

lations Act and impose a federal contract in interstate commerce that would avoid the state-by-state adjudication under fifty systems of law. I think we're at a time when we can't afford to have state-by-state contract regulation of interstate commerce.

ELIZABETH BAILEY: I would like to mention one other source of the airline reregulation that's occurring. The key problem is that deregulation has been a success for the public, but definitely not for labor. For example, new airlines like People Express and New York Air are paying jet pilots less than half of what the established airlines have to pay under their very generous contracts with labor. Airline labor enjoyed enormous rents under regulation, and those rents are being eroded in a deregulated environment.

I think this helps explain the "Christmas tree" package being hung on the CAB sunset bill, especially the introduction of a labor hiring-hall provision, where airlines have to give preference in hiring to personnel that other airlines have let go. It also helps explain what's happening at the ICC. Labor is moving there to block deregulation, because the rents to the drivers who are unionized are clearly enormous. So we shouldn't be too hard on the Reagan administration. Any administration will respond to groups that display a great deal of dissatisfaction. The pressure was not so strong a few years ago when labor didn't fully realize how much deregulation would reduce its rents.

MARVIN KOSTERS: I think that's an important point, but there are differences in viewpoint about whether that's a cost of deregulation or a benefit. [Laughter.]

ALFRED KAHN: I'd like to add a word here, by way of underlining Betsy's and Marvin's observations. There is no doubt that certain labor groups profited greatly from regulation. But there were others who were injured by it, and who are benefiting now from deregulation. In that second group I would include the long line of people who were applying for pilots' jobs at

those \$80,000 to \$100,000 salaries and couldn't get them, and who are now working for one of the new airlines at \$15,000 to \$30,000.

It's very much like the situation in the auto industry. The auto workers' wages and fringe benefits increased much more rapidly than average manufacturing wages during the decade of the 1970s—because for most of that period the auto industry was inadequately competitive. At whose expense?

Well, one very large group of people who were exploited are the unemployed auto workers, who would have kept their jobs if wages had been lower. So it's particularly distressing that as Japanese imports intervened to make the industry more effectively competitive and imposed some discipline on those wages, the Reagan administration stepped in and exerted pressure on the Japanese government to limit that healthy influence. ■

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## The Environment

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Robert W. Crandall

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**T**HERE'S NOT MUCH to be said about the substance of President Reagan's environmental policy because, frankly, very little of substance occurred in the first twelve months. Instead, I can only comment on the tone which has been set and the apparent lack of direction in major policy areas. Let me begin with a quote dated October 12, 1981—a little old, perhaps, but still a useful measure of the impression being created by Reagan's Environmental Protection Agency (EPA).

In the ten-year history of EPA, there have been periods of turmoil, but none rivals what is happening now under the reign of Anne Gorsuch. What was once a robust, dynamic entity has shriveled to a gray shadow of its former self, wracked by internal dissension, run by people with little expertise in environmental issues, and dogged by a paranoia that has virtually brought it to a standstill.

Now, that statement is not from the Environmental Defense Fund's house organ or from Ralph Nader. It's from *Automotive News*, a pro-business trade publication—part of Reagan's own constituency.

And, in my judgment, the statement rather accurately portrays the confusion and paranoia that has developed at EPA in the past year. The

agency's new leadership can fairly argue that the policies it inherited were so confused and inefficient that more than one year (or one administration) will be needed to straighten them out. Nevertheless, that leadership can't duck blame for the likelihood that the agency is now in such a state of disarray that it will not be able to recover even in the next three years. It is also worth noting that EPA Administrator Gorsuch and Interior Secretary James Watt are doing wonders for the membership drives of organizations like the Sierra Club. In fact, it appears to me that they are helping greatly to rearm the GOP's opposition for the next electoral battle.

Instead of serving up fodder for the environmentalists, the Reagan EPA could have used its first year to great advantage. The political climate was favorable for launching major changes in environmental programs and even in federal environmental statutes. By now, however, the administration's EPA appointees have so tarnished their credibility that I do not expect to see significant legislative changes any time soon—particularly with congressional elections coming up this fall.

Had the administration been ready and willing in early 1981, it surely should have been able to launch a major assault on the more

outrageous provisions of the Clean Air Act. With the act's reauthorization deadline coming up in September, air pollution policy was clearly on the political agenda. Thus, a proposal to accelerate the shift away from a cumbersome Gosplan approach and towards market incentives—a shift begun tentatively four years ago—would certainly have been welcome. There are people in California and on EPA's staff who would have been eager to help out. Just changing a few provisions of the Clean Air Act and nudging the bureaucracy at EPA would have been sufficient to save billions of dollars in control costs without sacrificing clean air goals.

