REGULATORY REFORM

REGULATION at 40

The last four decades have seen landmark liberalization of U.S. regulatory policy, yet many promising reform ideas now languish and policymakers have backslid in some cases.

BY PETER VAN DOREN AND THOMAS A. FIREY

Regulation debuted in 1977, just as the U.S. government began easing some of its heavy controls over markets that had been in place for decades. The previous year, Congress passed the Railroad Revitalization and Regulatory Reform Act, an initial, modest step toward railroad pricing deregulation. The year this magazine launched, Sen. Edward Kennedy opened Senate Judiciary Committee hearings on motor carrier regulation, which would lead to major deregulation of that industry. The following year, Kennedy contributed to the landmark Airline Deregulation Act.

Further reforms followed: the Staggers Rail Act and Motor Carrier Act in 1980; the AT&T consent decree, Garn-St. Germain Depository Institutions Act, and Bus Regulatory Reform Act in 1982; the Ocean Carriers Act in 1984. Later years would bring major liberalizations in energy, banking and finance, insurance, health care, and telecommunications.

Many of the academics and policymakers who led those reforms used this magazine to share their ideas and research with each other, the media, and the public. The list of contributors to *Regulation* during this period is remarkable: Alfred Kahn, James Miller III, Antonin Scalia, Murray Weidenbaum, Robert Crandall, Charles Schultze, Bill Niskanen, Walter Oi, Robert Bork, Bruce Yandle, Richard Gordon, Peter Schuck, Gregg Easterbrook, Laurence Lasagna, Christopher DeMuth, Richard Epstein, Joseph Kalt, Kenneth Arrow, Paul Joskow, Robert Litan, Kip Viscusi, Thomas Gale Moore, Ronald Coase, George Stigler, and many other extraordinary scholars.

The policies that resulted from their work have led to lower prices, greater product diversity, and more market competition, to the benefit of American consumers. Most policymakers and politicians recognize the success of these deregulations. There is no movement to reinstitute the Civil Aeronautics Board or repeal branch banking. Even in the darkest days of last decade's financial crisis, calls for restoring the repealed sections of the Glass-Steagall Act gained little traction.

Yet there is also little interest among many politicians and policymakers in future major liberalizations of the U.S. econ-omy (hazy Trump administration vows to repeal 75% of federal regulations and congressional efforts to reverse specific new rules notwithstanding), even in areas where analysts broadly agree the benefits would be exceptionally large. Beyond that, much of the public mistakenly believes that the deregulation era of the late 20th century benefited established corpora-tions by repealing environmental and consumer protections. Economists, in contrast, believe that deregulation, through the removal of government-instituted market protections for those corporations, forced them to compete more vigorously.

On this, *Regulation's* 40th anniversary, we provide this overview of American regulation and its reform, and offer some thoughts on how further liberalizations could be achieved.

THE RISE OF FEDERAL REGULATION

The common view of regulation in the United States is that, for its first century or so, the country embraced laissez faire; there was little government intervention in the private decisions of the free market. This is not quite true; state governments were active regulators in some sectors, especially banking. However, it is generally correct to say that *federal* regulation was limited until the years following the Civil War, and it expanded greatly during and after the New Deal.

Policymakers typically justify these interventions as necessary to combat "market failures"—situations where, in their judgment, market interactions do not produce acceptably "efficient" outcomes. These failure include market power (a buyer or seller, or a collection of buyers or sellers, dominates a market and manipulates supply and prices; examples include monopolies and cartels), negative externalities (situations where some costs of a transaction are involuntarily borne by nonparticipants in the transaction; an example is pollution), information failures (one party in a transaction has an informational advantage over other parties that distorts the market), and public goods problems (a supplier is unable to exclude nonpayers, resulting in some consumers "free riding" on the payments of others and the good being under-provided as a result; examples include some aspects of fire and police services and national defense). Each of these cases results in fewer transactions than would occur in a market without such failures, which means inefficiency and a loss of welfare.

