
Letters

We welcome letters from readers, particularly commentaries that reflect upon or take issue with material we have published. The writer's name, affiliation, address, and telephone number should be included. Because of space limitations, letters are subject to abridgment.

Don't Bury the Newborn

TO THE EDITOR:

First, we disagree with some of Dr. Johnston's critical assertions about trading in the South Coast Air Quality Management District (SCAQMD). Second, the article contains critical errors that need to be corrected. As co-sponsors of the Clean Air Auction (with Cantor Fitzgerald, L.P.) and being responsible for well over half of the pounds traded to date, we feel obligated to help set the record straight.

In his article, Dr. Johnston criticizes the Regional Clean Air Incentives Market (RECLAIM) adopted by the SCAQMD based on the **first six months** of RECLAIM's seventeen-year life. Dr. Johnston intimates that the RECLAIM program is "substantially flawed" and throughout the article leads a reader to conclude, in a number of ways, that RECLAIM is an abject failure. Asserting that the RECLAIM program is a failure is akin to turning out the lights on Eastern Europe's struggle for democracy within a year of the fall of the wall. Recognizing that there is

room for RECLAIM to improve, we assert that it is difficult to review and condemn a regulatory program based on the passage of six of the 204 months of its life.

In his critical assessment of RECLAIM and trading, Dr. Johnston highlights the example of a RECLAIM transaction between Union Carbide Corporation (seller) and Anchor Glass Container Corporation (buyer) involving more than 1,700 tons of NO_x RECLAIM Trading Credits (RTCs) and more than \$1.2 million. Dr. Johnston's assessment, however, includes inaccurate information. First, the author points out that this transaction involved an average price of \$700/ton of NO_x RTCs (in 1994 dollars). This price is then compared to the SCAQMD's projected price of \$577/ton (in 1987 dollars). To make an accurate comparison, the author should have at least compared the \$700/ton price to a SCAQMD price projection in 1994 dollars, e.g., \$759/ton.

However, the error is compounded when the author incorrectly asserts that the trade was only for RTCs usable in 1994. In fact, the trade involved a stream of RTCs for use to the end of the program. All of sudden, Anchor Glass looks like they got a veritable bargain! Where the SCAQMD projected that a stream of RTCs beginning in 1994 and ending in 1999 would sell for \$60,212, in 1994 dollars

(\$39,873, in 1987 dollars), Anchor paid only \$4,200 in 1994 dollars—less than one tenth of the projected price. RTC prices established in 1994 are well below many price projections, making market participation a profitable investment.

A related error is made in asserting that the total quantity traded in this transaction was 4.5 percent of the initial allocation (i.e., the allocation useable in 1994). In reality, the trade only involved 0.3 percent of the 1994 allocation—the balance came from out years (e.g., 1995 through 2010).

Dr. Johnston indicates that trading thus far "has been modest, to put it charitably." In actuality, trading has been rather robust. Inclusive of the Anchor Glass/Union Carbide trade, we are aware of at least sixteen trades that have involved more than 4.5 million pounds of RTCs. This total includes those that went through the Clean Air Auction held in July, as well as a number of trades that occurred before and after the auction.

In summary, it concerns us that outside observers are so quick to bury the program and condemn the work of its creators. At the very least, critical analyses, of which the author's article is not the first (nor will it be the last) should be founded on the facts. The RECLAIM program is in its infancy. The market is just beginning to sort itself out. Those industries included in it are struggling to move away from the traditional mode (*we'll only do what you tell us to do, when you tell us to do it*) and into one where clean air objectives become inextricably tied to business principles (*we can't afford to invest in anything but the most cost-effective solution*).

Let's hold off on burying the newborn and take another look at the baby in a few years. We believe that, with a bit more perspective and when equipped with the facts, Dr. Johnston will agree that RECLAIM will result in clean air at a lower cost.

