formal sense his theory could be elaborated to deal with the effect of changes in the supply of, and demand for, regulation. On the demand side, for example, the logic would be that recent increased regulation resulted from an increased wish for regulation by business, either through a fall in the cost of acquiring it or an increase in the demand for it at an unchanged cost. This would be absurd. The new regulation has generally been opposed by business and its introduction is difficult to explain in terms of the politics of economic interest groups. A behavioural theory of politics is of limited value in explaining the social and economic forces which have led to the recent increase in regulation. A study of recent economic and political history is more relevant. Relevant factors include a mixture of economic and social elements such as changed expectations of the ability of governments to solve social problems; the impact of Keynesian ideas on the size of government; attitudes that technology would solve all problems; high income-elasticity of demand in affluent society for goods and services which the market is poor at delivering; increased affluence; urbanisation and the resulting greater interdependence of people; the role of research in uncovering, documenting and exposing areas of market failure and the impact of Keynesian ideas on the size of government; attitudes that technology crusaders and entrepreneurs like Ralph Nader; the fact that a wide range of social groups have become organised or active; new ideas about social justice; the decline of deference by lower income groups; and the fact that the introduction of regulation often breeds demand for further regulation.

Stigler's thesis that "regulation is as a rule acquired by industry for its own interest" is most unhelpful in explaining this. It also fails to explain the recent rise of the deregulation movement!

7. For a theory concerned with questions of distribution, there is a neglect of the impact of regulation on different income levels and social groups. The "producer interest" embraces both capital and labour. The "consumer interest" or "the public interest" may embrace the rich or the poor in different cases. The liquor licensing laws probably impose a greater relative cost on persons in the bottom half of the income distribution, while the lawyers' conveyancing monopoly probably imposes a

proportionate, even a progressive, tax on persons with higher incomes. These conclusions need to be modified to the extent that the costs of regulation can be shifted. Wage and pension indexation, for example, may shift the cost of liquor regulation. The benefits of legal monopoly go to the people who constitute a middle or upper class group, while the liquor monopoly benefits are enjoyed by brewery managers and unions, brewery shareholders, regulators, and beneficiaries of the tax revenue (largely the public). Despite the difficulties of assessing the impact of regulation on the distribution of personal income and wealth, and on different social groups, a theory of regulation which overlooks this point altogether, and instead focuses on the technocratic point that producers appear to gain at the expense of consumers, is limited in its dimensions. To grasp the social significance of regulation, it is necessary to go beyond the categories of producer and consumer. Some regulation takes on a different significance when it is recognised which social groups stand to lose and gain from it. In general, it is not clear which social strata and income groups regulation benefits or hurts most, but it is a question which must be addressed, especially if policy conclusions on deregulation are to be considered.

The work of Lindblom in particular also raises an important related question. Lindblom contends, or implies, that government policies are biased in favour of big business. Whether or not this perception is correct (it does not seem to be shared by some important modern Marxists, for example), it does also raise the general question of whether the whole system of regulation exhibits general biases in one economic or political direction or not, and of whether theories of pro-producer bias need to be seen as an element in a broader picture.

8. It needs to be remembered that the emphasis in Stigler's theory on regulation as a device for redistributing income between groups in society tends to distract attention from the important possibility that far from being a zero-sum game, regulation may benefit or harm both producers and consumers.

9. Stigler's theory in its original form with its various qualifications, and Peltzman's formalisation, are both difficult to test in any simple fashion. In considering Australian applications of the theory, this paper will, to a considerable extent, rely on the simplest form of producer protection hypothesis.

The foregoing criticisms, which by no means exhaust the difficulties with Stigler's approach, mostly tend to limit and qualify, rather than destroy, Stigler's theory. They suggest, amongst other things, that industry specific regulation which confers concentrated benefits on concentrated industries and diffused costs on consumers is likely to exhibit a bias towards producer interests but that capture will be incomplete and some account will be taken of other interests. On the other hand, general regulation (and general constitutional rules) is unlikely to exhibit such a bias. The applicability of this generalisation is considered in later sections of the paper. A further issue posed in later sections is whether in the cases examined, a simple consumer protection hypothesis fits or whether a simple producer protection hypothesis fits better. Attention is also directed to the kinds of qualifications and complications which arise with simple theories. For the most part, little attempt is made to distinguish Stigler's theory from other producer protection theories.

VI. SOME SIMPLE APPLICATIONS

By way of further illustration and broadbrush testing of Stigler's theory, three cases are briefly considered: the lawyers' monopoly; liquor licensing; and the Australian tariff. At first sight, all may appear to conform with the predictions of Stigler's theory, though even the brief analysis of this section suggests in each case that there are significant complications.

1. Lawyers

In most Australian States, lawyers enjoy a statutory monopoly of most legal work. Subject to minor exceptions, only a barrister or solicitor has a right to appear on behalf of another person in a court. Only a qualified solicitor may act as a solicitor or, as such, issue any process or carry on or defend a proceeding in the name of another person in any court. With few exceptions, no one other than a barrister or solicitor can charge for various kinds of probate work, or for preparing a will, or any instrument which creates or regulates rights between parties, or relates to real or personal property or to a legal proceeding. In particular, in states other than Western Australia and South Australia, the performance of property conveyancing work for reward is restricted to qualified members of the legal profession. In South Australia, land brokers dominate conveyancing, though they must be licensed. Western Australia has adopted a more market-oriented approach with no licensing requirements for its settlement agents.

Solicitors' fees in non-contentious matters are set in New South Wales by a General Order. This is a committee comprising three judicial officers, the President of the Law Society, and one or more practising solicitors selected by the Chief Justice.[38] In Victoria[39] conveyancing fees are regulated by the Solicitors Remuneration Order which in turn is the product of a legal committee. Similar arrangements apply in other States with variations where the conveyancing monopoly does not exist. The fact that the monopoly is the product of State legislation automatically protects it from the Trade Practices Act 1974 (Cth).