That the administration did not even propose legislation to amend the Clean Air Act in its first year suggests a faint-hearted approach to environmental policy making. EPA spent months drafting legislation, but a draft was leaked to the Congress and subsequently disowned by the White House. As a result, the administration offered only eleven vague "principles"—and seemed to retire from the battle.

The foggy, politically timorous "principles" are unlikely to provide any impetus to congressional efforts at Clean Air Act reform. Take the following areas:

- We have by now considerable evidence that the auto emissions standards should be rolled back somewhat—that we have gone too far in attempting to control photochemical smog and CO from automotive sources. Despite this evidence, the Reagan administration, after a few stumbles, simply announced that it supports setting automobile standards at "more reasonable levels"—and, by refusing to provide details, gave Congress a perfect excuse for inaction.

- Another obvious target for change is the requirement that electric utilities install stack-gas scrubbers on all new coal-fired boilers, no matter how small the sulfur content in the coal they burn. The administration has meekly suggested that "uniform emissions standards" replace this inordinately expensive and counterproductive requirement.

- We know that the existing standards requiring uniform air-

pollution control technology in new industrial facilities inhibit new investment and prevent the introduction of market incentive systems. But, incredibly enough, the administration seems to want to keep uniform technological standards.

- The administration's commitment to cost-benefit analysis should also have led it to propose changing the absolutist nature of the ambient air-quality standards in the Clean Air Act. At present, these standards must be set at a level that protects the health of the most sensitive groups in the population, apparently without regard to cost or the degree of health impairment. Given the evidence that the dose-response relationship for most pollutants has no sharp threshold, this requirement cannot be met by any standard other than zero pollution. One cannot even imagine how a standard like that could be implemented. Adopting some form of cost-benefit test would set our entire air-pollution program on a more rational course. But the administration supports the existing statutory provision, apparently believing that deceptive standards-setting or a goal of zero pollution is better than rational cost-benefit analysis.

Moving on to more general matters, a reform-minded EPA leadership would have immediately given increased attention to improving the agency's monitoring and enforcement system. It seems ludicrous to me that we regulate air and water pollution extensively without being able to tell whether the regulation is working. Moreover, not only is EPA's monitoring of individual sources and ambient levels of both air and water pollution pathetically weak, but its enforcement system allows political capriciousness.

The Reagan EPA should also have begun to devise a research program aimed at identifying the important priorities for regulation. The agency cannot possibly carry out its bulging legislative mandate in full, and it cannot proceed rationally with a more realistic agenda without some priority-setting system. Unfortunately, EPA has never integrated its research with the design of new regulations, and indeed

has long displayed a cavalier attitude toward research. In the Carter administration, for example, EPA's research director presided over a questionable study on chromosomal damage at Love Canal and then deflected criticism by asserting that the results were only intended to be used in a court proceeding.

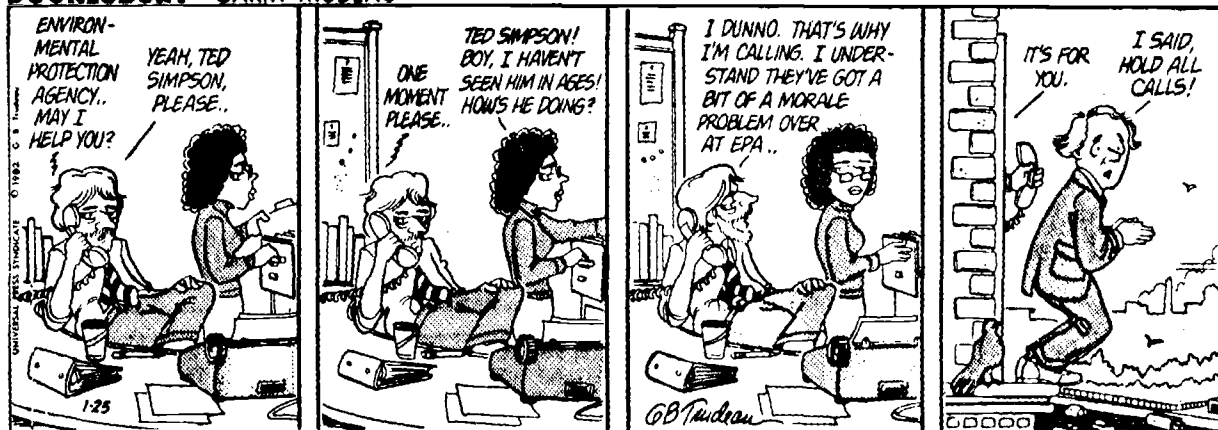
At present, EPA seems intent only on shifting some of its responsibilities to the states and attracting the President's attention by winning the budget-cutting sweepstakes. Clearly, the agency could operate on a lower budget if it shed some of the detailed regulatory responsibilities that various statutes have forced upon it and moved towards greater use of market incentives. But this does not appear to be the direction in which the Reagan EPA is headed.