Josh Margolis
 Director, Air Trade Services
 Dames & Moore

Robin S. Langdon
 Analyst
 Dames & Moore

Rumors of the Demise of RECLAIM "Greatly Exaggerated"

TO THE EDITOR:

James L. Johnston in his article "Pollution Trading in LA LA Land," calls Southern California's Regional Clean Air Incentives Market (RECLAIM) program "substantially flawed" and, based on this conclusion, wonders how "anybody should have expected a government attempt at inventing a market to succeed." But, to paraphrase Mark Twain, the rumors of the demise of RECLAIM are greatly exaggerated. While there are some flaws with the design of RECLAIM, this program should, nevertheless, result in Los Angeles reaching its emissions reduction goals more cost-effectively than with traditional command-and-control approaches. The RECLAIM program is the latest adaptation of incentive-based strategies to implement environmental policy, following the model implemented in Title IV of the 1990 Clean Air Act. Based on early returns from this program, the federal government indeed appears to have succeeded in "inventing a market" that works well. Trading of

allowances for sulfur dioxide emissions from power plants is occurring through both EPA's auction market and privately, and current prices for SO₂ permits are lower than forecast. Many utilities are switching fuels to avoid purchasing permits, a strategy analysts had hoped this program would promote by giving utilities more flexibility in their abatement responses.

Johnston's pessimistic prognosis for RECLAIM is predicated on several assertions. One is that because RECLAIM trading credits have been denied property rights status, trading will be limited and emissions reductions will come primarily from an exit of firms from the L.A. area. We take issue with these ideas. Considering property rights, there is nothing the government can do to surrender its statutory responsibility to protect human health and welfare. It can not commit future regulators *not* to change the rules of the program. Hence, one can not be assured an irrevocable property right in a constitutional sense, though there is a government-defined, intangible property right involved. The RECLAIM program deserves credit for its unusually honest advertising about its own limitations. To claim otherwise would be unenforceable. The important test is whether there is a proclivity toward a stable system of rules and a process that ensures rule changes will be well considered. RECLAIM is well designed on this score.

The notion that many trades must take place for a market to "work" confuses process with objectives. The objective is to reduce emissions to a given level cost-effectively, not to have lots of "action" in the market (although the latter is generally a sign of a healthy market). This objective may be reached by "trades" within a given plant, by "trades" across plants owned by the

same company, or by trades across companies. Only the last would actually show up as bona fide trades. In addition, the prospect of having to pay another company for permits to emit pollutants may spur companies to rethink their decisions about production processes and their capital investment and retirement plans, and make other adjustments that reduce demand for such permits. These activities would not show up as trades. Furthermore, to get RECLAIM off the ground, the South Coast Air Quality Management District (SCAQMD) needed to issue "excess" permits in the initial years of the program to keep political opposition and prices down. Combined with the one-year lifetime of the permits, these low prices discourage trades in the earliest years. As the excess supply of permits is eliminated over time, market activity may pick up. In any event, the pace of trades has no necessary relationship to cost-effectiveness.

We think that Johnston presents confusing arguments on a number of other important points. He laments the high cost of obtaining NO_x and SO_x emissions reductions and that the health benefits have not been shown to outweigh the costs. As one of us is on record questioning the net benefits of L.A. attempting to reach the current National Ambient Air Quality Standard for ozone, we are sympathetic. But, these concerns are besides the point. Emissions trading is a tool for cost-effectiveness—to meet a goal at least cost. It has no implications for the appropriateness of the goal and should not be judged on these terms.

One characteristic of RECLAIM which Johnston criticizes is the fee that is charged on permits owned by a firm, and which covers the administrative costs of running the new system. Johnston likens charg-

ing the fee on permit holdings to tipping the executioner to bring death quickly. But doubtlessly many in industry feel they are better off with the current arrangement, including paying the fee than they would be under a command-and-control alternative. On net, RECLAIM brings more flexibility and lower compliance costs than the command-and-control alternatives. Thus, the fee may be seen as paying for a public good, albeit one shared by a narrow group—the firms emitting NO_x and SO_2 —rather than the public at large.

Further, Johnston claims that the fee undermines the efficiency of the program. Clearly the fee has little, if any, negative implications for efficiency. There are no theoretical reasons for distributing the permits for free. If markets are perfectly competitive, the fee is irrelevant for efficiency as firms will price at their marginal opportunity costs irrespective of how permits are distributed. If markets are not competitive, there is an *advantage* to charging a fee because it forces firms to better recognize the opportunity costs of their emissions.

As for Johnston's call for a "neutral fee, such as a lump-sum levy which does not affect the firm's marginal costs," this is the last thing the doctor would order to promote economic efficiency. That fee would just be a tax on polluters without regard to their effort to control emissions.