A number of federal regulations and related domestic policies early in the post–Civil War era involved railroads. Policymakers believed that the threat of future competition on specific routes would discourage railroading firms from making expensive capital investments necessary to serve less populated areas. They also worried that railroads would not be able to assemble sufficient rights-of-way for their rail networks. To help with the latter problem, lawmakers extended federal and state eminent domain powers to secure those land rights for the railroads' use. Later, policymakers adopted rate regulation to prevent railroads from abusing their market power over specific low-density routes and also required federal approval for railroads to abandon lines in these areas that they no longer wanted to operate.

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The subsequent decades saw similar government interventions in other industries involving maturing technologies, including telephone, energy, broadcasting, trucking, and passenger aviation, as well as general efforts to combat market power (i.e., "trust-busting"). The New Deal era featured expanded federal involvement in labor markets and banking and finance. Finally, the late 1960s and early 1970s saw further federal interventions in retail prices, labor, and highway safety, and a broad push into health, safety, and environmental regulation.

THE ACADEMIC PUSH FOR DEREGULATION

In the mid-20th century, as policymakers continued to expand federal regulation, economists and legal scholars on university campuses and in Washington began to question the traditional "market failure" justifications for these policies as well as the assumption that government intervention altruistically benefits public welfare. Two developments propelled this movement: advancing computer technology and the increased availability of social science data allowed researchers to test claims about market failure and the results of government intervention, and public choice theory and the broader law & economics movement challenged traditional assumptions about policymakers' motivations.

A new, economic theory of regulation emerged that posits that these policies are commodities supplied by policymakers who redistribute benefits from some consumers and suppliers to others in an effort to increase policymakers' political support. Unlike the traditional "public interest" theory of regulation that holds that policymakers are altruistic actors who reliably improve public welfare, the economic theory posits that policies are crafted to increase elected policymakers' political support, and bureaucratic policymakers' agency budgets, job security, and prestige. This self-interested behavior is not the result of policymaker malevolence but of the incentives they face; those who behave in this manner tend to retain and expand their authority. They are inclined to continue regulating and adopting other domestic policy interventions until they can achieve no further net political gains.

With this arguably cynical view of government intervention in mind, policy researchers reappraised the landmark regulations of the previous decades. Their findings were disillusioning.

Railroads / The regulation of railroads ultimately increased the prices for shipping manufactured products and redirected the resulting revenue to subsidizing bulk commodity and agricultural shipments. That made Midwestern farmers and miners happy and protected railroads financially (at least for a time), but it harmed welfare overall by distorting the cost of manufactured goods, reducing consumers' access to them. Because the beneficiaries recognized their gain while the general public was largely oblivious to their losses under the regulations, policymakers were rewarded on net for this intervention.

In addition, freight on high-density, long-haul routes between cities was priced above cost, with the revenue used to subsidize short-haul, low-density rural routes. Again, this made some special interests happy, but hurt welfare overall because the higher cost of transporting goods between urban centers distorted markets.

This arrangement was threatened by the rise of trucking in the Depression era. Policymakers responded not by deregulating railroads, but by placing similar regulations on trucking in 1935, creating another network of cross subsidies. Again, these policymakers were rewarded by the beneficiaries, while the costs were largely hidden from the public.

Airlines / Airline regulation similarly created a fare structure that de facto taxed high-density, long-haul routes in order to subsidize low-density, short-haul routes valued by special interests. Regulators justified this by claiming it was necessary to provide safe, necessary air travel. But research on the intrastate air travel markets in Texas and California—which were large enough to be well developed but escaped federal regulation because they didn't cross state lines—revealed much lower fares and efficient operation without sacrificing flyer safety.

In the national market, in contrast, flights were much more expensive per passenger mile. But those higher fares provided little benefit to the airlines because they spent much of the resulting revenue on non-price competition in service: free drinks, roomy flights, helpful (and attractive) flight attendants, etc.

Telephone / Telephone rate regulation restricted entry and created cross subsidies from long distance to local service.