Entry to the profession is controlled by practitioners. In New South Wales there is the Barristers Admission Board, comprising mainly judges, though influenced by the New South Wales Bar Association, and the Solicitors Admission Board, comprising mainly judges, though influenced by the Law Society.[40] In Victoria, legal educators play a role in the corresponding bodies. However, contrary to Stigler's theory, inflow into the profession has often not been seriously limited. The New South Wales Law Society, for example, worked for the establishment of additional law schools in New South Wales so that all who wished to qualify would have the opportunity to do so.[41] As a result, it is not clear that the conveyancing monopoly, in the States where it exists, yields above normal *average* levels of income to lawyers,

38 N.S.W. Law Reform Commission, *The Legal Profession*. Discussion Paper No. 1, *General Regulation* (1979) 40.

39 For an analysis see J. Nieuwenhuysen and M. Williams-Wynn, "Conveyancing: The Pitfalls of Monopoly Regulation Pricing" (1980) 3rd Quarter *The Australian Economic Review* 29.

40 Note 38 *supra*, 36, 39.

41 *Id.*, 49.

even though there are claims that it leads to higher charges to the public, and a higher total of income to lawyers as a whole, than otherwise.[42] Potential monopoly profits *may* have been dissipated by competition for them in a fragmented industry. The legal profession in Australia, as in the United States, appears to have been unsuccessful in comparison with the medical profession in capturing above-normal levels of average income. The success of the medical profession in this regard is attributable to a monopoly of medical practice *and* more restricted entry to the profession. Further qualifications to Stigler's theory are that it does not fit South Australia, nor Western Australia, and that the political origins of the monopoly are probably better explained by the number of lawyers in politics than by votes or political contributions. Accordingly the tentative conclusions must be that, first, it is not obvious that a consumer protection theory fits in a straightforward way, though this paper admittedly does not examine this point;[43] secondly, Stigler's theory does not fit in a straightforward way, though this does not mean it can be rejected totally; and thirdly, the origins and continuation of the system might be partly explained by reference to the theory of political elites.[44]

2. The Liquor Industry

The principal public interest justifications usually advanced for regulating the liquor industry are that the excessive consumption of alcohol gives rise, first, to externalities in the form of noise, nuisance, disorder, public drunkenness and dangerous driving, and secondly, to alcoholism. Licensing, regulation of opening hours, supervision of the standard of the premises and character of the licensee, are claimed to be necessary to help overcome these problems.

It is difficult to take these claims very seriously. Regulation of closing hours restrains drinking in public during those hours, but not in private. During opening hours, the limitation in numbers of licensed hotels and retail outlets for packaged alcohol "does not appear to deprive anyone of the opportunity to drink in excess if he is so inclined".[45] Licensing standards appear to prevent the growth of the kind of popular catering establishment that would serve meals or drinks, or both, as the customer requires (as in Latin countries), and tends to concentrate public drinking in houses which are primarily designed for no other purpose. Moreover, the extremely restrictive system of licensing which is explicitly designed to guard against a possible "proliferation" of licensed premises does not seem justified by the claim that it prevents excessive drinking in unsatisfactory conditions. This argument confuses numbers and standards. The present tight licensing restrictions are not necessary to maintain standards. The standards of hotels can be maintained by the prescription of minimum standards. An increase in hotel numbers might also limit the size of

42 Nieuwenhuysen and Williams-Wynn, note 39 *supra*, provide evidence that average conveyancing charges seem higher in Victoria than in South Australia. It is not intended to imply that it would be in the economic interests of the profession to abolish the conveyancing monopoly since there would be an adjustment period, possibly of considerable duration, before the supply of lawyers adjusted downwards and average incomes were restored to current levels. I assume the supply of lawyers is sensitive to potential income, at least in the long run.

43 Note 39 *supra*.

44 See G. Parry, *Political Elites* (1970).

45 Monopolies Commission, *Report on the Supply of Beer* (London, 1969).

drinking "barns" and the disorder they cause in neighbouring areas. There are alternatives to licensing which would achieve similar objects as well or better: the health laws, the town planning laws, the use of local option, the use of police powers to control public intoxication and drinking by juveniles.[46] Licensing bears only a distant relationship to alcoholism and it seems that other approaches, such as education and treatment, are more appropriate. The public interest theory of regulation fits badly.

On the other hand, producers appear to benefit from the system. The inelastic demand for beer at competitive price levels makes a demand for regulation likely, since high prices make possible the earning of large monopoly profits. The high degree of brewer concentration facilitated the operation of a common retail pricing policy for beer, and in Victoria, for many years before the Trade Practices Act 1974 (Cth) such policy was enforced through financial ties between brewers and hotels and a system of rebates related to observance of the policy.[47]

One of the three objects of the Liquor Control Act 1968 (Vic.) is "that the provision for the orderly and economic development and improvement of that supply should also promote the interest of the businesses of all persons concerned in that supply and advance the security and stability of the same".[48]

Restrictive licensing of retail outlets not only protects hotels from competition but also protects brewers because new entrants cannot establish new distribution outlets. There is, however, the difficulty that many of the gains from regulation have been appropriated by non-producer interests, including Federal and State Governments in the form of excise taxes and licence fees, regulators in the State liquor control bodies, and employees in the form of high wage payments. In addition, there are interstate variations in the nature of regulation. Victorians, who see the establishment of a minimum retail price of packaged beer as confirmation of a producer protection theory, have not only to explain why hotel interests have prevailed over retail liquor merchants, but also why this form of regulation does not occur in other states. In addition, the political origin of liquor licensing is partly explained by the influence of religious groups. Although they have not achieved their ultimate aims of prohibition, their influence in bringing about and maintaining regulation has been very important. The absence of liquor licensing in Latin countries with their different religious attitudes to drinking is a further indication that pressures from producer interests alone may not account for the regulation of liquor trade. Merrett[49] concludes that this "costly and ineffectual" system of regulation persists because it offers something, even if not complete satisfaction, to producers, regulators, governments and religious groups and because the "community probably felt that the social problems associated with drink should be controlled in some way . . . [it] . . . accepted the *status quo* if only because so little information about the impact of the regulation was readily available".[50]

46 Consumer Affairs Council of Victoria, *Submission to the Board of Inquiry into the Liquor Control Act 1968* (Vic.) (1976).

