

THE ECONOMICS OF REGULATION

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Einstein to Roosevelt: "It is very perplexing. Relativity is so simple by comparison!"

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Preface

I won't give much history. Who cares what US telecom policy was between 1970 and 1980? A leading text spends xxx on that.

I won't cover ideas I don't think are valid, such as the Averch Johnson effect.

I'll try to be interesting.

I'll try to be short.

I really should cover health, education, and social security. Traditionally, regulation was put in IO, which covered antitrust policy, regulated industries, and "social regulation"—consumer protection and pollution. Labor regulation, health, education, banking, morals—indeed, most regulation—was ignored. Antitrust, in particular, gets way too much attention: One book spends xxx, another yyy pages on it. Antitrust is good for learning price theory and understanding markets, though, so it retains two chapters here.

Public finance courses took up the slack, or topical courses like labor economics or money and banking, for which these were fringe topics. I think they belong in a regulation course. Here, we should cover the sources of market failure and the restrictions governments put on our behavior to remedy them. Public finance is best allocated the task of how to raise and spend government revenue, with some overlap on the issues of taxation for incentivization instead of revenue and which goods should be public and which private.

Many of my students also take money and banking, and they do get some overlap. I am told it is useful to look at it from the micro point of view too, however.

I realize how useful business school training is for understanding government regulation. From finance: present discounted value, CAPM, market efficiency. From accounting: depreciation, assets and liabilities. From business law: corporations and torts. I write as if the student hasn't heard of any of these things, but it helps to have seen them before.

At the start of every chapter I have put a quotation and a picture. My aim is to teach something as well as provide visual relief from the pages of normal text. Do not think that I agree with all the quotations! In many undergraduate courses, instructors have given up trying to make students think, and just present facts to memorize and step-by-step ways to solve problems. I used to look down on that style of teaching. Now, I realize that

it is probably the best way to teach most undergraduates, because trying to make you think often just leaves you confused and upset without knowing anything more than when you started. After some time, I realized that many of you, when you say, "I am trying to think of the answer" mean "I am trying to remember the answer," not "I am trying to figure out the answer using the power of human reason." My current view is that a combination of approaches is best. Teach some materials by rote, so every student can get something out of the class if he is diligent. Teach some materials indirectly, so the student who is accustomed to multi-step analytic reasoning or less systematic synthetic intuition can puzzle out the subtle ideas. Thus, the picture for chapter 5, on monopoly, is a mail truck. Think about why that picture is there and you will be better able to answer test questions for chapter 7 on public utilities, even though chapter 7 never mentions the post office.

I would like to thank Stephanie Dohman, Melissa Frye, Cory Gathmann, Nicholas Georgakopoulos, Blair Mancini, and Mary McConnell for helpful comments.

An Important Note on References

Readers should have access to the sources of statistics, tables, and diagrams. On the other hand, they add a lot of clutter to a book. To provide information without reading clutter, I've put many of my sources here instead of in the chapter where they are used.

I have taken some ideas, facts, and references without citation (except to the original source) from the *Marginal Revolution* blog at <http://www.marginalrevolution.com> and *Wikipedia*. Sometimes I do not look up the original source at all, and I rely on *Wikipedia*. I really do think *Wikipedia* is the first place to look for facts. This can be dangerous, of course, so I have used my judgement in deciding which facts to find there. I have not even looked at what *Wikipedia* has to say about global warming, for example, because virtually all of the numbers relevant to global warming are subject to heated controversy. Information about things such as the governance structure of the FTC is more reliable, on the other hand, and Wikipedia is more up-to-date, and perhaps even more accurate, than any book and most other sources.

Please let me know, reader, if you find mistakes. I am sure there are a lot of them, because I have tried to provide institutional detail and real-life stories. The safe and easy thing to do in an economics text is to avoid mentioning any real-world facts at all. One is apt to make mistakes, enter controversy, and quickly become out-of-date. I'm risking that. As the legendary sign in the Old West saloon said, "Please don't shoot the piano player; he's doing the best he can." But you can tell him where he's made his mistakes.

Wikipedia entries can be found by googling. I have not put webpage references where I thought they would not be useful. Go to the web version of this book to click on links.

I have usually omitted footnotes from quotations. I have also changed punctuation freely, so that the sentence

(1) "Nevertheless, the trade war ended, and life continued."

would be quoted as

(2) "The **trade war** *ended*." (boldface and italics added)

rather than

(3) "... [T]he **trade war** *ended*[.]..." (boldface and italics added)

One need only to compare (2) and (3) to see why the conventional style is bad writing. It uses intrusive punctuation that distracts the reader while adding nothing except the useless information that the original phrase was

embedded in a larger sentence. You must trust me as an author not to quote phrases out of context. Providing pedantic styling is useless anyway since if I am so unscholarly as to quote out a phrase out of context, I can still deceive you by quoting entire sentences out of context or, better yet, simply forging my quotations outright. On the other hand, I will note added or omitted boldfacing and italics since those do change the meaning somewhat.

Some other books I recommend:

The Economist's View of the World Steven E. Rhoads.

Reforming Regulation by White

Giant Killers by Pertschuk

Yes, Minister.

Milton Friedman's *Capitalism and Freedom.*

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