Panel II: Public Versus Private Environmental Regulation

*Richard Lazarus, Second Panelist**

I want first of all to thank the Federalist Society for inviting me. When I was in Washington, D.C., in the Justice Department a few years ago, I would see the programs for the Federalist Society. The Society always had, I thought, some of the best, most interesting, and challenging panels of any program around, but I never felt that I could go because I was afraid that I might get mistaken for a federalist if I did. This way I finally was able to come without having to worry about it. (Laughter.)

What I did not anticipate, though, was how by walking into the banquet last night, I would shock a lot of the strong federalists that I knew when I was at the Justice Department. It was extraordinarily unsettling for them. Then I realized I had taken off my speaker badge. So I quickly put it back on, and you could see them acknowledging that it was all right, their program was still intact.

I became worried in preparing for this panel because I am fairly well aware of what people have written in this area, and I do not think there is as much room for debate on some of these questions as there might seem. But to the end of not building consensus, I would like to be more, rather than less, provocative, and let you all search for the common ground.

My basic thesis is that much, if not most, of free market environmentalism is unhelpful. It is an unhelpful diversion and it is time for people to stop dreaming about the free market in the environmental context. My concern is that free market environmentalism threatens to do what the deregulation movement of the early Reagan years did: to impede the development of needed regulatory reform in the environmental protection area, which had been well underway in the Carter administration, and included the use of market incentives.

It is time to accept the premises of the public law model that the free market will not attain the efficient allocation goals or the distribution goals of this country, that environmental protection standards cannot be defined by the free market. Instead we need to identify those circumstances, such as the one mentioned by Boyden Gray, where market incentives may work well within the public law model.

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Finally, I would like to describe how this debate is actually being played out in an interesting fashion between two prominent conservative Justices on the Supreme Court, Justices Scalia and Kennedy, with Justice Kennedy getting it right and Justice Scalia, not surprisingly, not. (Laughter.)

First, when dealing with an environmental protection law, there are really four basic legal regimes that you can use to achieve the right amount of pollution and the desired distribution of pollution. The first is the private property or free market model. Here, you assign private rights to the resources, allow contracts to freely function, and allow the marketplace to work. Theoretically, you come up with the allocationally efficient distribution and the fairest distribution. The role of tort law was simple: to defend the physical boundaries of those property rights—and nothing more. Tort principles did not purport to define property rights. That is basically the model which I presume the Framers assumed would dominate.

The second model is the tort or nuisance model, in which tort no longer just defends property rights from external invasion. Instead, tort law defines private property rights in the first instance. In this model, the courts have a very active role as regulators by interpreting and applying common law tort principles.

The third model is the public law model. It is a command-and-control, regulatory model, with legislatures and agencies dominating and establishing the standards. This is what dominates today.

The fourth is what I would refer to as the true regulatory reform model. In this model, the public law establishes the environmental protection objectives, but private market incentives are used to achieve the standards in an allocationally efficient manner. Such market incentives include taxes, deposit refund systems, and marketable permits.

Now I am going to try briefly to summarize free market environmentalism. I think parts of it ought to be applauded and others are misguided, but I am ultimately concerned that the debate it invites could set things back.

The basic argument of free market environmentalism is that the private property regime did not work well because it was not allowed to work well. The government undermined it. The proponents of free market environmentalism cite examples of government subsidization of the exploitation of Western public lands as showing that governmental interference led to less, rather than more, environmental protection. They also argue that the current public law command-and-control model is subject to special interest capture. As a result, they claim, it really just maximizes the wealth of a few interest groups. It follows that the command-and-control model is not true environmen-

tal protection, and it is not actually the result of the democratic process. Moreover, they maintain that it is extraordinarily inefficient in mandating uniform technology standards when, in fact, costs are quite divergent among those regulated.

Based on these critiques, free market environmentalists argue that we should return to the private property or free market model. My basic feeling is that there is some merit to the premises and virtually none to the conclusion. Where there is merit is in their argument that much environmental destruction of public lands was caused by the undermining of free markets. It is also certainly true that there is much inefficiency in the current command-and-control regulatory model.

But there is virtually no merit to the proposed solution that we return to the free market model. That government subsidies can corrupt the market in an anti-environmental way does not at all logically lead to the conclusion that the market model, left to its own devices, can adequately decide environmental protection standards or, indeed, should be allowed to decide environmental protection standards.