47 D. T. Merrett, "The Victorian Licensing Court 1906-68: A Study of Role and Impact" (1979) 19 *Australian Economic History Review* 123.

48 Liquor Control Act 1968 (Vic.) S.3(c).

49 Note 47 *supra*, 123.

50 *Id.*, 150.

A development of some interest has been the important impact of the Trade Practices Act 1974 (Cth), to a lesser extent the Prices Justification Act 1973 (Cth) and other forms of regulation on the industry. Price agreements by hoteliers were banned and the system of ties between brewers and hotels has been struck down in some states, with other states likely to follow. While the licensing system remains, the impact of these actions on competition in the industry is probably marginal. The brewers also received little comfort from the Prices Justification Tribunal, at least in the early years. Drink-driving legislation with its concentrated costs and diffused benefits has also not worked in the interests of the industry.

In summary then, a public interest theory explains the industry rather poorly, while a producer protection approach gives a better first approximation. Nevertheless, liquor regulation cannot be understood without taking account of religious interests, government and regulatory interests, and the fact that there is public support for some form of action regarding alcohol. Moreover, general regulation and "concentrated costs/diffused benefits" forms of regulation have not been in the interests of the industry.

3. The Australian Tariff

Regulation of the traded goods element of the manufacturing sector is mainly by tariff and other forms of protection policy, such as quotas. In a general sense, the system favours producer, including employee, interests at the expense of consumers. The benefits of protection are concentrated, while the costs are diffused, so that a Stigler-Downs explanation would seem relevant.

A difficulty with political theories of the tariff is that the political pressures affecting tariff decisions are complex, changing and hard to model in a simple way. Many interests oppose, or should oppose, high protection, including importers, some distributors, overseas producers, some consumer groups, and non-protected sectors such as farming and mining groups. Within the bureaucracy and within political parties, there are supporters and opponents. Attitudes to protection have been changing and the nature of protection itself has been changing. The general level of effective protection has fallen in the last ten years, with substantial falls in some sectors, but with an increase in the dispersion of protection, as the footwear, clothing, textiles and automobile sectors have experienced sharp rises in protection.

The structure of assistance to manufacturing has been investigated by Anderson[51] who concludes that the results, while not overwhelmingly convincing, appear to be at least generally consistent with the hypotheses suggested by the economic theory of politics. He also concludes that the evidence concerning changes in the structure of assistance is weaker, but not in contradiction to economic theories of politics.

An alternative approach to explaining the structure of assistance is that once the decision was taken to afford protection to almost any manufacturer who needed it to survive, the structure of assistance depended mainly on the comparative advantages and disadvantages of manufacturing industries vis-a-vis international competition and little on the interaction between lobby groups and the government.

51 K. Anderson, "The Political Market for Government Assistance to Australian Manufacturing Industries" (1980) 56 *The Economic Record* 132.

Gregory suggests that lobby groups may have been more important at broad sectoral levels, and may partly explain why manufacturing, for example, has received more assistance than agriculture or mining.[52] This approach provides a better explanation of the recent increase in dispersion of protection than any political theory.

The above examination of these three cases suggests that a consumer protection or public interest theory fits all poorly; that given the simple choice between producer protection and consumer protection theories, the former provides a better first approximation, and that, nevertheless, a producer protection thesis encounters substantial difficulties even in the three "concentrated benefits/diffused costs" cases considered in this section.

This suggests that there is a need to refine producer protection theories by identifying more precisely the circumstances under which "other complications" of the kind noted in the above cases are likely to arise. The liquor study suggests, for example, that a useful step would be to analyse the conditions under which regulation induced monopoly profits may be appropriated by third parties.

VII. OVERVIEW OF AUSTRALIAN INDUSTRY AND SECTOR SPECIFICATION REGULATION

> On the imposition of uniform duties of customs, trade, commerce, and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free.[53]
>
> Interstate trade and commerce is free from all restriction, whether legislative or executive in character, except to the extent that reasonable regulation of any activity, interstate trade and commerce as much as any other, is necessary to the continued existence of an orderd society.[54]

This section of the paper offers a brief, preliminary, very general and regrettably superficial overview of Australian industry or sector specific regulation as a whole. General forms of regulation that apply across all industries are not considered until the following section.

The primary producing sector is subject to much intervention, regulation and special financial and other assistance. There are organised marketing schemes, price support schemes, price stabilisation schemes and so on. There are, in addition, various special concessions to rural groups, for example, petrol price subsidies and fertiliser subsidies. There are special provisions for the taxation of farm incomes, and for finance of farmers. There are other, less obvious subsidies through government promoted research and road programmes, for example. A good deal of the intervention is piecemeal rather than co-ordinated. Section 92 of the Constitution

52 See comment of R. Gregory on the useful review by K. Anderson and R. H. Snape, "The Regulation of Import Competition and its Effects on the Environment of Australian Industry". *A.N.U. Centre for Economic Policy Research* Discussion Paper No. 5 (1980).

