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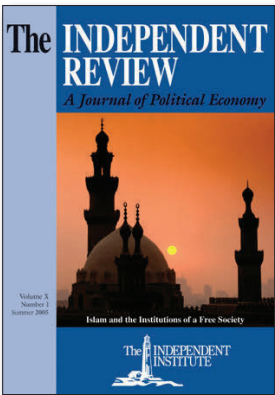


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Market-Based Environmentalism and the Free Market

They're Not the Same

— ♦ —

ROY E. CORDATO

Since the collapse of communism in Eastern Europe, overtly socialist solutions to public policy problems have fallen into disrepute, even among socialists. It now seems to be widely accepted among policy analysts of both the Left and the Right that direct government control of market activities and market outcomes—the so-called command-and-control approach to public policy—is an excessively costly way to achieve public policy goals.

Yet despite widespread rejection of outright socialism and command-and-control policies, there is little appreciation of truly free markets and the outcomes they are likely to generate. Policy makers do not value market exchange because it maximizes liberty and personal satisfaction of wants. Instead, policy makers value the market because they can manipulate it to produce a centrally planned outcome. This approach describes so-called market-based environmental policy.

All approaches to market-based environmentalism (MBE) tend to follow the same pattern. As MBE advocates Robert Stavins and Bradley Whitehead (1992) point out, “There are two steps in formulating environmental

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policy: the choice of the overall goal, and the selection of a means or 'instrument' to achieve that goal" (3). Specifically, government authorities first select a particular outcome (e.g., level of sulfur dioxide emissions or amount of recycled paper used in grocery bags) as a desirable goal. Viewing the behavior of individuals making exchanges in the relevant markets as something to be manipulated through public policies that create incentives to "do the right thing," policy makers then select an appropriate means for this purpose. In environmental policy, the two most highly touted instruments are excise taxes and tradable permits. These market-based approaches, advocated by professional economists and think-tank policy analysts on both the Left and the Right, actually use markets against themselves. In reality they are often meant to thwart the outcomes of true free-market activity.

I shall criticize the arguments advanced for market-based environmentalism, the most important of which have their roots in Pigovian welfare economics.¹ My criticism relies on arguments advanced by F. A. Hayek to demonstrate the impossibility of efficient central planning and by James Buchanan regarding the subjective nature of costs and benefits. The economic arguments for MBE have given it widespread appeal across the political spectrum. I shall argue that MBE has the same defects as full-blown socialism: it is inconsistent with individual liberty and, in practice, impossible to implement successfully.

Environmental Problems: Market Failure or Government Failure?

The reigning view of environmental problems considers them as inherent in a free society. If people are free to pursue their own self-interest—to produce and consume whatever they want, how and when they want it—polluted air and waterways, littered streets, and depleted natural resources will result. The typical characterization in most of the social science literature is that such problems represent "market failure." Pollution and environmental degradation are cited as evidence that Adam Smith was wrong, or at least naïve. People pursuing their self-interest do not necessarily advance the well-being of society as a whole. Therefore, it is not only appropriate for, but incumbent on, government to correct the market's failings.

This view constitutes a misunderstanding of the nature of a free society and a free-market economy. Contrary to the standard view, environmental problems are not an unavoidable side effect of a free-market economy. Instead, they occur because the institutional setting—the property rights

1. This area of economics is named for economist A. C. Pigou, who originated the analysis. See Pigou ([1927] 1952).

structure—required for the operation of a free market is not fully in place. Because, in all modern societies, government has taken nearly complete responsibility for the establishment and maintenance of this institutional setting, environmental problems are more appropriately viewed as manifestations of government failure, not market failure.

Environmental Problems as Conflicts over the Use of Property

In current debates over environmental issues, it has become common to abstract from individual decision makers in society and to view certain uses of resources as inherently problematical. Traditionally, conditions such as air and water pollution aroused concern to the extent that they harmed people. More recently this view has been abandoned. Now many argue that certain uses of resources should be regulated or proscribed not because they harm third parties but because they degrade “the environment.” For example, for many, strip mining, the use of landfills for the disposal of trash, and the cutting down of old-growth forests do not constitute problems because of harm to humans. Indeed, the fact that humans usually benefit from these practices is viewed with disdain. The traditional view of environmental problems, that they should concern policy makers because these problems involve harm to human beings, has been turned on its head. The modern view, adopted by many who advocate market-based “solutions” is that harming humans is justified in the pursuit of “saving” some aspect of the nonhuman environment.²

In a free society, concern for human beings must take center stage. In assessing environmental problems, the core question is how and why such problems interfere with individual decision making, construed as the formulation and execution of plans. As all formulation and execution of plans involve the use of physical resources, and such plans can legitimately employ only resources to which one has rights, any environmental analysis focused on the individual decision maker must pay attention to property rights.