First, why it cannot, and then why it should not. The reason why it cannot is, as Dick Stewart alluded to yesterday,[1] that there is a reason why the market and private property do not work in this area. Simply put, they are not capable of internalizing the external costs associated with environmental pollution. These costs are what the pollution problem is all about, and internalizing these costs is what environmental protection is all about.

The market cannot internalize these costs because internalization requires that there be clearly assigned private property rights in the environment to be protected, and in many cases it is impossible to assign such rights. Where the pollutant and the impact are distant from one another, the spatial externalities are simply too great to allow assignment and enforcement of the right. If the sulfur emission occurs in Ohio, it is difficult to assign rights to acid rain damaged lakes in Maine that can be meaningfully enforced against these distant sources in Ohio. There are also significant temporal externalities, which are often overlooked, where the impact is distant in time from the polluting action. How are we to assign property rights to future generations that can be enforced against actors today?

The fee simple absolute that Bob Ellickson mentioned yesterday[2] works quite well in some contexts, but not with all the kinds of air pollution and water pollution problems we have today. These

1. *See* Richard B. Stewart, *Panel I: Liberty, Property, and Environmental Ethics*, 21 ECOLOGY L.Q. 411, 412 (1994).

2. *See* Robert C. Ellickson, *Panel I: Liberty, Property, and Environmental Ethics*, 21 ECOLOGY L.Q. 397, 401 (1994).

problems present externalities far beyond the fee simple absolutes of any one landowner. This is especially true for hazardous waste sites, which is why Dick Stewart referred yesterday to the extreme importance of imposing financial responsibility and closure requirements on the owners and operators of hazardous waste sites.[3]

Even if you could manage somehow to define clear private rights to the competing interests in environmental conflicts, you would not be able to rely on the courts to resolve these conflicts between the rights holders. I would not expect that Peter Huber would advocate having the courts decide the questions of conflicts between rights in that context. First, you cannot assume the cases are going to be brought. Information and transaction costs are simply too high. There are too many people involved, many of them unrepresented in terms of temporal externalities. And even if you could bring the cases, the courts could not handle them.

This last point is the reason why we *should* not allow the market to set levels of environmental protection. It is really beyond the institutional competence of the courts to weigh the relevant competing considerations and to design the remedies that would be required. I remember quite well when Attorney General Smith took over the Department of Justice in 1981, one of the major objects of attack was judicial attempts to design remedies to deal with these kinds of institutional problems. The courts simply do not have the technological or policy expertise to make these decisions.

Resolving these conflicts over environmental impacts and deciding the appropriate level of environmental quality are not just economic choices. They are policy choices. Moreover, they force us to make decisions in the face of imperfect information and scientific uncertainty, which are other hallmarks of the environmental protection area. You have to decide how much risk you are willing to accept. You have to decide what to do about the possibility of irreversible effects over great space and over great time. The policy character of these choices is why courts not only cannot, but also should not, decide these issues.

It is a mistake to think about these issues as simply a matter of allocation efficiency. Ultimately, setting the standards in the first instance is a political decision, not a market decision. I noted in Boyden Gray's remarks that he quite rightly referred to the decision of whether to approach the acid rain question, what to do with those risks, as a political decision.[4] The market cannot necessarily be ex-

3. *See* Resource Conservation and Recovery Act § 3004, 42 U.S.C. § 6924 (1988).

4. *See* C. Boyden Gray, *Panel II: Public Versus Private Environmental Regulation*, 21 ECOLOGY L.Q. 434, 434 (1994).

pected to make the correct decision here. You have to decide what risk to accept and what to do in the face of uncertainty. You must decide how to define yourself now in relation to future generations. You also have to decide how you value distributional fairness. These are political decisions. These are policy decisions. These are decisions for the democratic process, not for the courts and not for the marketplace.

What we can avoid, though, is having the government serve the exclusive role. We can move to a regulatory reform model, and that is where the debate should be. The government can set the environmental protection standards and then use market incentives, the kinds of things that Boyden Gray was advocating, to achieve those standards. Those kinds of reform are essential. But we need to have honest debate about this. We need to rid the debate of the exaggerated promises of economists, who advocate a return to a private property model. We should have the debate devoid of the political rhetoric about the sanctity of the free market and the constitutional codification of that system.

