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## American business and the law

### Enemy of the states

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### Companies are increasingly worried by the growing power, and desire, of America's state attorneys-general to regulate and punish them

WHEN Ford Motor Company paid \$52m last December to resolve claims that it had misled consumers about the safety of its sports-utility vehicles, it settled not with America's federal authorities, but with 50 state attorneys-general. When Household International paid \$484m last October to settle allegations of predatory mortgage lending, it also settled with the states. Over a year after WorldCom collapsed amid massive accounting fraud, Bernie Ebbers, the firm's former chief executive, was this week having his fingerprints taken—not by federal prosecutors, but by officers instructed by Drew Edmondson, attorney-general of Oklahoma.

Not long ago the offices of most state attorneys-general were chasing nothing more exciting than petty fraud. Today, truly ambitious holders of office influence the way America does business, tackling issues ranging from antitrust and product liability to environmental regulation and customer privacy. This year alone, the 500 lawyers under the command of Eliot Spitzer, New York's attorney-general, have busied themselves with hedge-fund regulation (this week winning a \$40m settlement from Canary Capital), conflicts of interest on Wall Street, predatory lending by consumer-finance firms, drug pricing and more. Connecticut's attorney-general, Richard Blumenthal, has led the states' antitrust investigations into Oracle's attempted hostile takeover of PeopleSoft, a business-software rival, pre-empting a parallel federal antitrust investigation. After the Environmental Protection Agency announced changes last month that would ease the burden on owners of power plants and factories to upgrade pollution controls when expanding or renovating facilities, attorneys-general from Massachusetts, Pennsylvania, New Hampshire, New Jersey and New York said they would sue to block the new rules.

## Presumed public-spirited

Unlike consumer-protection groups and class-action lawyers, which pursue similar legal actions, state attorneys-general are usually presumed by the courts to be acting in the public interest, so they always get their cases heard. Still, big firms have the resources to tie up for years a state that acts on its own, says Tom Miller, Iowa's attorney-general. The crucial recent change, says Mr Miller, is the way the states have begun to work with each other.

Together, America's 56 state attorneys-general (along with the 50 states come representatives from Guam, American Samoa and the like) field nearly 12,000 lawyers, according to their national association, NAAG. Together, they can bring simultaneous suits in over 50 jurisdictions. Almost all of the states' most celebrated settlements have been the product of such "multistate actions"—including, above all, their landmark \$246 billion settlement in 1998 with America's tobacco industry. NAAG does much of the co-ordinating, levying membership dues that fund a string of committees overseeing antitrust, bankruptcy, consumer protection, environment, health care and so on. Multistate actions, says Mr Miller, have helped to "move the balance of power" between big firms and state governments. Phil Carlton, a lawyer who runs a firm that helps companies find local lawyers in state capitals, calls the combined power of the states an "awesome threat". "They are erecting a new branch of government," he says.

Supporters of the states say they are filling a void left by negligent federal regulators and politicians, who are in the pockets of big business. Mr Spitzer says that, as a young lawyer, he believed firmly in the federal government's prerogative to take the lead in regulating business. But the Securities and Exchange Commission failed to tackle conflicts of interest on Wall Street, forcing Mr Spitzer to intervene against his principles and make the banks settle and reform themselves. The National Highway Transport Safety Administration failed to take Ford to task for its contribution to rollovers caused by burst Firestone tyres, so the states did its work. Filing his charges against WorldCom, Mr Ebbers and five other former executives, Mr Edmondson said he acted because, "I don't think this firm has been punished."

Thus, state activism is said to ebb and flow with the philosophy of the federal government. In the 1980s, the states parried Ronald Reagan's deregulatory policies with their own brand of consumer activism. George Bush's friendliness to big business is getting a similar reception now. Such checks and balances, claims Mr Miller, a Democrat, are part of the "genius" of the American federalist system.

Critics point to the pernicious lessons of the 1998 tobacco settlement. This taught the states the value of pooling their resources—not just with each other, but with the class-action lawyers whose attempts to wring damages from the tobacco industry had failed until then. As politicians, the attorneys-general won plaudits from voters for championing public health, along with big campaign donations from the trial lawyers, whose fees they helped to secure. As local officials, they found a rich new source of state revenue, thus enhancing their position in the machinery of state government. Ever since, personal ambition (a state's attorney-general now often goes on to become its governor), plus the states' deepening financial crisis, have pulled energetic attorneys-general ever further away from their duty to pursue the wider public interest. From his \$1.4 billion "global settlement" with Wall Street's ten-biggest securities firms in April, Mr Spitzer wrung nearly \$500m for state coffers, and invaluable publicity for his blossoming political career—without even detailing quite how the banks were supposed to have broken the law.

In the end, the states will be judged on the quality of their policymaking. That depends, in part, on whether it makes sense to regulate business federally, or in the states. Decentralisation lets local communities match local rules to local values. It also lets competing governments experiment with policy. It was the deregulation of airlines in Texas and California in the 1970s, for instance, that showed federal government the way. Yet regulations in one state can have unpleasant effects on business in another. Poorly-funded states might lack expertise to regulate properly, and a patchwork of state-by-state regulations might heap costs on doing business nationally, reducing the ability of companies to reap economies of scale. Because potential economies of scale are growing in many markets, and because rapid technological change might strain the expertise of local regulators, argues Robert Hahn of the AEI-Brookings Joint Centre for Regulatory Studies in a recent paper, the burden ought increasingly to fall on proponents of decentralisation to justify their policies.

That is the opposite of conditions in America today: the states have power and popularity, while big government in Washington, DC gets all the scrutiny. One reason is that the Republicans, the traditional pro-business party but also the one in favour of greater state rights, are currently in power. So long as this continues, the state attorneys-general should flourish. Business had better watch out.

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