For example, air pollution creates a problem to the extent that it interferes with individuals as they formulate and execute plans. This can happen only if the pollution somehow interferes with an individual’s exercise of rights to his or her property or if uncertainty prevails concerning who actually has the rights to a particular resource. Viewed in this way, all environmental problems involve conflict over the use of property. Person A and person B are attempting to use resource X for conflicting purposes. Either A

2. For an excellent discussion of this issue and the motives underlying much environmental advocacy, see Kaufman (1994).

or B clearly has the relevant rights to X but these rights are not being enforced, or the rights to X have not been clearly defined, that is, neither A nor B nor anyone else has the relevant rights to X. In the former case, the environmental problem is one of property-rights enforcement. In the latter case, an authoritative decision must be made regarding who should have the rights. The foregoing conditions establish the relevant parameters of environmental problems from a humanist, as opposed to an environmentalist, perspective.

Two simple examples can highlight each of these possibilities. Imagine a community with a cement factory that emits dust into the air without the consent of people nearby. Because of the dust, people in the community must wash their cars and house windows more frequently. The dust also soils clothing hung out to dry and creates respiratory problems for those who breathe it. This problem is clearly one of property-rights enforcement. The problem arises not because the dust is emitted into the air but because it has direct contact with what is indisputably people's property—their cars, houses, laundry, and lungs—and thereby interferes with their planned use of it. Here the conflict concerns the use of property to which ownership is clearly defined but regarding which some rights are not being strictly enforced.

An example of the second type of problem involves the use of a public waterway such as a river. A factory uses the river as a receptacle for waste generated by its production process. Downstream, homeowners use the river for fishing and swimming. Suppose factory waste renders the river unfit or at least less fit for these purposes. The central problem here is not simply that the river is being polluted, but that plans for its use are in conflict. Unlike the rights in the cement-dust case, the rights to the river are not clearly defined, so the public policy issue involves who should have what rights.

Property rights must be clearly defined and enforced in order for a free market to exist. If problems arise because these institutional requirements are not met, it is wrong to blame the free market for the problem. In each of the examples just presented, a problem arises because the institutional prerequisites of a free market are, in one way or another, not fulfilled. The problems should not be blamed on market failure when a free market is prevented from coming into existence. The problem actually represents institutional failure, as the institution of private property itself is not being sustained. From a public policy perspective, a “crack” exists in the property-rights structure. In general, a genuine free-market policy would first identify the specific interpersonal conflicts that have emerged, then identify and repair the flaws in the property-rights structure that have given rise to the conflicts.

This assessment suggests that “free-market environmentalism” is simply

an attempt to advance the free market in areas plagued by conflicts over portions of the physical environment. It should be noted, however, that the focus is on human freedom and welfare and not the nonhuman environment itself. The result of free-market policies in dealing with such issues may not always be consistent with goals of environmentalism as typically construed, although often they will be.³ The defining characteristic of free-market activity is the institutional setting in which it occurs, not the outcomes it generates.

In the ideal institutional arrangement, all resources are privately owned, and all owners can employ their property in any way they wish. The only legal constraint is that no one be allowed to infringe the equal rights of others.⁴ Once these conditions are established, the market process is open ended. The actual results reflect the interaction of individuals pursuing their own objectives, often by making exchange contracts with others. True free-market public policy should not focus on particular outcomes with regard to the environment or anything else, including prices, costs, and output levels. Instead, it should focus on correcting flaws in the institutional setting that are giving rise to human conflict and thereby preventing the efficient pursuit and attainment of goals. From this perspective, what have come to be called environmental problems are indeed problems in many cases, because they are rooted in deviations from the optimal property-rights structure.