53 Section 92, Commonwealth of Australia Constitution Act 1900.

54 C. Howard, *Australian Federal Constitutional Law* (2nd ed. 1972) 262.

has imposed some limits on the degree of regulation possible. The picture is nevertheless hardly a *laissez-faire* one, and it lends some support to a crude producer protection view. In the words of one writer:

> Public policy towards agriculture is usually most evident in the area of marketing and prices. The stated aims of government policy in this area vary in detail, but they may be epitomised by saying that the primary objective is almost always to raise and stabilise the incomes of farmers.[55]

This is not to say that the agricultural sector is a net gainer from Australian regulation. The tariff imposes a significant cost which cannot be passed on in overseas markets. Similarly, the arbitration system probably does not serve the interests of the farm sector, as the wage costs it imposes cannot be passed on. It is probably only in those sectors which benefit very greatly from direct regulation of agriculture that there is a net gain from regulation.

The mining sector also experiences some regulation, with foreign investment controls, crude oil and some other price controls, some export controls on occasions, environmental and land-use controls, and so on. These do not obviously conform to a producer protection hypothesis.

Both the mining and agricultural sectors, the two chief exporting sectors, are also greatly affected by one form of regulation with pervasive effects on the economy as a whole — regulation of the exchange rate which determines the price in Australian dollars which is received for exports. In the longer term there is not a great deal that governments can do to control exchange-rates directly, as their value is determined exogenously. In the short term, exchange-rate regulation appears to have had some bias towards export and import competing, rather than consumer interests. This has been brought about by a reluctance to revalue quickly enough when the occasion demands (as in the early 1970's) and by a tendency to try to keep the exchange value of the Australian dollar low so as to assist export and import competing sales.

The fact that regulation of the traded goods element of the manufacturing sector by means of protection seems to have had in general a producer protection bias has already been noted. Apart from this, some industry specific regulation occurs within manufacturing, often to the benefit of the regulated. An example includes the brewing industry, also already discussed. In the Victorian bread industry, controls over baking location tend to favour small rural bakers at the expense of large, and probably more efficient, enterprises.[56] Nevertheless the general picture is not one of widespread industry specific regulation in the manufacturing sector. Where it occurs, it may have a producer protection bias.

In communications there are respectable arguments to justify some form of licensing to allocate the limited spectra available. For a long time, however, the allocation of radio licences was greatly restricted so as to favour producer interests. The most notable example was the delay in introducing FM radio. After a long struggle radio licensing has now been liberalised to an extent which confounds the producer protection interest. Many of the benefits of television licensing, however,

55 K. O. Campbell, *Agricultural Marketing and Prices* (1973) 56.
56 D. Cousins, *The Victorian Bread Industry*. Unpublished M. Ec. Thesis, Monash University (1978).

have been appropriated by other interests including: rural interests, with a heavy allocation of licences at the expense of more city allocations; unions, with Australian content requirements; other input suppliers, for example, prices for programmes purchased from overseas are presumably related to Australian revenue; and governments, in the form of special licensing fees.

In the transport sector interstate road transport is largely unregulated, unlike in the United States, despite demands from many in the industry. The controversial interpretation of section 92 of the Constitution by the High Court of Australia has been a major obstacle to regulation. At State level road transport is still regulated to a significant extent, although increasingly the tendency is to deregulate. Taxis are regulated in all States seemingly to the benefit of producers. Railways are publicly owned: they receive some special protection from road transport in some cases. Air transport much more nearly resembles a producer protection model. There is the complication nevertheless that one of the beneficiaries is the publicly owned TAA, a possibility not contemplated by Stigler.[57] Shipping appears to benefit from its special treatment under the Trade Practices Act 1974 (Cth), as well as from other restrictions.

Regulation of two other important sectors, construction and distribution, also presents a complex picture, though entry controls are of less significance than elsewhere. Entry controls and other elements of regulation in the financial sector are more significant and at present are under review by the Campbell Committee.[57a]

There is much occupational licensing. It is this form of regulation which most neatly fits the Stigler thesis. The professions do not present a simple picture since some are regulated in their own interests and others are unregulated. Many professions are not exempted as such from the Trade Practices Act 1974 (Cth) (although the Act does not reach many unincorporated bodies). The Act does treat price fixing in relation to the supply of services differently from price fixing in relation to the supply of goods. The latter is prohibited outright, whilst in the case of the former the possibility of authorisation exists. In addition, price recommendation schemes in relation to goods or services may also be authorised if more than fifty parties are involved. Authorisation depends, however, on a public benefit test.

This overview suggests some tentative conclusions. First, there is a good deal of industry or sector specific regulation. It works more in the interests of producers than consumers. Secondly, there are many industries not subject to industry specific regulation. At present, Stigler's theory is not sufficiently operational to provide a basis for predicting which industries are regulation-prone. Thirdly, sectoral level regulation varies in intensity in Australia. The reasons for this are worthy of further exploration. Finally, it would be an exaggeration to say that the economy as a whole is best characterised as a regulated one.

57 P. J. Forsyth and R. D. Hocking, *Regulation of Air Transport*. Forthcoming C.E.D.A. paper. Of course, a publicly owned body may not pursue the public interest but a special theory is necessary to cover the interests it is likely to pursue.

57a Committee of Inquiry into the Australian Financial System, *Final Report* (1981), which was completed after this paper was written.

