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REGULATION was first published in July 1977 "because the extension of regulation is piecemeal, the sources and targets diverse, the language complex and often opaque, and the volume overwhelming." REGULATION is devoted to analyzing the implications of government regulatory policy and the effects on our public and private endeavors.

For the Record

An Update on E-Z Trial

In previous issues of *Regulation*, I expressed my concern about the failure of the Occupational Safety and Health Review Commission (OSHRC) to conduct an independent survey of the fairness and efficiency of its pilot E-Z Trial program for small employers facing alleged OSHA violations, before permanently adopting E-Z Trial. [See "*OSHA Review Commission's E-Z Trial: Backdoor Authoritarianism?*" *in* Regulation, *Vol. 21, No. 3, and "For the Record," in* Regulation, *Vol. 22, No. 3.*]

I am pleased to relate that the chairwoman of OSHRC has authorized an independent survey to evaluate the fairness and efficiency of E-Z Trial. The Conflict Resolution Institute at Indiana University is conducting the survey.

VELMA MONTOYA
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Revisiting "Market Failure"

A READER'S OBSERVATIONS

On Transactions Costs In "The End of Market Failure" (*Regulation*, Vol. 23, No. 2) Richard O. Zerbe Jr. and Howard McCurdy discuss some aspects of transactions costs. They give the example of one party producing $125,000 damage by pollution, which could be eliminated by the expenditure of $100,000 on pollution-eliminating equipment. They go on to say that if the transactions costs are less than $25,000, one could expect efforts to eliminate the externality to ensue.

In fact, I think that they have omitted a predicate. Efforts to eliminate the externality will occur in the manner and for the cost described only if well-defined property rights have already been established, so that the producer of the pollution has the right to emit such pollution. If he has that right, the only recourse by the injured party is to pay to have pollution equipment installed in an attempt to save the $25,000. If the polluter does not have the right to pollute (or if rights are not well established), the party being damaged to the tune of $125,000 would have an incentive to try to eliminate the pollution through legal methods, as long as the expected costs of the solution are borne by the polluter and the costs of a lawsuit or lobbying effort are either less than $125,000 or are expected to be reimbursed (as in a lawsuit where the loser pays court costs).

Using this approach, which to me seems appropriate most of the time, given the nebulous status of rights to pollute, the case for "market failure" could only be made using the higher value. Thus, the failure to stop the polluter from polluting would imply expected transactions costs of more than $125,000 rather than transactions costs of more than $25,000.

On Law Enforcement A second area of the article about which I have a question relates to statements about the advantage that governments have in law enforcement. Although the authors may well be correct, this section of their article is not referenced. Perhaps it is another fable of the bees or of the lighthouse? Indeed, a recent book (*To Serve and Pro-*

We welcome notes about current regulatory topics, letters that challenge or expand upon material we have published, and replies from authors. The writer's name, affiliation, address, and telephone number should be included. We cannot publish all the letters we receive, and we may reject any letter at our discretion. We may edit letters for length, clarity, and conformity to our editorial style.

tect: Privatization and Community in Criminal Justice, by Bruce Benson) suggests that in some situations (and perhaps in many others) privatization of policing may well be cost effective.

On Dispute Resolution Surely the authors realize that the notion of Microsoft having policing and court responsibilities is a strawman argument. In the 1950s, one could have argued that the government's monopoly on delivering mail should continue because Nabisco could not be trusted to do so. Of course, 50 years later we now have lots of private mail delivery, ranging from Federal Express and UPS to instantaneous (and almost free) e-mail services.

The authors are indeed correct that no group could legitimately unilaterally proclaim itself policeman and jury, but certainly there should not be anything wrong with parties contracting to allow certain disputes to be resolved using nongovernmental institutions.

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IN REPLY

Mr. Weingarten makes three observations about "The End of Market Failure": property rights are important in reducing transactions costs, the government's advantage in criminal law enforcement may be illusory, and privatization may yet be efficient in areas not yet recognized. My co-author and I agree with those observations.

Mr. Weingarten correctly points out the importance of well-established property rights in reducing transactions costs. But even without property rights specified there will some relevant (higher) level of transactions costs. Thus, our example works whether or not property rights are specified, as it just assumes some arbitrary transactions costs. The point is that having well-specified property rights reduces transactions costs—a point with which we agree.

> The point of our article is that there is no case for market failure; what appears to be such failure is just a reflection of costs.

Mr. Weingarten also correctly points out that whether or not the polluter should have the right to pollute depends on the effect of the assignment of this right on transactions costs. He appears to assume, however, that it is best if the polluter has the right to pollute, and that negotiations proceed from there. Transactions costs, however, may well be less if the polluter does not have the right to pollute. In this case, the polluter may well unilaterally install pollution-eliminating equipment without negotiations or suit. In any particular case the right answer to the allocation of liability will depend on a number of detailed considerations.

We disagree with Mr. Weingarten's example of market failure in an important sense. The point of our article is that there is no case for market failure; what appears to be such failure is just a reflection of costs. There is a case for reducing costs, whether by specifying property rights or reassigning liability so as to reduce costs, and so forth. Those who would talk of market failure should just talk about their proposal to improve the situation, whether it involves more or less use of markets.

Finally, we are happy to agree that in some cases, and perhaps in many, privatization may be more efficient. We have no more reason to trust government than to trust Microsoft. Our argument is simply that in some cases the costs of monitoring government might be less than the costs of monitoring Microsoft—indeed this criterion can be made a sort of definition of government.

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