Before the development of microwave communications, long-distance service was provided over costly coaxial cable. As a result, that service was predominantly used by wealthier callers who paid rates far above marginal costs, providing revenue for the cross-subsidies. But as microwave service expanded and middle-class households became more mobile, both the cost and "progressive" justification for cross subsidies grew increasingly untenable because of competitive entry into long-distance services. By 1981, interstate calls were 8% of total minutes, but were paying 27% of local phone costs. These distorted rates attracted competitors who, when blocked by regulations and AT&T, ultimately forced the Justice Department to bring an antitrust suit that ended the regulated AT&T/Bell System monopoly.

Electricity / The evolution of the power industry in the first half of the 20th century resulted in monopoly providers with large generating facilities servicing small regions. Policymakers adopted rate regulation of these natural monopolies with the justification that it would reduce electricity rates and increase consumer access and consumption relative to laissez faire.

Yet research found that rate regulation of power companies had not lowered rates. Instead, it had biased the power industry toward increasing generation to meet underpriced peak demand, making the system prone to excessive capital costs. Utilities overbuilt their power plants—especially nuclear-powered facilities—and passed the cost onto consumers, with regulators' approval.

Banking / Historically, banking regulation in the United States benefited government by providing it revenue, and benefited banks by protecting them from competition. In early U.S. history, states awarded banks market power over small geographic areas in exchange for assessing them heavy taxes and fees, which the banks then passed onto their customers. States prohibited nationwide banking and severely limited statewide "branch" banking, even though branching and interstate banking would have been a great convenience to depositors and a boon to business and borrowers. Also, they would have protected banks from regional bank collapses like the ones that occurred in the years prior to the Great Depression and the early years of the Depression itself.

Depression-era banking regulation (mandatory government-managed deposit insurance and the separation of commercial from investment banking) combated those collapses, but the policies mainly helped firms instead of consumers by shifting bank risk onto taxpayers. The landmark 1933 Banking Act was a classic logrolling compromise in which populist supporters of small, rural banks won federal deposit insurance (over the objections of President Franklin Roosevelt, the Treasury, the Fed, and the American Bankers Association) in exchange for limiting the investment banking activities of commercial banks, which were at the time construed as the great villains of the Depression. The legacy of banking regulation has been an immensely fragmented banking system whose costs are excessive.

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Health and safety / People commonly believe that the wave of federal health and safety regulations that began in the 1970s has made American workers safer. Prima facie support for this is given by accident data; since the 1970s, industrial accidents of all kinds have declined. But that support erodes as the scope of the data is broadened: accident rates declined for decades ahead of the 1970s regulations. There was no further downward shift in accident rates following the creation of agencies like the Occupational Safety and Health Administration.

The long duration of steadily falling accident rates indicates that "secular forces," not regulation, have been the most important contributor to safety improvements over the past century. Safety is a normal good, and as people's real income rises, they will consume more of it. So as American living standards rose in the 20th century, workers demanded safer workplaces, insisting on higher pay in return for taking risk. Employers responded by supplying more safety.

This underscored another revelation of researchers studying market failures: the marketplace appears to be far less vulnerable to failure than what policymakers had assumed. The existence of a health risk, for instance, does not necessarily imply the need for regulatory action. Through normal market forces, either workers receive wage compensation sufficient to make them willing to bear the risk, or employers reduce risk in order to reduce the wage premium. As a result, the health risk is internalized into the market decision.

Environment / Many people don't know that in the spring of 1970 the California State Senate, citing environmental concerns, voted to ban the internal combustion engine by 1975. This utopian idea, which received seemingly improbable support from the United Auto Workers—ultimately did not come to fruition because of its impracticality, though some Golden State policymakers still support the idea.

The federal Clean Air Act reflects the same utopian thinking. For conventional pollutants, the U.S. Environmental Protection Agency must prepare a document every five years that "accurately reflects the latest scientific knowledge" on the health effects of exposure. It must then set a standard that is "requisite to protect the public health…, allowing an adequate margin of safety" to ensure "an absence of adverse effect on the health of a statistically related sample of persons in sensitive groups." The Supreme Court ruled in 2001 in *Whitman v. American Trucking Association* that the Clean Air Act "unambiguously bars costs considerations from the [pollution limits]-setting process." Thus, EPA decisions on conventional pollutants are all about the benefits of emission reduction as ascertained by science—whatever the costs, even if they far dwarf the benefits—because that is exactly what the law instructs the EPA to do.