58 J. G. Crawford, *A Commission to Advise on Assistance to Industries* (1973) 12.

VIII. DOES STIGLER'S THEORY APPLY TO FEDERAL GENERAL REGULATORY BODIES?

> But the parties to such conflicts of interest will not always be equally well represented in the argument and discussion which precede final decisions by Government and Parliament: those likely to gain directly from a particular measure, such as a tariff or subsidy, will tend to be more concentrated, organised and articulate, than those likely to lose from the measure. If Parliament is to have regard for the equity of its decisions on assistance to particular industries, and for the longer term implications of these decisions for the community as a whole, it must, I believe, have a source of advice such as the Commission, that can inform it on those matters which particular interests will tend to neglect.[58]

This section of the paper asks whether Stigler's theory, or any capture theory, applies to the major federal regulatory bodies in Australia: the Prices Justification Tribunal (now defunct), the Trade Practices Commission and the Industries Assistance Commission. The Foreign Investment Review Board and the National Companies and Securities Commission are not considered.

Of the three bodies, the section focuses most on the Prices Justification Tribunal which was a regulatory body on most definitions of the term, even though its recommendations were not legally enforceable. In addition, it is worth discussing the suggestion which is sometimes made that the P.J.T. served industry rather than consumer interests. As to the Trade Practices Commission, it is sometimes suggested that trade practices laws merely establish or influence the competitive conditions under which firms operate and are not a form of regulation. It is rare to hear the suggestion that the Trade Practices Act 1974 (Cth) favours industry. Nevertheless the role of the trade practices legislation and institutions is discussed. The section also discusses the Industries Assistance Commission briefly. The position of the I.A.C. seems straightforward: it seems to serve the general interest. The chief complication, that the *system* of industry assistance appears to serve the industry rather than the general interest, has been dealt with earlier. The principal point is, as the quote at the beginning of the section suggests, that the existence of independent bodies seemingly serving or trying to serve general rather than sectional interests is inconsistent with Stigler's theory, at least insofar as it applies to regulation that is not limited to individual industries.

1. Prices Justification

The Prices Justification Act 1973 (Cth) established the P.J.T.[59] as a body whose function was to determine whether prices charged by companies for sales in Australia were justified and, if not justified, what lower prices would have been. Section 18 of the 1973 Act required companies with annual sales in Australia of $20 million (later $30 million) to notify increases in prices and prices of new products in advance to the P.J.T. unless exempted by the P.J.T. Amendments to the Act in 1979 largely abolished that requirement except in limited circumstances, and by 1981,

59 Readers should note that I was a member of the Tribunal from its inception.

only oil refining and marketing companies notified prices (wholesale) of petroleum products. There were no legal sanctions to enforce the public inquiry decisions of the Tribunal, although there was virtually total compliance with its recommendations over the years.

It is difficult to see how a producer protection hypothesis could fit the activities of the Tribunal. There always was, and remained to the end, an industry lobby which wanted the Tribunal to be abolished. There is little dissent from the view that in its early days, when it perceived itself as having an anti-inflationary role, the Tribunal significantly reduced prices compared with what they would otherwise have been.

From the latter part of 1974, when it became apparent both to the then Labor Government and to the Tribunal that this was not a desirable role to play following the change in economic conditions in that year, the Tribunal played a more limited role, concentrating on cases where they may have been abuses of market power. Whose interest did the Tribunal serve? Did it serve the interest of producers?

It is very doubtful that the P.J.T. served producer interests. First, the political analysis which underlines Stigler's theory of regulation does not obviously apply to a body which regulated a large number of diverse industries rather than a single one. Secondly, where regulation serves industry interests, it typically does so by strengthening market power, usually by limiting entry or establishing a cartel. The P.J.T. did not directly or indirectly limit entry to an industry, nor confer statutory monopoly rights. Nor did the P.J.T. establish a cartel in competitive or oligopolistic industries: it set a maximum, not a minimum price. The much paler suggestion that the P.J.T. may on occasion have caused a closer parallelism in prices in some oligopolistic industries is considered below. Thirdly, there is the suggestion that the findings of the P.J.T. at public inquiries that prices were justified, or alternatively its decisions to hold no public inquiry into firms' prices, enabled firms to charge higher prices than otherwise. Since the P.J.T. did not increase the market power of firms, the question must be asked of how P.J.T. actions led to higher prices. In competitive industries, the P.J.T. could not cause a rise in market prices. In monopolistic industries, the suggestion that P.J.T. prices were higher than firms would charge in an unregulated situation requires an explanation of why firms were not charging those higher prices before being regulated, together with empirical evidence. Of the possible explanations, the only one with any kind of potentially logical foundation is the suggestion that customer resistance to price increases was lowered by knowledge that the P.J.T. had not objected to the increase, but there is little evidence of this. Big industrial buyers and retail chains, for instance, did not appear to have relaxed their vigilance nor to have altered their buying procedures, nor to have reduced the numbers of their buying staff on account of the existence of the P.J.T. There is no evidence that P.J.T. decisions were a determinant of "consumer resistance". Consumer resistance is determined principally by such economic factors as competing demands for the consumer's dollar from other goods.[60]

Fourthly, even if in isolated cases the P.J.T. arrived at prices which were higher than they otherwise would have been, it does not follow that on balance the P.J.T. served the interests of industry, since its price lowering effects would probably offset its price increasing effects.

There remains the suggestion that the P.J.T. may have encouraged a closer parallelism of prices on the part of oligopolies. This kind of effect may have occurred during earlier periods (for example, during wartime) when price control was on a product basis and did encourage cartel-like behaviour at times. The argument was less persuasive, however, when prices were generally set on a company by company basis, with different prices being notified by companies and with different prices being then found justified by the Tribunal.[61] The Tribunal did not lay down a formula which firms had to follow in setting prices and it allowed them some flexibility in following their own traditional methods of price-setting, again aiming to lessen forces making for closer parallelism. In any event, the possibility only really arose when there was prior notification of proposed price increases, and this disappeared after 1978, except for the oil industry.