Congress has clearly forced the agency (and OMB) to continue its pork-barrel programs. Its ridiculously inefficient sewage-treatment grants to local municipalities to pay for gold-plated facilities whose costs far exceed their benefits continues on far too grand a scale. And the hazardous-wastes program, involving the expenditure of "superfund" revenues collected from chemicals producers, is proceeding apace after an early attempt by the current EPA leadership to drag its feet.

The recent interest in Administrator Gorsuch's proposed budget and staff reductions has distracted attention from the real issues in environmental control. Better monitoring, improved research, and some modifications in environmental statutes could provide both budget cuts and improved environmental policy, particularly if the cuts were taken in the wasteful pork-barrel programs described above. Instead, the agency appears directionless—buying time while sending out signals to business of a new cooperative attitude.

There is enormous room for improvement at EPA. Study after study documents the inefficiency of the current regulatory approach and its lack of enforceability. If the new federalism were accompanied by an attempt to simplify the traditional air and water pollution programs through the use of market incentives, while improving moni-

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toring and enforcement techniques, the agency could contribute substantially to both regulatory reform and regulatory "relief." Unfortunately, little attention seems to be devoted to market incentives after the push given to them during the Carter administration. Leadership in the new federalism for environmental policy will apparently have to come from states such as California and Maryland which seem intent on exploring the greater use of market incentives.

Research on monitoring techniques, health effects, and other costs of pollution is more appropriately funded at the federal level, given the wide application of such research across the states. In this area, sad to say, there appears to be little or no movement. It would not be surprising if, in another ten years, we approached the setting of the smog standard by citing again an unreplicated study from the 1950s as the basis for concern that smog aggravates respiratory diseases. Nor would it be surprising if advocates for tighter or looser air-quality controls based their arguments on the results of monitoring just fifty-one sites across the country. With this kind of information, sensible policy is at best the result of a lucky guess.

The turmoil described by *Automotive News* is most apparent in EPA's personnel policy. Administrator Gorsuch's two top aides have already resigned. The head of the agency's research division has not even been named, despite the new leadership's calls for more attention

to research. And most of the appointments made to date are industry people with little understanding of the issues.

IN SHORT, there is little to report, but much to lament in the first year of the Reagan administration's environmental policy. Though they may not admit it, the environmentalists have much to cheer—they have a new and ever so vulnerable target to shoot at in 1982 and 1984.

### Discussion

BRUCE YANDLE: As between the two extremes of going full steam ahead with reforming environmental regulation or being dead in the water, I wonder if there might not be some relative benefits to the latter. For one thing, there are some scattered indications that a few states are doing rather innovative things. The state of Maryland, for example, is moving to a marketable permit program for air emissions and Wisconsin already has in operation a marketable permit system for controlling effluent discharges on the Fox River. Now, these may be the only two cases in existence, but they may mean that all is not lost in terms of getting efficiency-enhancing programs.

Second, we may get some help from another quarter. The frost belt states have of course been supporting strict new-source standards for competitive reasons. But as industry continues to move to the sun belt, an equilibrium will be reached,

so that both regions will be similarly affected by the standards. In other words, all those old plants will be new plants. And the frost belt won't want higher new source standards then.

Perhaps these two things together offer some prospect for more efficient regulation?

MR. CRANDALL: To respond to your second point, first, Bruce, I would ask if you've been in a passenger train or a steel mill recently. It's by no means clear to me that all of the nation's steel plants and railroad facilities will be new any time within the next few generations. I don't want to wait that long for the needed change.

I agree, however, that our best chances for regulatory reform in certain environmental areas, particularly in air pollution policy, come from the states. Probably, responsibility for environmental regulation belongs with the states anyway, and most of it ought to be returned there. Unfortunately, the administration is not really pushing that way. Its talk about a "new federalism" really sounds more like a desire to ease enforcement than a call for decentralization.