One attribute of a tradable permit system is that it allows firms "dynamic flexibility," i.e., the flexibility to delay major capital investments until they are justified economically. The value of this attribute is quantified as an "option value." Mistakenly, Johnston seems to want to subtract the option value from the estimated savings from trading, compared to command and control. If a firm acquires a permit,

it will have to pay for the option component. But since the option has value to the firm, it will be willing to pay for it. Command-and-control does not deliver a similar option, which is the main point of RECLAIM. The option value does not diminish the cost savings, but contributes to them.

While we view with favor the growing interest in and implementation of tradable pollution permit systems, the state of the art is still immature and, not surprisingly, RECLAIM has its problems. One of its most serious problems, as Johnston points out, is in defining permits with a one-year lifetime. This short life span encourages frantic scrambling for permits every year, raising the transactions costs for the system above what they would be if permits had longer lives. Further, the short life span discourages banking. Banking would lead to quicker clean ups in the early years of the program, while also reducing the cost of compliance, as firms use their bank as an insurance policy against eventualities that they otherwise would have to insure against.

Other concerns with RECLAIM include omitting mobile sources, consumer products, and small stationary sources; although including these sources would not be easy or costless administratively. And the program has not integrated systems for trading volatile organic compound (VOC) emissions and particulates although the SCAQMD does feature VOC trading within EPA's Emissions Reduction Credit program.

Nevertheless, RECLAIM represents a serious attempt on the part of SCAQMD officials, industry, and environmental groups to make markets work for the benefit of the environment and to reduce the intrusiveness of government. Free marketers, such as Mr. Johnston, often

see major problems in any government role in the economy, without closely considering the problems with alternative arrangements. Indeed, Johnston's article offers no advice on how the external costs of pollution are to be properly taken into account without government's intervention. There are some things that private markets cannot do or cannot do well, and, in most circumstances, forcing polluters to take into account the negative consequences of their actions is one of them. This is particularly true when those damaged are many but the damage is not very great to any one of them. Certainly Dr. Ronald Coase, whom Johnston invokes in his call against government intervention, would not count on the market for handling this type of problem. But RECLAIM takes a big step toward implementing the principles articulated by Coase, by pursuing cost-effective, incentive-based environmental regulation.

Alan J. Krupnick
Senior Fellow

Resources for the Future

Dallas Burtraw
Fellow

Resources for the Future

"A Rube Goldberg Instrument"

TO THE EDITOR:

James L. Johnston's discussion of Southern California's RECLAIM program is helpful to all who take the environment seriously. Those who truly value improved air quality in Southern California must surely want simple, low-cost policies that deal with real problems. Johnston's close scrutiny of the RECLAIM program suggests something else is going on. The environmental com-

munity must be appalled.

SCAQMD years ago made a name for itself in policy circles by introducing a simple and workable emission fee system, which Johnston discusses. At the time of its implementation, the fee was developed solely for revenue purposes. In the wake of the taxpayer revolt, the District, like other state agencies, was told to find revenue to support its operations. However, as the fee was raised in search of more revenue, the District learned about demand curves. Emissions went down.

What had been a revenue producer took on features of a workable emissions control fee. All who followed the evolution of pollution control policy learned some valuable lessons from SCAQMD's experiment: an appropriate level for an emission control fee is not necessarily the correct level for a tax revenue maximizer. Corollary: if the correct fee for limiting emissions to the cost-beneficial level does not maximize agency revenues, then the fee is too low.

The SCAQMD was also an early promoter of emissions offsets ratios, which could be manipulated to extract the last bit of emissions control from the stationary source community. What appeared to be a property rights solution that sparkled with efficiency gains for all parties became a device that could be used to maximize pollution reductions from stationary sources. Meanwhile, the lower cost option of buying out or randomly checking and banning dirty automobiles remained dormant. Not many offset transactions occurred.

Now the inventive SCAQMD has ventured forth with its own version of marketable pollution credits, which are not to be confused with property rights. But as Johnston tells us, the agency is still hungry for revenues. What could be an efficiency-enhancing property rights scheme, with rights to specified, reduced lev-

els of emissions endowed to existing firms and SCAQMD acting as a clearinghouse and record keeper, turns out to be a Rube Goldberg instrument that mixes fees and credits in ways that distort both of them.

