Regulate and Protect

Government and Business

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So What?

When you visit Taco Bell, Burger King, or McDonald's, you're likely not thinking about the government. You're probably just trying to get lunch! But, believe it or not, government is closely involved in every bite of food you enjoy from these fast-food restaurants. It has rules that make sure the food you eat is handled, prepared, stored, and served safely. You can read about some government regulations on fast food in the article "FDA Regulations on Fast Food" by Gerald Hanks: http://smallbusiness.chron.com/fda-regulations-fast-food-64834.html.

But regulations like these don't just apply to restaurants! Government plays an important role in our private enterprise system. Keep reading to learn more about the interesting relationship between government and business.

Objectives

A Describe how government is involved in business.

B Explain ways in which government regulates business.

Government in Business: Why?

Original intentions

When the United States was born, government was not intended to have a hand in business. Businesses would be free to act in their own best interests without government involvement. The basic role of government in business would be as a referee only. Government's role would include:

- **Protecting business property**
  Government would provide fire, police, and military protection. It would issue trademarks to businesses to protect their products, copyrights to artists and writers to protect their creations, and patents to inventors to give them control of their inventions.

- **Enforcing business contracts**
  Contracts between businesses and customers would be legal and binding. In other words, if a business had a contract with a customer to provide certain goods or services, government would require the business to fulfill the contract and the customer to pay for the goods and services received. If the customer refused to pay, s/he could be taken to court and forced to pay the bill.

- **Settling business disagreements**
  Disagreements between businesses would be settled in government courts.

- **Setting and collecting taxes**
  Government would set and collect taxes on the products businesses sell. These funds would be used to help pay the expenses of government. The government would also set and collect **tariffs**—extra taxes on imported products. Tariffs promote the sale of American-made products by making imports more expensive to purchase.

A changing role

As the country grew and business expanded, government's role in business was forced to grow as well. Each area of government involvement had to be expanded, and new areas of responsibility were added. Government's role now includes not only passing laws that affect business but also enforcing those laws. Let's consider some of the reasons why this new role was necessary:

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▲ Government fills needs that businesses can't fill. For example, government collects taxes to build and maintain roads.

- **Growth and expansion**

  The most obvious reason for the expansion of government's role in business is the growth of the country. As the population grew, so did the need for more and different kinds of businesses. People also began to realize that the public has needs that business can't fill. They wanted government to meet those needs. For example, we all use the highways whether or not we have enough income to help pay for them. Since no business could afford to build and maintain all the roads in the country, government collects taxes to pay for road construction and maintenance.

- **Industrialization**

  As the country grew and business expanded, it also became more industrialized. Factories were built to produce goods, and changes in methods of production required government to take a more active role in watching over this production. This was necessary because not all businesses considered how their actions would affect others. Some businesses took advantage of other businesses or treated them unfairly. Some were unfair to their workers. In some cases, workers asked government to protect their rights and to make sure businesses treated them fairly.

- **Attitude changes**

  Changes in people's attitudes also caused government's role in business to expand. As the marketplace became more complicated, consumers turned to government for protection from dishonest or deceptive business practices, such as false advertising and the sale of harmful products.

- **Environmental concerns**

  An increased understanding of the dangers of pollution and awareness of the limited supply of certain resources have brought about more government involvement in business. People have demanded that government require businesses to help conserve resources and to stop polluting the environment.

  The Environmental Protection Agency (EPA) is in charge of protecting the environment in the US. You can read more about specific regulations on the EPA's website: http://www2.epa.gov/laws-regulations. How do you think these regulations affect businesses in your community?

- **Government in business**

  Government has also become an active participant in the world of business by producing certain goods and services that it sells to consumers, as well as by employing thousands of workers. For example, the United States Postal Service provides customers with the ability to post mail all over the country and across the world.

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▲ The United States Postal Service is one example of the government's participation in business.

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- **Changes in technology**
  The rapid growth of electronic commerce has made it necessary for the government to become increasingly involved in considering how business should be conducted over the Internet. For example, the government has passed COPPA (the Children's Online Privacy Protection Act), stopping companies from collecting personal information from children under the age of 13.

All of these developments have changed government's original role in business greatly. Government today has become not only a referee, a protector, and a tax collector but also a producer, a spender, and a regulator.

Purposes of government involvement

In the private enterprise economy of the United States, government and business have different goals. The goal of business is to make a profit. The goals of government are to protect the rights of individuals and businesses and to provide a stable environment.