But let me stress that in order to implement some of the innovative procedures in transferable permits, we must first get rid of the new-source standards required by the Clean Air Act. California and Maryland are going to have difficulty getting around those requirements. And certain frost belt states will insist on enforcing them.

GEORGE EADS: I agree with Bob that a great opportunity for proposing fundamental changes in some of the environmental statutes has been missed. . . . Before Anne Gorsuch it was a close argument between the environmentalists and the economists as to whether to amend the Clean Air Act. The environmentalists would argue that we economists might gut the act, and we would insist that we'd act responsibly. But

now all they have to do is ask, "How will Gorsuch administer a Clean Air Act that gives her more flexibility?"—and that's the end of the argument. Reformers can't get anybody to listen, even in the Republican-controlled Senate. So, I doubt there's any point now in trying to get the administration to change its position and propose amendments. I don't think they would be seriously considered on the Hill. ■

Deregulation and Monetary Control Act of 1980. Since this act added more regulation than it repealed, its title shows, I guess, that Congress does not apply a truth-in-labeling standard to itself.

The deregulation consisted mainly in the provisions affecting interest rate ceilings on checking accounts and on time and savings accounts, sometimes and a bit inaccurately lumped together as Regulation Q. The ceilings on time and savings accounts are supposed to be phased out over six years by the Depository Institutions Deregulation Committee, a new regulatory body composed of the heads of the banking agencies. So far this committee has been moving in less than giant steps. After eighteen months of meetings, it decided in September 1981 to raise the passbook interest rate ceilings by half a percent. At that pace, with market rates then around 16 percent and passbook rate ceilings fixed at a little over 5 percent, it would have taken quite awhile to catch up. But even that was too fast for the S&Ls: the decision was rescinded in November. At the committee's present pace, it won't finish the job in sixty years, let alone in the six required by the 1980 act.

On checking accounts, the liberalization was more decisive. The act largely repealed the ban on the payment of interest on checking accounts by authorizing nationwide NOW accounts beginning in 1981. A NOW account is a way of paying checking-account interest without admitting that that's what you're doing.

The other deregulatory action was somewhat ambiguous. The act displaces state usury ceilings on mortgages and business loans—once again we've had to learn that when usury ceilings "bite," the effect is not cheaper loans but no loans—but the act goes on to authorize the states to reinstate usury ceilings simply by voting to do so.

As to the other areas of bank regulation, there has been talk, importantly at the Treasury, but very little definitive action.

In the area of product restrictions, for example, the Reagan administration is supporting a bill that would allow banks to under-

## Financial Institutions

*Kenneth Scott*

**T**HE BANKING INDUSTRY would seem a promising field for deregulation, if promise is indicated by the quantum of regulation that you can find in an industry. Commercial banks, savings and loan associations, mutual savings banks, and the like must be among the most fully, indeed exhaustively, regulated businesses in the land.

There is product regulation restricting the kinds of services banks and bank-holding companies can offer. There's a lot of regulation of geographical markets—entry, branching, whether a firm can operate across state lines. There is the extensive and traditional area of safety regulation designed to protect bank depositors, or perhaps it's the Federal Deposit Insurance Corporation (FDIC) or the Federal Savings and Loan Insurance Corporation (FSLIC) that is being protected. This includes portfolio regulation, liquidity requirements, interest rate ceilings, capital adequacy requirements, and so on. Finally, over the last decade and a half, there's been a vast growth in consumer regulation, aimed at protecting borrowers I suppose, consisting of rules on bank advertising and disclosure, truth-in-lending, and specification of the substantive terms of loan instruments in general and various mortgage instruments in particular. All of this has been added to long-standing usury regulation of lending rates.

There have also been some stirrings of regulation that can be seen as an effort at credit allocation favoring one group of borrowers over another. The Federal Reserve Board engages in this from time to time when it urges member banks, which might want to get loans from the discount window, to avoid undue increases in business credit or speculative credit or something else that's out of favor at the moment. Congress has gone further with its Community Reinvestment Act which, if it's understandable at all, has to be understood as an awkward first attempt to subsidize certain groups of borrowers: inner-city borrowers, minority borrowers, or somebody.

So with all of this regulation out there—and that's not all of it—what progress has been made? Well, a bit. The bank regulatory agencies, for example, have been engaged since 1977 in an effort to simplify some regulations and procedures, a project to which the Fed gave the literate but intimidating title of Project Augeas.

It's a minor achievement. Every time you simplify, you make the newcomer's access to that body of regulatory material perhaps a little easier, but for everybody already in the business what you mainly do with the new wording is introduce new uncertainties.

A more recent and more notable step is the Depository Institutions