In the past, I have suggested that an artificial market may be better than no market at all. After reading Jim Johnston's piece, I am almost ready to recant. To my knowledge, none of the much-heralded artificial market schemes have flourished. Invariably, the bureaucratic concrete stifles practically every trade that might emerge. The exceptions are found in cases where firms cannot relocate at low cost, like regulated public utilities that have a duty to serve and firms in extractive industries, or where the gains from trade are so large and immediate that the buyer can justify the transactions cost and uncertainty.

But to SCAQMD's credit, the agency may, just may, be nudging us in the right direction. With agency-decreed performance standards in place, trading institutions being built, and with old auto junking working at the margin, we are learning at California's expense. We may be a bit closer to the day when property rights to clean air are defined and real markets emerge. When that day arrives, we may again see enforcement of common-law rights. We will have escaped environmental feudalism.

What about SCAQMD? When real markets emerge, organizations like SCAQMD will likely become impartial experts who monitor emissions and record transactions. SCAQMD revenues? Those will have to come from fees charged for their market-supporting services.

*Bruce Yandle
Alumni Professor
Economics and Legal Studies
Clemson University*

JOHNSTON Replies:

The three letters commenting on the article about pollution trading in the South Coast Air Basin (SCAB) are as interesting as they are diverse. One offers some details about the low level of trading that is taking place. Another repeats the tired old clichés about the supposed advantages of pollution trading and remains blind to the actual performance. The third is the most remarkable. It presents a reasoned rendition of how the initial promise of pollution trading has been betrayed.

Margolis and Langdon from Dames & Moore have provided a useful correction to my point about the first trades reported by Reuters. The prices, it turns out, are lower than the District's estimates. The trading volumes are also much lower than I reported because I assumed the trades were all for 1994, rather than spread out into future years.

All of this is interesting. However, it changes my conclusion ever so slightly. My original interpretation of the prices (high) and trading volumes (low) contradicted the claim of the environmentalists like Jim Jenel that the market was flooded with credits. With fuller information from Dames & Moore, it appears that the prices were lower, not higher than official estimates, and volumes were even a tiny fraction of 1 percent instead of 4 percent as seemed to be implied by the District press release. The corrected results still fail to support the glut hypothesis because the volumes are even smaller than originally indicated. It is hard to see evidence of a flood when the trading landscape is dry as a bone.

The more important inference to be drawn from the very low prices and volumes is that the system is far less valuable than originally esti-

mated. Indeed, this is startling news and suggests that the system be reevaluated right away if it is to be saved.

I find it mildly amusing that Margolis and Langdon assert the Anchor deal was "a profitable investment" because it was concluded at a price "less than one tenth of the projected price" produced by the District. Goodness, a private transaction that is different from that predicted by government. That could only surprise government people and their paid consultants.

The letter from Krupnick and Burtraw takes me to task for not trusting government. I plead guilty. It is probably due to the fact that I spent most of my professional career as an economist working in the private sector rather than on government contract.

First let's take up the property rights point. Krupnick and Burtraw seem to think that the implication of well-defined property rights means that no one can change their mind after such an institution is put in place. Clearly, change occurs in environments where the property rights are well defined and enforced. Indeed, change there is facilitated precisely because the property rights are well-defined.

The relevance of the property rights point has to do with the Fifth Amendment of the U. S. Constitution. It requires compensation for property taken by the government. This does not mean that government cannot change its mind. It simply provides for compensation for damage caused by the government when it unilaterally alters course. In other words, it makes government responsible for its actions. Without such protection, there is no limit on the number and severity of the mistakes that will be made. Moreover, the emission sources will have to invest heavily to insure themselves against

actions by the government or choose not to trade and instead leave the area. Indeed, this may be what is behind the very low prices and volumes reported in the letter by Margolis and Langdon.

Krupnick and Burtraw comment on the poor results in early trading by asserting that the system for political reasons was front-loaded with excess permits. There is no mention of this that I can find in any of the documentation. Indeed, the RECLAIM report goes to great pains to point out that the year-to-year emission reduction schedule is virtually identical to the previous command-and-control alternative. I guess it is possible that there is a secret political agenda at work here. If so, its disclosure by Krupnick and Burtraw would be enormously embarrassing to the South Coast Air Quality Management District. But it does not make sense to me. To distort the trading of credits in the early years in exchange for the vague promise of better behavior later would destroy the what is left of the credibility of the system. While the District may have made errors in the design of the system, I do not believe they are deceitful.