The Clean Air Act has not been amended since 1990. In the absence of statutory change, the utopian "costs-don't-matter" air quality standards will continue to be a serious issue.

POLICYMAKERS EMBRACE DEREGULATION (SOMETIMES)

According to the economic theory of regulation, policy change occurs as a result of policymakers' incentives. Research demonstrating that specific markets function well without regulation and that existing regulation harms public welfare is not, by itself, sufficient incentive for deregulation. The latter part of the 20th century provided more effective incentives for policy change—in some cases.

Beginning in the 1960s (if not earlier), the United States faced reinvigorated economic competition from countries that had rebuilt their industrial capabilities following the devastation of World War II. At the same time, the U.S. economy was struggling under growing fiscal burdens from the Great Society programs and the Vietnam War, as well as rising inflation from Federal Reserve efforts to stimulate the economy. Those struggles contributed to the "Stagflation" of the late 1960s and 1970s as bouts of high unemployment and double-digit inflation provoked political demands for policy change that would improve economic efficiency.

Initial moves toward liberalizing some markets were made as early as the John F. Kennedy administration and later in the Gerald Ford administration. But the deregulation movement really took off in the latter half of the 1970s. As noted earlier, Sen. Ted Kennedy, with the help of committee counsel Stephen Breyer, seized upon economic research indicating that deregulating certain parts of the transportation sector would lower prices without sparking the grim consequences that regulators had long predicted. For lawmakers who were contending with Stagflation, the opportunity to lower prices and spur the economy by simply reducing government intervention was appealing.

As the U.S. economy recovered and expanded in the 1980s and 1990s, the economic demand for deregulation seemingly would have waned. Yet major liberalizations and other domestic policy reforms continued: the Base Realignment and Closure Act of 1990 (which technically was defense policy but really targeted domestic spending on labor and land), National Energy Policy Act in 1992, Federal Agriculture Improvement and Reform Act of 1996, and Gramm-Leach-Bliley financial reform in 1999. Some of those initiatives were motivated by fiscal pressures; both Presidents George H.W. Bush and Bill Clinton worried about the budget deficit and saw market liberalization as a way to cut government spending and even generate new revenue. The development of information technologies in this period may have contributed to further deregulation as long-established industries—banking, broadcasting, retailing, telecommunications—found novel ways to employ the new innovations.

The economic benefits from these deregulations were profound. Not only did they reduce prices and improve offerings in their specific sectors, but they contributed to major economy-wide innovations such as just-in-time delivery systems and online commerce.

THE 21ST CENTURY

The momentum for market liberalization reversed in the new century. No policy change in the last 16 years would seem to qualify as a major deregulation, while such initiatives as the 2001 USA PATRIOT Act, 2002 Sarbanes-Oxley corporate governance act, 2002 and subsequent farm bills, 2005 Energy Policy Act, 2010 Patient Protection and Affordable Care Act, 2010 Dodd-Frank financial regulation act, and 2015 Federal Communications Commission "net neutrality" regulations have expanded federal intervention in markets and added tens of thousands of pages to the U.S. Code of Federal Regulations.

Like the preceding deregulatory period, this new era can be attributed in part to external developments—that is, major news-making events. The 2001 al Qaeda terrorist attacks on New York and Washington and the accounting scandals of 2001–2002 motivated the PATRIOT Act and Sarbanes-Oxley, respectively, while the financial crisis of 2007–2008 and ensuing recession propelled Dodd-Frank.