There is also the view expressed by some radicals that the P.J.T. served to uphold the capitalist system by giving respectability to business decisions. Whether a producer or consumer protection hypothesis applies is, however, an unimportant detail in this context.

In short, there is little substance to the suggestion that the P.J.T. was anything other than it seemed to be: a body established to prevent unjustified price rises and to curb possible abuses of market power.

2. *Trade Practices*

It has been said that —

> In due course the Trade Practices Act 1974 may come to be described as the most important piece of business legislation of this century, at least as far as its impact upon business decision-making is concerned.[62]

It is difficult to regard the existence of the Trade Practices Act 1974 (Cth) and its accompanying institutions, the Trade Practices Commission, the Trade Practices Tribunal, and the Federal Court of Australia as consistent with producer protection theories and the political analysis underlying them.

60 In B. Dabscheck, "The P.J.T.: A Perverse Case of Windowdressing" (1977) *The Journal of Industrial Relations* 133, it is claimed that the P.J.T. contained price rises when the economy was on the upswing and increased them when it was on the downswing. The evidence adduced in support of the latter part of this proposition is thin. Reliance is placed very largely on N. R. Norman, *The Prices Justification Tribunal: Stage Two* (1976) 11. Dr Norman's main conclusion is that "the stage-two operations of the P.J.T. tended to exert little downward influence on profitability and activity (except in certain corners of the industry)". Norman points to "two routes through which the P.J.T. might actually have contributed to inflation" but does not suggest that the net effect of the Tribunal in this period was to add to inflation. Dabscheck produces no other empirical evidence. In any case, any finding that the P.J.T. altered the pattern of pricing over the business cycle would not support any claim that on balance it operated in the interests of industry. There is also now some emerging econometric evidence that the P.J.T. contained prices from 1973 to 1976.

61 R.R. Officer, "The Prices Justification Tribunal: Retrospect and Prospect" (1976) 1 *Australian Journal of Management* 57, 67. The Tribunal was taken to task for recommending different prices for an identical product produced by different companies.

62 R. Baxt and M. Brunt, "A Guide to the Trade Practices Act 1974" (1974) 4th Quarter *The Australian Economic Review* 5.

The Trade Practices Act 1974 (Cth) has a double thrust:

(i) to strengthen the competitiveness of private enterprise at the various levels of production and distribution of industrial and consumer goods and services — to the benefit of the public as ultimate consumers and to the benefit of business in general.

(ii) to strengthen the position of consumers relative to producers and distributors — to the benefit of consumers (and ethical traders), and to the benefit of competitive process, since producers and distributors will be activated to compete more on the fundamentals of price and quality.[63]

The Act prohibits certain restrictive trade practices, and misleading, deceptive and other specified conduct. The restrictive trade practices prohibited relate to provisions in agreements or convenants substantially lessening competition including price fixing, monopolisation, resale price maintenance, anti-competitive exclusive dealing, anti-competitive price discrimination, some mergers and primary and secondary boycotts, including some by employees. Some practices can be authorised if an applicant demonstrates to the Commission that the practice satisfies a public benefit test.[64]

The Act prohibits misleading or deceptive conduct in trade or commerce generally, and prohibits specified false representations and other particular unfair conduct relating to the sale of real and personal property and the provision of services. In addition, the contractual rights of consumers are strengthened by the Act implying certain conditions and warranties into contracts for the supply of goods or services to consumers, who may in some circumstances include businessmen. Rights are extended for consumers to rescind contracts or seek damages from sellers where there is a breach of a condition implied by the Act. Further, purchasers of goods of a kind ordinarily acquired for personal, domestic or household use or consumption are given rights of action to seek damages from manufacturers (or importers) of goods in certain circumstances. These rights of the consumer are private rights which he can exercise in local courts.

Are there any respects in which the thrust of the Act has been so weakened as to render it an instrument which serves producer interests or of no effect? The authorisation procedure, and notification procedure in the case of exclusive dealing, involves acceptance of the principle that competition should not be pressed so far as to operate to the public detriment, but the weight which is attached to producer as opposed to consumer interests in determining the public benefit is customarily small. Some concessions to small business, or at least to the small business lobby, have been made in introducing section 49 (which relates to price discrimination) and then retaining it in the light of many recommendations that it should be abolished. The price fixing provisions of the Act treat the suppliers of services more leniently than the suppliers of goods, but only a little more so. Likewise the concessions made to trade association price recommendation schemes are comparatively minor. There is

63 Trade Practices Commission, *Trade Practices Act 1974 As Amended to 6 December 1978* (1979).

64 Notification of exclusive dealing also secures protection from the Act until the Commission decides to the contrary. The Act is, however, too complex to summarise here. For a treatise see B. G. Donald and J. D. Heydon, *Trade Practices Law* (1978) Vol. 1.

the perennial question of whether the Act strikes the right balance between preventing unmeritorious mergers and permitting desirable ones. A similar question concerning balance could be raised about the monopolisation provisions of section 46. Although the somewhat more lenient treatment accorded to so-called Type 2 market power situations (monopolisation, mergers, for example) than to Type 1 market power situations (cartels) may partly be explained by an economic theory of politics, it is only fair to say that there is a much more powerful economic efficiency case for acting against Type 1 than Type 2 forms of market power.