The most important point that Krupnick and Burtraw make is that RECLAIM will achieve lower compliance costs. According to the District, the annual savings will average \$58 million during the first six years. The logic offered by the District, and apparently accepted by Krupnick and Burtraw, is based on the contrast between the two ways of achieving the reductions.

The command-and-control version of the Air Quality Management Plan specifies the technology that will be used by the emission sources and pretty much assumes that the overall reductions will be achieved. Specifically, the requirement is for "best available control technology" for new sources and the "best avail-

able retrofit technology" for existing sources.

RECLAIM, by contrast, is supposed to allow a great deal of flexibility in achieving reductions. The idea is that sources with low costs of reduction will overachieve their targets and sell the excess to sources with high costs. Of course, the baseline emissions from each source must be identified and subsequently monitored every year of the program. The notional saving therefore is the difference between the efficiency gains from increasing flexibility and the cost of monitoring and enforcement at each source.

However, the RECLAIM system has substantially the same requirements for control technology because they are defined in state law. That implies that RECLAIM offers little additional flexibility in reducing emissions. Thus, the site-specific monitoring and enforcement costs will most likely cancel any possible savings.

The District inadvertently admitted as much in its estimates of the equilibrium prices for the RECLAIM trading credits. By taking the equilibrium prices for NO_x and SO_x reductions in each of the first six years, the marginal and average costs can be calculated for RECLAIM and compared with the command-and-control alternative.

The results from that exercise indicate that the savings are negative rather than positive. That is, RECLAIM is likely to be \$71 million more costly every year than the command-and-control alternative.

Krupnick and Burtraw conclude by claiming that no advice is offered on how to proceed. Moreover, they state that Ronald Coase "would not count on the market for handling this type of problem." The answers to both of these points are clearly laid out in the article.

First, it has to be shown that the

benefits of further reducing emissions exceed the cost. From what we know from existing studies, it appears that they do not, at least for the time being. The consequence of ignoring that step is to seriously retard the economic recovery of Southern California and incur the wrath of the voters. This in turn will seriously endanger the RECLAIM experiment.

If the time comes when the benefits do exceed the cost, then the proper approach is the one that Coase has already suggested. Rely on the courts to work out the decisions in individual cases of injury where the environment liability is assigned. Coase helps us a lot in understanding that for a large number of cases, it matters not so much where the liability is assigned, just that it is clearly assigned.

As for what Coase would say about these artificial market mechanisms created by government, he has already spoken. In his seminal 1960 article on "The Problem of Social Cost" he says, "To make the owner of the factory liable for the damage caused to those injured by the smoke, or alternatively, to place a tax on the factory owner varying with the amount of smoke produced and equivalent in money terms to the damage it would cause, or finally, to exclude the factory from residential districts ... lead to results which are not necessarily, or even usually, desirable."

The letter from Bruce Yandle is a delightful change in pace from the other two letters. Despite being an early supporter of emission offsets, Yandle now feels that the market mechanisms actually instituted have been a betrayal of property rights principles.

It is worthwhile to read Yandle's letter more than once because it describes the initial promise and the subsequent subversion of a good idea by the government. Never

mind that the flawed implementation was done with the best of intentions. Errors are still errors and it does not help to postpone their correction with lame excuses and pleas for more time.

Besides being a careful observer, Yandle is a scrupulously honest analyst. The profession has too few of the likes of him.

He follows the Coase tradition in looking forward to an "enforcement of common-law rights." The very least that can be done by the rest of us who care for the environment is to do what is right rather than what is politically tolerable.

Jim Johnston

Lies and Lawyer-Bashing

TO THE EDITOR:

In his article about lawsuits in California ("Golden Lawsuits in the Golden State," *Regulation*, 1994 Number 3), Steven Hayward argues that economic revival in California and around the country requires that we scale back our civil justice system. Nothing could be further from the truth. Our legal system is, in fact, a sound, market-based mechanism for ensuring high-quality, safe goods and services—the cornerstone of a thriving economy.

The United States has the most open and accessible civil justice system in the world. Like our democracy, it is an institution of which we should be immensely proud and protective. Yet the American public has an increasingly negative view of our legal system. Why? Because, for over 20 years, big business has waged war on the American civil justice system.