This loss of deregulatory momentum is unfortunate as there are many public benefits to be gained from further liberalization—as regularly documented in the pages of *Regulation*. Some of these forgone benefits have gained public and political attention in recent years—examples include land-use (e.g., relaxing zoning and building restrictions), health care (e.g., easing drug-approval requirements), and occupational licensing (e.g., ending or reducing training and license requirements)—yet reform continues to come slowly if at all.

TOWARD FUTURE REFORM

Can additional liberalizations be achieved in the near future? Reformers have suggested three strategies to spark further deregulation: electoral reform, process reform, and education. We consider each of them below.

Electoral reform? / Many deregulation advocates have argued that further reform can be achieved only through the political system: elect more pro–free market policymakers to Washington and state capitals.

The new, Republican-controlled Congress and Trump administration appear to exemplify this approach. Candidate Trump's platform included the bold vow to roll back "75%" of federal regulations, and deregulation has been a standard Republican campaign promise for decades. President Trump has already ordered that the issuance of any new federal regulation be accompanied by the repeal of two regulations, and that the cost of complying with federal regulations be frozen for the next year so that the incremental cost of new regulations be offset by regulatory cost reductions elsewhere. Meanwhile, Republicans in Congress have begun using the seldom-triggered Congressional Review Act (CRA) to overturn regulations issued in the final months of the Obama administration. (See "Obama's Record-Setting Midnight," p. 5.)

But beyond CRA actions, it's unclear what concrete steps the new administration and congressional lawmakers will take—or even what it means to repeal "75% of federal regulation" or two old regulations for one new one. Though many good regulatory reform ideas have been suggested by D.C. think tanks, university-based policy researchers, and Capitol Hill committee staffers, none have yet been publicly embraced as major initiatives of Congress or the Trump White House, unlike the reforms of the 1970s–1990s. It's fair to wonder whether the politicians' vows of deregulation are more atmospherics than actual policy goals.

Besides, it's uncertain whether they would have true electoral backing for bold action. Voters may say they support "deregulation," but their voting behavior suggests that they really are disinterested in regulation or they accept the old public interest hypothesis that government regulators invariably benefit the public. Moreover, they often *reward* politicians for tilting the marketplace in certain special interests' advantage.

In too many cases, if a member of Congress were to disdain regulation and other economic favors across the board, she would likely succeed only in depriving special interests in her district of benefits from "gaming" the marketplace, and from "logrolling" opportunities to secure congressional colleagues' support for policies important to her constituents. As a result, her constituents would bear heavier regulatory burdens and pay higher taxes and prices, while lawmakers in other districts bestow on their constituents the benefits of government programs and logrolling agreements.

Any lawmaker who wants to be reelected (which is practically all of them) realizes that a principled stand against economic favoritism will cost her votes and financial support necessary for reelection. A legislator who promises to vote against economic favors and then does so cannot count on reelection unless her constituents are somehow obligated to reelect her if she sticks to that promise. Reform-minded legislators are trapped in a "prisoner's dilemma" game: they are safe only as long as they stick together and hold an unchallenged majority position in the legislature. But if that majority breaks, the benefits go to the defectors while non-defectors will be punished. This realization sours many reform-minded politicians.

Some electoral reformers have suggested term-limiting officeholders to disrupt this game by reducing the pressures of reelection. But as long as a lawmaker has the opportunity to be reelected even once, or move on to another elected office, there will be temptation to abandon the pledge and pursue special interest support. Moreover, constituents who impose term limits on their elected officials put themselves at a disadvantage to neighboring districts that do not adopt limits. Again, these constituents would deprive themselves of economic favors but would still pay the taxes and higher prices that fund government favors that will flow elsewhere.

What if term limits were imposed constitutionally over an entire legislature? That would not eliminate the underlying problem of constituent self-interest. Instead of re-nominating the same politicians for reelection, party organizations would find candidates who would strive faithfully to continue delivering the economic favors pursued by their departing predecessors. Specific lawmakers might change, but the political and economic games would continue.

Process reform? / Members of Congress *do* understand that economic favoritism is a prisoner's dilemma game. And when the stakes have been high enough, they have found ways to cooperate to avoid the costs. One example that is often propounded as a model for broad process reform is the Base Realignment and Closure (BRAC) system.