On occasion, however, establishing a free market will conflict with the goals of environmentalism as usually construed. An example pertains to the treatment of endangered species. It has become common for the U.S. Fish and Wildlife Service (FWS), in enforcing the Endangered Species Act, to place controls on the use of privately owned land deemed either an actual or a potential habitat for an animal listed as endangered. From a free-market perspective, such restrictions become the source of institutional failure rather than the solution of market failure. In such cases the policy generates a conflict between the actual owners of the land and certain nonowners who use the state to gain decision-making power over the use of the property. A free-market advocate, environmentalist or not, would oppose such policies and favor the individual whose property rights are being transgressed. Free-market environmental policy cannot be unbiased or even democratic. It must be distinctly biased in favor of whoever has title to the portion of the environment in dispute.

3. For an excellent discussion of how respect for private property and free markets often comports with the goals of environmentalism more broadly conceived, see Anderson and Leal (1991).

4. For discussions of the economic efficiency implications of this institutional framework, see Kirzner (1963) and Cordato (1992). For discussions of some of the philosophical aspects, see Rand (1967) and Rothbard (1973).

Of course, the free-market environmentalist would oppose the FWS regulations, but might be willing to attempt to raise funds to purchase rights to the desired property for the purpose of preserving the habitat. This kind of activity distinguishes a general supporter of free markets from a free-market environmentalist. They differ in their private activities, not in their public policy stance.

In general, free-market advocates argue that nature will fare better under a regime of private property and free exchange than it will under other institutional arrangements, because the profit motive, coupled with the obligation not to violate the property rights of others, leads to the conscientious stewardship of natural resources. As stated in one study in the growing literature:

Unfortunately, under current institutional arrangements, too many people find that environmental destruction rather than conservation is in their self interest. Most of our environmental problems arise because resources such as air, water, forests, and many species of birds, fish, and other wildlife are owned in common. Because these resources have no owners, they have few protectors and defenders. Because there is no market for these resources, people have poor incentives to maintain their value.... The institutions that have worked well for us in other areas of economic life include private property, markets, a price system and methods for punishing people who violate the rights of others.... Government is needed to create the legal framework. Within that framework, people should be free to experiment and innovate to solve problems which large bureaucracies are unlikely to solve. (Task Force Report 1991)

Free-market environmentalists have done a good job of demonstrating how the institution of private property has led in the past, and could lead in the future, to attaining many of the goals espoused by the environmental movement.

Still, the end result of a free-market process may not coincide with the goals of environmentalists, particularly if those goals require restrictions on the use of resources for their own sake or relate to issues where no physical or economic harm to human beings is involved. Recognizing this fact, most mainstream environmentalists remain antagonistic to truly free markets. But some have also come to recognize that politically controlled markets can be useful tools, in a manipulative sense, for the advancement of their aims. These more mainstream environmentalists, with the intellectual assistance of some segments of the economics profession, are spearheading the recent advocacy of the policies known as market-based environmentalism.

Market-Based Environmentalism: Stealth Socialism

It is ironic that although the intellectual foundation of MBE has been laid largely by conservative economists, MBE is embraced more or less enthusiastically by liberal environmentalists. The economists have given the environmentalists a means of dispensing with command-and-control regulatory policies while maintaining their command-and-control ends. Whether intentionally or not, many economists, most of them conservative, have become efficiency consultants for the traditionally anti-free-market environmental movement. These economists have demonstrated that the environmentalists can attain their goals more “efficiently” by creating suitable incentives in the market than by setting rigid rules and standards for production processes. Writing as both a conservative and an economist, Murray Weidenbaum, former chairman of President Reagan’s Council of Economic Advisers, succinctly states the basic principle of MBE: “In the various circumstances when government does regulate (as in the case of reducing environmental pollution), conservatives prefer that government policy makers make the maximum use of economic incentives. Thus, to an economist, the environment pollution problem is not the negative task of punishing wrongdoers. Rather, the challenge is a very positive one: to alter people’s incentives” (Weidenbaum 1992, 497).