Government takes different kinds of actions to meet its goals. In some cases, government intervenes in the operation of the economy. For example, the government may lower interest rates to speed up business activities. In other cases, government regulates business, such as passing laws that require businesses to label the ingredients on food products. Whether government is intervening in the business world or regulating it, government involvement in business has some specific purposes. Let's consider some of them:

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▲ The ingredient lists on the food products you buy are just one example of government regulation.

- **To provide public goods**
  In a pure **private enterprise** economy, all goods and services would be provided according to the law of supply and demand. In other words, business would supply what consumers demanded, and everything would come out evenly. In reality, however, businesses cannot supply everything that consumers demand. What business could afford or would want to supply public education? Who could afford to spend the many billions of dollars necessary to build an aircraft carrier for the US Navy?

  Such goods and services are called **public goods**. These are goods and services that we all use. They cannot be withheld from people who don't help pay for them. Public goods are provided by the **public sector**, that part of the economy that is owned and operated by government at all levels.

- **To improve public welfare**
  Government intervenes in the economy by operating public welfare programs for the benefit of people who are unable to provide for themselves. You might be familiar with public welfare programs such as SNAP (Supplemental Nutrition Assistance Program) and unemployment compensation. These programs not only benefit the people who need them, but they benefit business as well. People who receive the funds use them to purchase goods and services they otherwise could not afford to buy. Other examples of government assistance programs that affect business are job-training programs and loans to small businesses.

Supplemental
Nutrition
Assistance
Program

This article by Dan Charles, "How 'Double Bucks' for Food Stamps Conquered Capital Hill," (http://www.npr.org/blogs/thesalt/2014/11/10/361803607/how-double-bucks-for-food-stamps-conquered-capitol-hill) explains one interesting way government is improving public welfare. People who qualify for SNAP benefits are able to double the benefits' value when they buy local fruits and vegetables. By doing this, government improves the lives of people and their local economies.

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- **To protect public health**

  Government has passed many laws intended to protect public health. Businesses that produce food, drugs, and cosmetics must follow government regulations in their production. These products must undergo lengthy testing to ensure that they will not harm consumers. Builders may not use harmful products such as asbestos in their buildings. Water supplies must be treated to remove harmful bacteria, and sewage must be disposed of in a safe manner. Restaurants must be licensed and undergo frequent inspections to protect patrons.

- **To stabilize the economy**

  The government affects business directly through its **monetary policy**. The monetary policy determines the amount of money that will be in circulation and the level of interest rates. Increasing the amount of money in circulation has a positive effect on businesses because it increases the demand for goods and services. Raising the prime interest rate has a negative effect on businesses by making it more expensive to borrow money. Higher interest rates may slow business activities in general, while lower interest rates may speed up business activities.

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▲ The government's monetary policy determines the amount of money that will be in circulation and the level of interest rates.

  Government intervenes in business through its **fiscal policy**. Fiscal policy is used to set levels of government spending and taxation. If government spends more, demand for goods and services will increase. If government spends less, that demand will be reduced. If government increases taxes, consumers have less **disposable income** (money left after taxes are paid). The less disposable income consumers have, the less they can spend on consumer goods. This reduces sales for businesses. On the other hand, tax reductions increase consumers' disposable income. This leads to increased demand for consumer goods and increased sales for businesses.

- **To protect specific businesses**

  A direct form of government intervention in business occurs when government provides **price supports** for certain items. For example, food prices sometimes fall because of overproduction by farmers. When this happens, government price supports allow farmers to make enough money from selling their products to pay their costs. The government provides price supports by buying enough farm products to keep prices at a level that will give farmers a profit.

  Businesses may also receive financial help from government in the form of **subsidies**. Subsidies are financial assistance such as grants or tax breaks. Businesses most likely to benefit from government subsidies are those found in the transportation, housing, agriculture, and mining industries.

  This article by Marc Davis, "Government Subsidies for Business," goes more in depth about which businesses receive subsidies: http://www.investopedia.com/articles/basics/11/introduction-to-government-subsidies.asp.

- **To conserve the environment**

  Government can act in several ways to conserve the environment. One way is to pass laws that prohibit business activities that harm the environment. Examples would include laws controlling the use of dangerous chemicals or materials. Or, government can require the use of products that will do less damage to the environment. Government may even require that some resources be replaced as they are used. For example, businesses that cut down trees may have to plant new ones.

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▲ Government may intervene in the business world to conserve the environment.