(i) some primary produce marketing arrangements.[65]

A number of exemptions have been written into the Act. These include exemption for conduct that is:

(a) specifically authorised by a Federal or State Act or a Territory Law; or conduct that arises from;
(b) industrial agreements in respect of the remuneration, conditions of employment, hours of work or working conditions of employees;
(c) sale of goodwill;
(d) compliance with standards prepared or approved by the Standards Assocciation of Australia or the Australian Gas Association;
(e) partnership agreements between individuals;
(f) export agreements, particulars of which have been disclosed to the Commission within fourteen days of being made;
(g) consumer boycotts;
(h) certain arrangements relating to the law of patents, copyrights, trade marks or designs;
(i) some primary produce marketing arrangements.[65]

Many of these exemptions are explicable on public interest grounds. Others may be more contentious, such as primary produce marketing arrangements and trade union activities, though in these cases the arguments in defence of the exemptions are the weak bargaining power of workers and primary producers, the fact that there is a conciliation and arbitration system set up under different legislation, and the possible desirability of greater stability in primary producer prices. The exemption of conduct sanctioned by Federal or State laws enables many professional and other cartels to escape the operation of the Act, chiefly by securing protective State legislation. At the Federal level, it seems that restrictive practices at the stock exchange will be examined by the National Companies and Securities Commission rather than the Trade Practices Commission, an outcome which may protect that bastion of private enterprise from the invigorating effects of competition a little longer. The State Government has also bowed to pressure from service station owners and enacted franchising legislation which is seemingly at variance with the general objectives of its trade practices legislation.[66] Another apparent concession to

65 Some of these exemptions only apply to particular classes of conduct, and not to all conduct.

66 This legislation makes it difficult to suggest that regulation serves the interests of big business. The petroleum marketing franchising legislation was opposed to major oil firms. The fact that regulation often serves small business interests rather than big business interests is a frequent theme of Stigler and one does not have to look far for Australian examples — restrictions on new retail developments in established shopping areas; closing hours legislation; occupational licensing.

sectional pressures occurred when the Government made successful submissions on behalf of newsagents to help save their exclusive agency arrangements.

Despite such isolated cases of successful avoidance of the main thrust of the legislation, there can be little doubt that the Trade Practices Act 1974 (Cth), and its associated institutions, has accomplished the opposite of what Stigler's theory would predict. The impact of the Act in promoting competition far outweighs any gains made by sectional groups in recent years in obtaining legislation favourable to their own interests.

3. Industries Assistance Commission

In this section of the paper a distinction is drawn between the system of industry assistance generally, and the role of the Industries Assistance Commission (I.A.C.). The I.A.C., the successor of the Tariff Board (established in 1921) came into being on 1 January 1974. The primary function of the I.A.C. is to advise the Government on the nature and extent of assistance which should be given to industries in Australia. The I.A.C. differs from the T.P.C. which has adjudicatory powers. It also differs from the P.J.T. whose public inquiry determinations, although not legally enforceable, could not be characterised as being merely advisory to the Government.

The I.A.C. was instituted following a report by Sir John Crawford.[67] The reasons for having a Commission were as follows:

> First, it can assist the Government to develop its policies for improving the allocation of resources among industries in Australia. Second, it can, because of its independence, be expected to provide advice on these policies which is disinterested. And third, it can facilitate public scrutiny of these policies.[68]

Crawford stressed the value of the Commission being able to take a co-ordinated view of all forms of assistance available to Australian industry, including the rural sector. As the quote at the beginning of this section shows, he also saw the Commission as a source of disinterested advice in an area of government activity subject to conflicting pressures from special interest groups in the community.

The approach of the Commission to protection is well known. Whatever might be said of the approach of the Tariff Board before the middle of the 1960's, the I.A.C. has repeatedly made it clear that a reduction of levels of assistance which are high is required. Its general stance has been made clear in its annual reports: specific recommendations for lower levels of protection have been made in its reports on individual industries, though a significant number of them have been rejected by governments.

4. General

A consideration of the work of the P.J.T., T.P.C. and I.A.C. leads to the conclusion that general federal regulatory bodies do not serve producer interests. Rather, they are set up as a counter to sectional pressures. The I.A.C. exists in order

67 Note 58 *supra*.
68 *Id.*, 6, 7.

to provide disinterested advice to the Government. The T.P.C. and P.J.T. are given power to make important decisions. The aim of establishing them is not merely to delegate power which a busy Parliament does not have time to administer. If that were the object, the power could be delegated to Ministers, aided by their departments. The real reason for having bodies of this kind is to make them as immune as possible from sectional and political pressures. This aim is largely fulfilled. It is one way in which legislatures respond to avoid the kinds of difficulties which Stigler sees as inherent in regulation.

It may be contended that the T.P.C. especially, and even the I.A.C., are not regulatory bodies and that it is therefore inappropriate to use them to rebut Stigler's theory. It is perhaps less productive to consider the definition of regulation than to determine whether Stigler's general theory of legislation (and economic theories of politics on which it is based) is partially weakened by evidence of the existence of general regulatory bodies working for public rather than sectional interests.

This section of the paper also provides a small amount of evidence relevant to a more general proposition, namely that where regulation extends across the range of industries, it does not generally work principally in the interest of the regulated, whatever else it does or does not do. As has been noted, there is little reason on the basis of Stigler's political analysis to expect that general regulation should work in the producer interest. Even cursory observation indicates that, for the most part, environmental, occupational safety and health, consumer protection and such other newer forms of regulation, have not worked in the interests (at least in the immediate narrow sense) of industry, and they have certainly not been welcome, save in the case where the regulation serves to protect industry from overseas competition, as it sometimes does in laying down safety and other standards which it is difficult for overseas producers to meet. There is some evidence though that in some cases the impact of the new legislation has been slight, for example, environment protection laws.

IX. THE LABOUR MARKET

> The new province is that of the relations between exployers and employees. Is it possible for a civilised community so to regulate these relations as to make the bounds of the industrial chaos narrower, to add new territory to the domain of order and law? . . . the might of the State is to enforce peace between industrial combatants as well as between other combatants; and all in the interest of the public.[69]

Stigler's theory was designed to apply to product markets. Having regard to the fact that there are two major conflicting interests in labour markets, those of employers and unions, it is not so apparent that Stigler's theory might apply in the industrial relations area. Yet in Australia it may well. There is, at any rate, an uncanny resemblance between labour market institutional arrangements and the outcome which Stigler's theory would predict for industry regulation.