Conservative economists have been quite successful in convincing former regulatory zealots in the environmental movement that command-and-control policies are a cumbersome and unnecessarily costly way to achieve their ends. MBE has won the whole-hearted endorsement of the Progressive Policy Institute (PPI), the think tank most closely associated with the Clinton administration. PPI authors Robert Stavins and Bradley Whitehead (1992) state:

Command and control regulations were powerful in the early battles against environmental degradation, but they have begun to reveal many of the same limitations that led to the collapse of command and control economies around the globe. Command and control regulations are often economically inefficient—that is excessively costly.... Market based policies start with the assumption that the best way to protect the environment is to make it in the daily self-interest of individuals and firms to do so. The key to greater environmental protection, then, is...decentralization—by changing the financial incentives that face millions of firms and individuals in their private decisions about what to consume, how to produce, and where to dispose of their wastes. (iii)

Clearly, MBE is outcome driven. Its thrust is to manipulate market incentives in order to achieve a centrally planned outcome with respect to the use of natural resources. As argued by Stavins and Whitehead (1992), "Policies are needed to mobilize and harness the power of market forces on behalf of the environment, making economic and environmental interests compatible and mutually supportive. Policy makers must begin to link the twin forces of government and industry" (3). Clearly, MBE differs fundamentally from public policy meant to promote free markets. Whereas proponents of the latter see free markets as a means of fostering liberty and human well-being, proponents of MBE see it as an instrument for "harnessing" the activities of people "on behalf of the environment."

Green Taxes and Economic Analysis

Excise taxes and tradable permits are the two major policy instruments advocated most frequently as part of MBE. The justification for using excise taxes to promote environmentalist goals ("green taxes") has its roots in Pigovian welfare economics. Welfare economics is the part of economic analysis that sets the standards by which economists make public policy prescriptions. Mainstream economists have adopted Pigovian welfare economics, the approach expounded in most economics textbooks. Nearly all advocates of MBE, on both the Left and the Right, give lip service to this sort of welfare economics (Repetto and others 1992; Viscusi 1992; Weidenbaum 1992; Stavins and Whitehead 1992).

From this perspective, the success of market activity depends on market outcomes, particularly the prices and quantities that markets generate. Certain price-quantity outcomes are deemed "efficient," contributing positively to social welfare, whereas "inefficient" outcomes reduce social welfare. When efficient outcomes are not generated, free markets are declared a failure, and the primary purpose of public policy is manipulating the choices of market participants to achieve the correct results.

This approach to environmental policy has many flaws, most of which stem from methodological errors in the economic analysis underlying the policy prescriptions.⁵ In the standard argument, social welfare is maximized when markets conform to a set of ideal conditions known as "perfect competition." Perfectly competitive markets have many buyers and sellers, all perfectly informed of relevant market conditions; costless entry and exit; and homogeneous product lines. Given these conditions and the attainment of systemic equilibrium, prices will accurately and completely reflect the marginal costs of production and, as a result, the quantity of any good

5. For extensive discussions of the economics, see Cordato (1992, 1995).

produced and sold will be efficient. All costs of production or consumption are "internalized," that is, borne by the producers or consumers of the product. The market thus "succeeds" in generating the correct, perfectly competitive outcome.

Within this framework, pollution constitutes a problem because it gives rise to incorrect outcomes. In the cement-dust example, the cement company is not bearing all the costs of its production. People in the surrounding community whose plans are disrupted by the pollution also bear some of the costs. In such cases the price of the product is too low, the amount produced too high. The market is said to fail. If the cement company were bearing all the costs, including the pollution costs now borne by others, its costs of production would be higher, it would produce less, and consumers would pay a higher price for cement.

Policy makers use market-based policies to manipulate market incentives ostensibly to obtain the "correct" result, that is, the result that would occur in a perfectly competitive market. In a situation like that of the example, most economists would advocate levying an excise tax. The goal is to impose a tax on each unit of production of the polluting firm that exactly equals the pollution costs borne by the outside (nonconsenting) community. The firm would then have an incentive to behave as if it bore all the costs of production and hence to generate the sought-after "efficient" market outcome. The tax "succeeds" where the free market "fails." As Weidenbaum (1992) argues, "Pollution taxes serve to correct a serious source of market failure: the absence of 'price' needed to prevent the careless and excessive use of scarce environmental resources. Taxation...is a basic way of working through the price system" (499).