Following the end of the Cold War, there was broad recognition that the United States had a large and costly surplus of domestic military installations in light of the nation's new defense needs. But it was politically difficult to close those bases because local congressmen would block legislation that jeopardized their districts. In essence, national defense had become a jobs program for civilian base employees and contractors, with little benefit and considerable cost to the broader American public.

To end this stalemate, Congress largely took base-closure decisions out of lawmakers' hands. Under 1990 legislation, they delegated to a base-closure commission the politically difficult task of identifying military facilities that could be closed at little risk to military preparedness. Dozens of installations were subsequently closed as a result of four successive BRAC rounds.

The apparent success of the BRAC process depended on two ingenious provisions of the authorizing statute. First, the base closure commission's lists of facilities to be shuttered had to be accepted or rejected *in toto* by the White House and Congress; there was no opportunity for individual lawmakers to save "their" bases. The bad medicine had to be swallowed whole or not swallowed at all, in public view. Second, Congress could reject the full list of proposed base closures only if it passed a resolution of disapproval within 45 days of the White House's having approved the list. Because the BRAC commission strategically compiled and forwarded small lists of unnecessary bases, only a small minority of congressional districts would oppose each BRAC round, while the rest of Congress and the White House stood to benefit from the savings. As a result, Congress never rejected a BRAC list.

Unfortunately, the BRAC process does not appear to be adaptable to many other congressional deliberations, including regulation. In fact, it may be a one-of-a-kind success. There have been other attempts at such independent commissions, but Congress has never given any of them the power that it gave the BRAC commission. Under most circumstances, Congress will not cede such power because to do so would eliminate the stuff of congressional life: logrolling.

And even BRAC hasn't been as successful as the above narrative suggests. Though Congress has never rejected a BRAC list, it also hasn't considered many lists. The system fell apart after the 1995 list because commission members wanted to turn their attention to the many bases in electoral vote–rich Texas and California. Clinton may have been a budget hawk who approved the 1995 closure list, but he didn't want to jeopardize his reelection chances in those states. As a result, he invented ways to block his having to consider a subsequent list. Since then, Washington lawmakers have similarly avoided compiling lists that would significantly affect California and Texas, resulting in only one additional BRAC round, in 2005. Beyond that, advocates of keeping bases open began to shift their lobbying efforts from lawmakers to BRAC committee members, in essence reinstituting the game.

If economic favoritism can't be averted, perhaps Congress could at least find a less costly way of distributing largesse to its intended beneficiaries. For instance, instead of regulating markets, government could give direct subsidies to the special interests currently favored by regulation, but in return economists would design the subsidies in a way that reduced the market distortions caused by regulation.

The 1996 farm bill, titled the Federal Agricultural Improvement and Reform Act, tried to do this for the market-distorting system of price supports and acreage controls that had augmented farmers' incomes for 60 years. The act replaced price supports and acreage controls with direct subsidies, to be distributed on a fixed, five-year schedule. Farmers would get their money, but market forces would decide how much food was produced and at what price—a considerable improvement over previous policy.

Farmers were happy with the new program in 1996 and 1997 because then-high farm product prices meant the new subsidies were larger than the price support payments they would have received under the old system. But when farm prices plummeted in 1998 and 1999, Congress reneged on the payment schedule and gave farmers about $6 billion in additional subsidies—evidence, if any were needed, that lawmakers cannot make long-term commitments to stop rewarding special interests out of taxpayers' wallets.

Analysts can provide intellectual ammunition and "how-to" for the executive in this regard, but their analysis does not drive the policymaking process. They can only wait and hope for promising opportunities to deregulate.

The good news, in this case, is that Congress gave farmers their extra $6 billion as a lump-sum payment rather than revive price supports. The bad news is that, since then, Congress further reneged and reinstituted agriculture subsidies that once again distort farmers' crop-planting decisions.