69 H. B. Higgins, *A New Province For Law and Order* (1968) 1, 2.

An examination of the historical background to the establishment of the Australian system of arbitration lends considerable support to the thesis. In the 1890's the emerging general union movement was crushed in a series of strikes. Defeated in its attempts to set up a private cartel, the labour movement realised that it could achieve this aim more effectively through the political process. It was aided by middle class radicals. Employers opposed the proposed system but later sought to use it to their advantage as much as possible, particularly by attempting to secure enforcement of awards.

The trade union movement did not achieve all of its aims initially. Some regulatory costs were imposed and it was only much later in the 1960's, with full employment and enhanced bargaining power, that an important cost — penal sanctions — was effectively removed.

The arbitration system sets a minimum price for labour and thereby operates a cartel. It does not set a maximum price, as a public interest-minded regulator might. The system gives trade unions the advantage of a choice between arbitration and collective bargaining. At any one time some stronger unions tend to prefer bargaining, while weaker unions seek matching increases through the Commission on the basis of comparative wage justice considerations. Over the course of time, unions also have the choice of whether to rely primarily on arbitration for wage increases, as they do during recessions when their bargaining power is weak. During periods of full employment, the majority rely more on collective bargaining.

Besides this cartel creating effect (Type 1 market power), the system also confers, or strengthens, monopoly power (Type 2 market power) on trade unions through a number of routes such as the registration provisions, preference to unionist clauses (where they exist) and so on.

The system has imposed costs on the trade unions but they do not seem to outweigh the benefits. The costs formerly included bans clauses. They still include the cost (non-economic) of some regulation of their internal affairs but this is fairly slight and benefits unions in some respects.

There is not the space to examine in detail[70] the applicability of Stigler's thesis here, nor the complications: whether employers gain or lose; whether the system has had a narcotic effect on unions over the years and weakened their bargaining power; what would have happened in the last eighty years in the absence of arbitration; and whether, even if the system is tilted in favour of unions, it still brings about a more orderly system of wage determination than otherwise, thereby serving both public and trade union interests. Nevertheless, it is hard to think of a substantial area of the economy which Stigler's theory better approximates.

70 I am presently engaged in an exercise along these lines.

71 M. Friedman and R. Friedman, *Free To Choose* (1980).

X. CONCLUSIONS

Government intervention in the marketplace is subject to laws of its own, not legislated laws, but scientific laws.[71]

The major hypotheses about the effects of regulation — *consumer protection, perversion, no effect,* and *producer protection* — all have sufficient shortcomings to conclude that if there are laws of regulation they have not yet been discovered. In particular, the quest for a simple general theory of regulation which captures the complex forces at work in business regulation looks unpromising. Nevertheless, Stigler's attempt to develop a theoretical underpinning for a producer protection theory of regulation contains a rudimentary analysis of the conditions under which regulation is sought and granted. There are, however, serious theoretical deficiencies with his pioneering contribution, including its breakdown when regulation takes forms other than the conferring of concentrated benefits and the imposing of diffused costs. It is not helpful in explaining the recent growth of regulation, nor very relevant. Even so, it may be that with more case studies of regulation, it will be possible to make fruitful generalisations about the demand for, and supply of, regulation.

The theory of economic regulation is not at present sufficiently well developed to predict which Australian industries are likely to be prone to industry specific regulation, although a development of theory to enable this to occur cannot be ruled out. Once there is industry specific regulation it is possible to identify a number of instances where it seems to operate more in the interests of producers rather than consumers. Even so, there are a sufficiently large number of counter-examples (for example, those cited in the concentrated cost diffused benefit category) for Stigler's theory to lack predictive value and for it to be little more than a warning about industry specific regulation. Moreover, even where the thrust of the regulation seems to be biased against consumer interests, there always seem to be significant complications: the lawyers' failure to control entry; the conflicting pulls of regulation of the liquor industry; the tendency for third parties (including governments) to appropriate the benefits of regulation; and so on. The existence, or recent existence, of federal regulatory bodies like the Prices Justification Tribunal, the Trade Practices Commission and the Industries Assistance Commission seems inconsistent with Stigler's theory. They provide evidence relevant to the proposition that general forms of business regulatory legislation appear not to work in the interests of producers, whatever else they do. The effect of section 92 of the Constitution provides some evidence for the view that constitutional rules do not work in sectional interests. Stigler's theory may be most relevant of all to the labour market, but this requires further analysis.

Caution about policy conclusions is warranted. While industry specific regulation needs to be viewed with caution, it should be remembered that there are examples of industry specific regulation that do not principally serve producer interests. They include regulation of cigarette advertising, drink-driving laws and food and drug safety laws. On the other hand, while general regulation (and constitutional rules) are less likely to be subverted by sectional interests, they are only desirable if they

pass the social cost/benefit test. Moreover, additional problems are involved in deregulation: these have barely been faced by theories of regulation.

Even momentary consideration of policy conclusions highlights a basic problem with theories of regulation. The term "regulation" is an unsuitable basic unit for analysis, and for policy conclusions. It is too general for the purposes of economic analysis. The effects of entry-barring regulation are different from those of state promoted cartels and from those of pollution preventing rules. A more disaggregated analysis is required. On the other hand, regulation is too narrow a category for the analysis of the political economy of government-business relations. For the purposes of political economy, the full range of government policies affecting business must be considered rather than regulation in isolation. It is for this reason, above all perhaps, that a satisfactory general theory of regulation is unlikely ever to emerge.