This approach to dealing with pollution problems necessarily leads to the manipulation of markets for the achievement of political goals. The tax "corrects" the market failure only if imposed exactly as economic theory dictates. But the perfectly competitive conditions that the policy is supposed to induce are so highly stylized and otherworldly that they provide no real-world guidance for imposing the appropriate taxes.⁶

To implement the Pigovian program, policy makers must be able to measure the spillover costs associated with the pollution. But as James Buchanan (1981) has emphasized, "Cost is subjective; it exists only in the mind of the decision-maker or chooser.... Cost cannot be measured" (14-15; see also Buchanan 1969). Economically relevant opportunity cost is the satisfaction forgone in choosing to do one thing rather than another. If someone washes his car more frequently because cement dust from a nearby cement plant is soiling it, his cost is the greatest satisfaction he expected to

6. For a detailed discussion, see Cordato (1989, 1992).

receive by doing something else. Clearly, this is both unmeasurable and unknowable by any outside observer. Therefore the “correct” market outcome also is unknowable. As Buchanan (1969) has concluded, “In order to estimate the size of the corrective tax...some objective measurement must be placed on these external costs. But the analyst has no benchmark from which plausible estimates can be made” (72). Anyone defending the use of such taxes as a means of enhancing economic efficiency would first have to explain how Buchanan’s objection can, in practice, be overcome.⁷

Advocates of corrective taxes ignore the subjective-cost issue; they proceed with their analysis as if the problem did not exist. They reach conclusions about social costs without a hint that the numbers cited are supposed to measure something conceptually unmeasurable. For example, one analyst confidently proclaims that “the current net tax per gallon [of diesel fuel] is 13 percent of the price, while the environmental cost per gallon is 50 percent of the price. The tax on this fuel could be raised substantially to promote its efficient use” (Viscusi 1992, 18). In light of Buchanan’s arguments, one can only wonder what these numbers actually measure, but clearly they are not measures of economically relevant opportunity costs.

In applications, mainstream welfare economics is timeless and does not allow for change, invoking static equilibrium analysis. Analysts assume that information gathered today relates equally to tomorrow. But such constancy would require that input scarcities, technology, population, and people’s preferences remain fixed. Once any of these variables changes, current information—intended to shed light on the costs of pollution and therefore on the correct outputs, prices, and taxes—becomes outdated. Inasmuch as these variables are in reality constantly changing, identifying the appropriate corrective tax is an impossibility. Even if actual opportunity costs were being measured, all cost-benefit analysis would necessarily be based on historical evidence, much of it already several years old when gathered. Any corrective tax would be obsolete even before its calculation.

Both the subjective-cost problem and the time-passage problem exemplify a more fundamental problem of information or knowledge. This dooms all attempts at efficient central planning, including Pigovian corrective taxation. F. A. Hayek articulated this argument against socialist planning in the 1930s and 1940s. He emphasized that the information necessary for

7. Although economists advocating MBE recognize Buchanan’s public-choice analysis in assessing the extent to which government activity is likely to correct for market failure, they ignore the implications of Buchanan’s cost theory for the use of social cost-benefit analysis. A consistent application of Buchanan’s arguments implies that real-world social cost-benefit analysis, including the type suggested by Coasean property-rights analysis, is a logical impossibility outside a perfectly competitive general-equilibrium world. But any world with externalities is not such a world (Cordato 1989).

central planning “never exists in concentrated or integrated form but solely as dispersed bits of...knowledge which all the separate individuals possess” (Hayek 1948, 77). Pigovian welfare economics rests on a general-equilibrium analysis of the economy. But in order to know the “correct” price-output combination in any one market where the tax is to be applied, the analyst must have the same information for all markets. As attested by an ardent supporter of such taxes, “The general equilibrium model of resource allocation which underlies formal welfare economics represents...a general analysis of the interrelationships of markets throughout the economy...it requires knowledge of the structure of preferences of all consumers and the technologies available to all producers” (Kneese 1977, 57).

Because the data required to manipulate markets as prescribed by the theory are impossible to gather, and the efficient outcome therefore impossible to identify, in practice the model serves merely as “cover” for those seeking to manipulate markets for various purposes.⁸ Because there is no real standard by which the adequacy of the data can be gauged, the Pigovian approach to dealing with environmental problems has given rise to a frenzy of green-tax proposals, all claiming to promote economic efficiency.