There are places where market incentives can work quite well within the regulatory public law model. Examples are taxes for waste disposal, deposits for environmentally harmful constituents, "cash for clunkers" to try to return some of the most polluting vehicles, and marketable permits for some kinds of discharges.

But one has to acknowledge that there are also limits. Market incentive approaches cannot decide the environmental protection standards and the level of environmental quality in the first instance. Further, it is often quite difficult to determine how to apply market incentives to achieve the standard that one selects; emissions fees are one example. Also, in many contexts market incentives simply will not work. If there are too few market participants, a market will not develop. If there are too many, the transaction costs of setting up the government bureaucracy to administer private property rights simply may overwhelm the advantages.

More importantly, there are lots of circumstances with threshold localized environmental effects, where the distribution of pollution rights does make a difference. Marketable permits should work better for acid rain than for almost any other environmental issue, because the source of the pollution consists of a large number of relatively large companies in the Midwest that all contribute to a common pool of air pollution going to the Northeast. Thus, which source is actually emitting the stuff is fairly fungible, at least theoretically. That is not the case where there may be localized threshold effects in a particular area. In the latter context, we do care about exactly which source is

polluting. We have divergent costs associated with the pollution. There, the free market model begins to have some problems.

What concerns me is that by overselling what free market environmentalism can accomplish and by buying into some of the political rhetoric, we may impede debate about exactly where free market environmentalism works and where it does not. I think it can accomplish a lot. I think there is no question that building market incentives into the public law model is the way to go to obtain needed cost savings and to reach the next level of environmental quality, which is also needed. But to advocate a return to the old free market model is extraordinarily misguided.

Finally, how is this debate manifested in the Supreme Court? I think it is quite evident at the moment in the tension between the opinions of two conservative Justices. Justice Scalia's opinions, not surprisingly, are very reflective of the free market, private property model. In a sense, he seeks to try to codify it in the Constitution. I think Justice Scalia is trying to resist the public law model in two distinct lines of cases, and in both contexts his reasoning evinces a strong distrust of the democratic process. The first line of cases is his taking decisions, while the second is his standing decisions.

In his taking decisions, such as the *Lucas* case, Scalia seeks to limit government regulation that adversely affects private property values by limiting such regulation to the common law of nuisance.[5] This very much harkens back to the common law model. More interesting, perhaps, are his standing decisions, such as the second *Lujan*[6] case, which Professor Sunstein has written about.[7] Here, by limiting Article III standing and the ability of Congress to create Article III standing, I believe Justice Scalia is seeking to erode the enforcement of those public law statutes that Congress has enacted. In this way, he uses the Constitution to resist the adequate enforcement of the public law model.

By contrast, look at Justice Kennedy's separate opinions in those cases.[8] I think he believes and understands the appropriateness of the public law model. Justice Kennedy is willing to allow the legislature to go beyond common law nuisance in restricting private property. Even when such police power action would render the property valueless, Justice Kennedy appreciates that the complexity of ecosystems and the fragility of some parts of the natural environment mean that state

5. *See* Lucas v. South Carolina Coastal Council, 112 S. Ct. 2886, 2900 (1992).

6. Lujan v. Defenders of Wildlife, 112 S. Ct. 2130 (1992).

7. Cass R. Sunstein, *What's Standing After Lujan?: Of Citizen Suits, "Injuries," and Article III*, 91 MICH. L. REV. 163 (1992).

8. *Lucas*, 112 S. Ct. at 2902-04 (Kennedy, J., concurring); *Lujan*, 112 S. Ct. at 2146 (Kennedy, J., concurring).

legislatures must be allowed to redefine the permissible scope of private property rights in natural resources. This may be necessary even when doing so may thereby completely destroy settled economic expectations. Justice Kennedy is likewise willing, unlike Justice Scalia, to allow Congress to authorize citizen suits where the plaintiffs allege injuries and chains of causation that do not rise to the level of traditional common law notions of injury and causation.

The opinions of Justice Scalia and Justice Kennedy are fundamentally in tension, and although Justice Scalia wrote the opinions for the Court in *Lucas* and *Lujan*, I am here to tell you today that Justice Kennedy, not Justice Scalia, will ultimately speak for the majority of the Court. Justice Kennedy, not Justice Scalia, is the true federalist in this area.

Thank you.