A final process reform favored by many analysts is the creation of an independent agency staffed by economists that would issue reports about the costs and benefits of economic regulation. The thinking is that such analysis, currently performed mostly by think tanks and academics, might have more clout if it were an official independent part of the political process. Supposedly, policymakers would read these reports and voters would read of them in the press, and they would sour on government intervening in the market.

As policy analysts, we are sympathetic to this idea. We are also skeptical of its potential for success. History indicates that such efforts, by themselves, have little effect on policymakers and the public.

For instance, in the early 1960s the Kennedy administration installed innovative Ford Motor Company president Robert McNamara and RAND economist Alain C. Enthoven, along with McNamara's cadre of Ford "Whiz Kids"—young management sciences experts and quantitative analysts—in the Pentagon. They institutionalized the role of economic analysis in the Defense Department as a clever way to say "no" to the demands of the services for more bases and equipment. But this effort was effective only as long as it had White House support. The Systems Analysis Office was never more powerful than when Enthoven ran it in the 1960s. But when Richard Nixon became president and installed Melvin Laird as secretary of defense, the balance of power in program selection shifted back to the services. Never again would analysts dominate the services because no subsequent president has wanted it that way. Iconoclastic analysis of the sort provided by the Whiz Kids is effective only if the party in power wants it to be effective.

As *Regulation* has chronicled, similar efforts have been tried in both Washington and state capitals in recent decades. "Sunset" provisions on regulations, mandatory cost–benefit analysis, and other forms of regulatory review seem to have little effect on regulation—unless they have strong support from the president or governor. Yet even in those cases, it's not really the analysis that drives deregulation; it's the will of the chief executive. Analysts can provide intellectual ammunition and "how-to" for the executive in this regard, but their analysis does not drive the policymaking process. They can only wait and hope for promising opportunities to deregulate, like those that brought about the liberalizations of the late 20th century.

Is education the only hope? / The education of future policymakers may lead to more rational regulation, if not less regulation. The legal profession supplies the judges who interpret laws and regulations, as well as a healthy fraction of legislators, regulators, and their staffs. As a result of the rise of the law & economics movement at the University of Chicago, the tenured faculties of all elite law schools now include economists. One cannot graduate from a top law school without having some training in how markets work, how robust their efficiency characteristics are, and how efforts to regulate them often have perverse results.

But the last, best hope for deregulation rests with future generations of voters. They get the legislators and laws they demand. It is easy for voters to demand regulation—or to acquiesce in it—because most voters do not understand its effects: higher prices, higher taxes, and less freedom. Today's students are tomorrow's voters, and we must nurture such understanding in them. The more that students are exposed to knowledge about the benefits of free markets and the costs of regulation, and the more they see these lessons play out in their daily lives (e.g., Uber, Airbnb, food trucks, microbrewing and microdistilling), the less likely they will be to vote for politicians who favor government intervention in markets—or at least so we hope.

To be sure, such an educational effort conflicts with the public interest view of government and markets that has been popular on college campuses and in the public for at least 100 years. Many believe this view cannot be reversed. But what other strategy offers more promise?

If a majority of citizens believes that it is both good and unproblematic to demand economic favors from government, then politicians will accommodate those demands. There are no institutional magic bullets that can stop them.

CONCLUSION

The public interest theory of regulation asserts that markets often do not work well. That is, markets supposedly are not efficient and consumers do not get a fair shake. Under this theory, regulatory intervention in markets by government, if intelligently designed, can make markets more efficient and fair.

Yet when researchers began investigating real-world regulations to measure these benefits, they were disillusioned. Few public benefits were found, but there were plenty of special interest benefits as well as gains for the policymakers—and plenty of deadweight loss. More encouraging, the researchers discovered that most regulated markets did not have market failures in the first place, and thus would be more efficient if regulations were removed. And for those markets that do have failures, regulation often has not improved efficiency.

Instead of benefiting the public, regulatory intervention usually redistributes from some firms to others and from some consumers to others, and imposes net costs in the process. Given the many economic challenges the United States faces in the 21st century, these redistributions will increasingly weigh on public welfare. *R*

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