- **To protect consumers and investors**

  Government often regulates business to protect consumers. Examples of consumer-protection laws include laws passed to prohibit false advertising and deceptive labeling and packaging; laws to require product testing to ensure that goods are safe to use; laws to set standards of safety in building construction; and laws to make food inspection mandatory to ensure that food is wholesome and is appropriately handled and stored.

  In the early 2000s, a number of corporate accounting scandals involving large companies prompted Congress to pass the Sarbanes-Oxley Act, also known as the Public Company Accounting Reform and Investor Protection Act of 2002. The goal of this and similar laws is to regulate business practices and financial reporting to protect investors.

- **To protect competition**

  Government tries to promote free competition for business by banning or regulating monopolies. A **monopoly** exists when a single business influences the entire production of a particular good or service. Since a monopoly eliminates any major competitors, the monopoly can control the price of the product by restricting production. The monopoly can also charge different prices to different customers if it chooses. It may even refuse to sell its product to particular businesses. This could cripple their operations. A monopoly may use resources inefficiently and pass the cost of its inefficiency along to consumers.

  Sometimes, however, it is best to have a single provider of a product. This is called a **natural monopoly**, and public utilities are a good example. Think about what your hometown would be like if several different businesses tried to compete to provide consumers with water. Since each business would need its own water and wastewater network, pipes would be everywhere. In addition, the cost of setting up and operating these networks would be very expensive. Eventually only one of the businesses would make enough profit to survive. The surviving water company would become a natural monopoly. Of course, like other natural monopolies, utility companies need to be controlled so that the best interests of consumers are safeguarded. One way that this is accomplished is through public utility commissions which monitor the practices of the monopoly. Government may also decide to deregulate certain industries where natural monopolies exist to increase competition and consequently lower prices for consumers.

▲ Monopoly isn't just a board game! A monopoly exists when a single business influences the entire production of a particular good or service.

What does government do when it thinks a natural monopoly has run its course? It deregulates! In deregulated states, consumers are able to select their own energy providers. Read this article from Open Secrets, "Electricity Deregulation," to learn more: https://www.opensecrets.org/news/issues/electricity/.

- **To regulate workplace conditions**

  Government regulation of business includes regulating the working conditions provided by businesses. Sometimes, there are hazards in the workplace—fumes from chemicals, dangerous equipment, etc. In such cases, government may require the business to use safety practices that minimize the risk of injury to workers.

  Other working conditions may be regulated by government as well. Minimum-wage laws specify the lowest hourly wage that businesses can pay workers. Other laws prohibit discrimination in employment practices and require equal pay for equal work.

- **To protect business property**

  Government continues to provide physical protection for business property and to issue trademarks, patents, and copyrights to protect products and ideas. Government has also passed zoning laws to protect the value of business property. For example, sections of a city may be zoned for certain kinds of businesses, such as office complexes or retail establishments. In this way, business owners are assured that no one can open a landfill or some other undesirable business in the neighborhood.

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Summary

The role of government in business in the United States has changed and evolved since the country was born. Government is involved in business to provide public goods; to protect public health and welfare; to stabilize the economy; to protect businesses, consumers, investors, and competition; to conserve the environment; to regulate working conditions; and to protect business property.

TOTAL RECALL

1. What were the original intentions of government's involvement with business?
2. Why did government's role in business change over time?
3. What are the purposes of government's involvement in business?

The Gray Zone

Zoning laws vary from state to state and town to town. In some instances, zoning laws may permit businesses such as adult bookstores, pawn shops, or tattoo parlors to open in certain districts; however, other business owners in the district may not want this to happen. They may protest or take other actions to prevent the new business from opening. What do you think? If it's legal for a business to open, do other business owners in the area have a right to try to keep it from happening?

Government in Business: How?


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Government passes laws to regulate business activities. In some cases, the laws establish permanent regulatory agencies. These agencies are responsible for enforcing the regulatory laws. Let's look at a few of the laws and agencies that currently regulate business activities.

Regulatory laws

There are several kinds of regulatory laws, passed to regulate many kinds of businesses. Some of the laws prohibit certain kinds of business activities, such as presenting false information in advertising. Other laws control what businesses are allowed to do. For example, a business that extends credit to customers is not allowed to harass customers about the debts they owe the business. There are also laws that require businesses to meet certain government standards. Businesses making products that could be harmful must be sure those products meet government safety standards.