The most famous, or notorious, of the green-tax proposals was President Clinton’s ill-fated BTU tax. Although one may suspect that the real purpose of the proposal was to fatten the U.S. Treasury, its supporters touted the tax as a weapon in the battle against global warming. The proposal was a case study in the methods of MBE. An environmental goal was established: reduction of carbon dioxide emissions into the atmosphere. No evidence was presented that human welfare had ever been impaired by CO₂ emissions (Michaels 1992). Further, the global warming hypothesis—that at some unspecified future date such emissions will harm humans—has been accepted by only a small minority of atmospheric scientists. But proponents forged ahead. A 1990 Congressional Budget Office study, which helped to set the stage for the BTU tax proposal, candidly noted that “although there is great uncertainty about the extent to which such global warming is likely to occur, what its effects might be and the costs of efforts to slow the progress of warming, the potential consequences have led to calls for immediate action” (ix). In other words, regardless of the science or the economics, supporters voiced “calls for immediate action.” Ultimately, all such tax schemes promote the goals of the politicians and interest groups supporting them.⁹ As with the BTU tax,

8. For example, the same model is invoked to justify increasing taxes on tobacco.

9. Public choice analysis maintains that politicians and bureaucrats, even if they possess the information necessary to improve social welfare, support laws and regulations that help them achieve their own goals and the goals of their political supporters. For a classic case study of environmental policy making along these lines, see Ackerman and Hassler (1981).

they have the added effect—fortunate in the eyes of many of their advocates—of increasing federal revenues and expanding government control over the use of productive resources.

Tradable Permits Are Not Property Rights

Taxes are one tool in the kit that advocates of MBE carry to the policy making table. Another is tradable permits. Whereas green taxes alter prices in order to affect resource use in accordance with political desires, tradable permits serve as “property rights” for the same purpose. In advocating tradable permits, environmentalists again have taken their cue from ideas originally put forth by conservative economists. Working along lines laid down by Ronald Coase (1960), these economists have emphasized correctly that many, if not all, genuine pollution problems arise from a lack of property rights in the use of resources.

Coase argued that if property rights are clearly defined and well enforced and can be cheaply exchanged, then parties can resolve pollution problems by bargaining. When Coase’s conditions are met, there is no need for a cumbersome regulatory apparatus or a government bureaucracy to create an efficient allocation of resources. The “Coase Theorem” does not tell us what the efficient outcome should be. This intellectual modesty distinguishes Coase’s argument from the argument of those who invoke his analysis to justify MBE. Although Coase’s argument is sound, it says nothing about the nature of property rights, requiring only that once established, they should be freely tradable. Unfortunately, Coase’s ideas have been imported into environmental policy debates, not to expand property rights but to justify the rearrangement and restriction of existing rights.

The now-standard approach of the advocates of MBE goes as follows. First, they identify something as excessive, for instance, the amount of waste going into landfills or the amount of fossil fuels used to generate electricity. Then, they arrive at an amount acceptable to the relevant politicians and special interests. To realize this amount, they take away the existing right to engage freely in the activity and then allocate new rights such that the total amount of the activity does not exceed the politically determined target. The new, more restricted “rights” take the form of a specific number of permits, each of which allows an individual or firm to engage in a certain amount of the disfavored activity. Holders of permits may buy or sell them. Holders therefore have a financial incentive to reduce the amount of their own disfavored activity. If a company can reduce its restricted activity sufficiently, it can obtain revenue by selling its unnecessary permits. To reiterate, the objective is not to advance free markets as such but to “harness market forces” to achieve a politically determined goal.

Tradable permits to pollute are the most commonly espoused form. But other forms are also advocated, where no specific pollution or emission is involved, most notably to promote recycling and to create a market for recycled materials where otherwise none would exist. With respect to pollution permits, which were adopted as part of the 1990 Clean Air Act Amendments, Stavins and Whitehead (1992) describe the system as follows:

[T]he government establishes an overall level of allowable air pollution and then allocates permits among the firms...in a relevant geographic area so that each firm is allowed to emit some fraction of the overall total. Firms which keep their emissions below the allotted level may sell or lease their surplus permits to other firms or use them to offset excess emissions in other parts of their own facilities. (6)

One may argue that such schemes simply establish property rights to the use of air. And after all, doesn't air quality suffer because no one owns—and therefore protects—the air? Yes, but the real problem is not air quality as such. The real problem is that emissions eventually land on someone's property. In the cement-dust example, problems arise not because the dust is emitted but because it touches people's cars, houses, laundry, and lungs. Tradable pollution permits that might be issued to the cement factory could, depending on the permissible level of emissions and the prevailing cost conditions, still fail to prevent the factory from impinging on the property rights of people nearby. Robert McGee and Walter Block (1994) have argued forcefully that such permits are simply licenses to violate rights and therefore inconsistent with free markets. They maintain that "perhaps the major fault with trading permits is that while they allow market forces to allocate resources, they entail a fundamental and pervasive violation of property rights" (57).