Since business is always changing, old laws are frequently revised. New laws are also constantly being created. Businesses must know which laws affect their operations and comply with those laws. Some of the laws that are in force today include laws to:

- Control monopolies and unfair competition
- Protect small buyers from **price discrimination**
- Set product-safety standards
- Require honest labeling and standard packaging of products
- Prohibit the sale of impure food, drugs, and cosmetics
- Regulate product warranties
- Outlaw the harassment of debtors
- Protect the rights of workers and of consumers
- Regulate prices and wages
- Prohibit false or deceptive advertising

Regulatory agencies

A great many government agencies have been set up to monitor business activities. These agencies are often called *watchdog* agencies because they are constantly watching to see that businesses follow the law. Some of these agencies have the authority to impose fines or other types of punishment on businesses that violate the law. Current, important regulatory agencies include:

The Federal Trade Commission (FTC) established in 1914; the FTC administers and enforces laws to prevent price fixing, to prohibit unfair competitive practices, and to regulate false or deceptive advertising.

The Federal Communications Commission (FCC) established in 1934; the FCC regulates interstate and international communications by radio, television, wire, satellite, and cable.

The Food and Drug Administration (FDA) established in 1906; the FDA tests foods, cosmetics, and drugs to prevent the sale of unsafe items.

The Occupational Safety and Health Administration (OSHA) established in 1970; OSHA ensures safe and healthful working conditions for employees.

Other methods of government control

There are some other methods of government regulation with which you should be familiar. Two of these methods are licensing and using wage/price controls.

Licensing. **Licensing** is the process of issuing a permit allowing an individual or a business to function in the marketplace. To obtain a license, the business or individual must meet government requirements. For example, a real estate agent must have a license to work in or to operate a real estate agency.

Licensing allows government to control who operates certain businesses and the way in which they are operated. Government can deny licenses to unqualified persons or to businesses that don't meet government regulations. Government can also cancel a business's or individual's license if the appropriate requirements are not maintained.

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▲ Some businesses or individuals, like real estate agents, must meet government requirements to obtain licenses.

Wage/Price controls. The government occasionally reglates businesses by using wage and price controls to set ceilings on wages and prices. In other words, the government tells businesses the maximum amounts they can pay workers and/or charge for their products. As you might expect, wage and price controls are not popular. These controls are, therefore, used only in times of economic or national crisis.

Effects of regulation

Government regulation has both positive and negative effects on business. On the positive side, businesses are protected by government regulation from the unfair competitive practices of other businesses. Regulation of the use of resources gives all businesses fair access to those resources. Patents, trademarks, and copyrights provide legal protection for a company's products. Government regulation also provides businesses with specific rules to follow in their dealings with consumers.

Expense and inefficiency are probably the greatest negative effects of regulation. Businesses may need large numbers of employees just to handle government requirements. Some businesses become so involved in meeting government requirements that they do not operate efficiently.

Costs of regulation

Government has two main sources of revenue to pay the costs of regulation. Government receives money from businesses and individuals in the form of different kinds of taxes. When this is not sufficient, the government borrows money.

Taxes. Changes in prices charged by businesses affect the amount of income government receives. When prices go up, wages and profits usually go up, too. This means more tax money paid to government. When prices go down, wages and profits generally decline, also. This means less tax money to support government expenses. Government collects several kinds of taxes from businesses.

Borrowing. Government can borrow money from other countries or from the private sector. The **private sector** is that part of the economy that is owned and controlled by individuals or businesses. Usually, government borrows money by issuing bonds. When people purchase government bonds, they are actually lending their money to a government for a stated period of time. Government promises to repay the amount borrowed at the end of that time and to pay the bondholder a specified rate of interest for the use of the money.

What sort of taxes do businesses pay? Read this article from Investopedia, "Types of Taxes," to learn about the most common types of taxes that businesses are required to pay: http://www.investopedia.com/walkthrough/corporate-finance/2/taxes/types-taxes.aspx.

Summary

Government passes laws and establishes agencies to regulate businesses. It also regulates business through licensing procedures and wage/price controls. Government regulation has both positive and negative effects on business. Government pays the costs of regulation by collecting taxes and borrowing if necessary.

TOTAL RECALL

1. What are the two main ways that government regulates business?
2. Explain licensing and price/wage controls.
3. List some positive and negative effects of government regulation of business.
4. How does government pay the costs of regulating business?

Make It Pay!

What laws does your hometown have in place to regulate business? How do they affect your place of employment? Your parents' or guardians' jobs? Your favorite shops and restaurants? What are the purposes of these laws?