A truly free-market approach would allow the damaged parties to sue the offending parties for remedies rooted in a stricter enforcement of property rights. Plaintiffs would seek either compensation for damages or some form of injunctive relief. Another alternative would be a Coasean solution: the cement companies would purchase the relevant rights from the affected parties.

If a tradable permit implicitly grants the polluter the right to disregard the property rights of others, it is clearly inconsistent with a free-market economy. On the other hand, if a polluter's production activities do not violate the property rights of others, no problem exists and no policy action

is necessary.¹⁰ Tradable permits have been advocated increasingly in the latter setting, where no one's rights are being violated but where an activity is deemed harmful to the environment per se or otherwise aesthetically displeasing.

One such instance pertains to setting recycled-content standards for production processes, as advocated by the Progressive Policy Institute's Mandate for Change:

[T]he government would set an industry-wide...recycled content standard which individual firms could meet in one of two ways: They could use the required percentage of secondary materials or they can use fewer secondary materials and buy permits from other firms that exceeded their recycling requirements.... Recycling credit systems could be...used for a variety of products, including newsprint and used lubricating oil. (Stavins and Grumbly 1993, 211)

The sole purpose of this policy is to promote recycling and reductions in landfill usage for their own sake. In the market, producers and consumers are rejecting many recycled materials as less desirable than virgin materials. Recycling advocates complain that "as more states and municipalities have adopted recycling programs, the increased supply of recovered materials has often outpaced demand for recycled or secondary materials. In some instances, this glut has resulted in the subsequent landfilling of separated, recyclable materials" (Stavins and Grumbly 1993, 211). Instead of reaching the obvious conclusion, recycling zealots support tradable permits as a scheme for forcing trash onto a resistant market.

Conclusion

Hayek (1967) argued that in a free society the "rules of just conduct" need to be "ends independent" (160–77). Legal arrangements should not favor the goals or purposes of some individuals or groups over others. Instead, such rules should be structured so that they maximize each individual's chances of accomplishing his own goals. Hayek also argued that once it is decided that a liberal social order is desirable, the propensity of policy makers to predetermine specific market and behavioral outcomes must be stifled, as liberty conflicts inherently with deterministic public policies. The rules

10. Arguably this was the case with the 1990 Clean Air Act Amendments, which instituted tradable permits with respect to emissions associated with the generation of acid rain. Prior to passage of the statute, studies demonstrated that many of the harms allegedly caused by acid rain either did not exist or were much less severe than originally thought (Krug 1990). If acid rain harms northeastern lakes as some allege, a free-market remedy would consist of holding the offending utility companies responsible for damages, possibly by requiring them to pay for liming the damaged lakes. This action also would be much less costly.

“should consist solely in prohibitions from infringing the protected domain of each which these rules enable us to determine. Liberalism is, therefore, inseparable from the institution of private property” (165).

Hayek’s guidelines point toward a true free-market approach to environmental issues. We must establish rules of conduct that clearly define people’s rights, their “protected domain.” The primary goal of all public policy, including environmental policy, should be the enforcement of rights once they are clearly defined. There is no proper role for the “ends-dependent” policies of the market-based environmentalists. As evidenced by Stavins and Grumbly’s view of industries that fail to incorporate the “right amount” of recycled materials in their production process, the purpose of MBE is to thwart free decision making and the results to which it gives rise.

In assessing environmental issues, alternative policy approaches have been incorrectly categorized. The primary choice is not between command-and-control and market-based policies. Instead, it is between free-market policies, based on clearly defining and protecting property rights, and socialist—or, perhaps more precisely, mercantilist—policies, based on furthering the societal and personal goals of politicians and special-interest groups.¹¹ The latter includes both command-and-control policies and those labeled “market-based.”

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11. For why mercantilism may be a more precise term, see Ekelund and Tollison (1981).

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