This war of propaganda has employed lawyer-bashing rhetoric, misuse of statistics and anecdotes,

and outright lies to convince the public to despise a system designed to bring it justice. By making the judicial system unpopular with the public, and through massive campaign contributions and lobbying efforts, corporations have been able to persuade lawmakers to curb the ability of consumers to hold corporations accountable for harms caused by dangerous products and practices. In typical fashion, Steven Hayward uses these same self-serving claims to argue for further cutbacks in consumers' legal rights.

For example, Hayward singles out California as being more litigious than other states, asserting that "more than 850,000 lawsuits were filed in California courts in 1992." But this is only half the story. Hayward fails to mention that California ranked only 29th in total civil lawsuit filings per 100,000 people in 1991. Furthermore, since 1989, the number of personal injury lawsuits filed in California has gone down, while the state's population has increased.

But focusing on the numbers of lawsuits and lawyers in California is quite beside the point. The point is that, as a mechanism to compensate injured consumers and deter unsafe products and practices, the American civil justice system delivers a great deal of protection at a minimal cost.

Consider just one area of the legal system that has been under attack by business interests: the product liability system. Product liability lawsuits represented only .04 percent of the entire civil court caseload in 1991. That year, the total cost of the product liability insurance system, according to data submitted to the National Association of Insurance Commissioners, was about \$4 billion, or .2 percent of total product retail sales. This figure is less than what Americans spend annually on dog

food.

What do we get for this small investment? Thousands of people who have been injured by defective products get compensation, dangerous products are recalled or redesigned, and future injuries are prevented because manufacturers are deterred through financial incentives from marketing dangerous products in the first place. And almost no tax dollars are expended!

Here are just a few examples of marketplace dangers that were reduced because of product liability lawsuits: the Dalkon Shield intrauterine device, a contraceptive that led to infertility and even death for thousands of unsuspecting young women; asbestos, the toxic insulation that has poisoned hundreds of thousands of workers and their families; and silicone gel breast implants, allowed to remain on the market for over a decade while the manufacturers had evidence of illness and injury associated with devices. Use of the devices was not restricted until evidence was uncovered in lawsuits indicating potential life-threatening injuries from the silicone inside the implants.

In addition to these well-known cases, hundreds of less-publicized lawsuits make consumers' daily lives much safer. For instance, due to a lawsuit brought in New Jersey, certain utility lamps now carry a warning about the danger of explosion if they are used near flammable vapors. The case arose when an auto body mechanic used one such lamp while removing a gas tank from a damaged car, and the lamp exploded after reacting with gasoline vapors.

The National Center for Catastrophic Sports Injury Research reports that in 1990, for the first time in 60 years, not one single high school or college

football player died from a head or spinal injury. The Center attributes the reduction in deaths to the improved safety and design of football helmets brought about by lawsuits.

In each of these cases, it was the legal system, not taxpayer-funded government regulation, that uncovered the defects in the products and provided the incentives to make the products safer or remove them from the market. Our government health and safety agencies will never have enough resources to police the entire marketplace so that it is safe for consumers. This is more true now than ever before, as the size of the government shrinks in an effort to reduce the national deficit. By placing costs of injuries on the parties who are responsible for causing those injuries, the civil justice system uses private incentives to make the marketplace safer.

In addition to playing fast and loose with statistics, Hayward sprinkles his article with anecdotes about crazy or frivolous lawsuits. This is also a favorite tactic of business groups seeking to reduce their liability. But almost without exception, upon further investigation, we find that lawsuit anecdotes are full of mischaracterizations and half-truths. This is what happened in 1988 when the news magazine show *60 Minutes* looked at TV ads by the insurance industry that blamed a "lawsuit crisis" for the rise in insurance rates. *60 Minutes* interviewed the parties involved in the cases, as well as the juries and the judges. The show found gross mischaracterizations and exaggerations in every case. They even reviewed a story that had been told on a previous *60 Minutes*, and discovered that

they, too, had been the victims of a false anecdote.

In sum, Steven Hayward does a great disservice by mimicking the claims of business interests that have a financial stake in reducing their legal responsibility for the products and services they provide. In fact, the American civil justice system stands as a model for the world in its ability to provide broad-based access to justice for injured individuals, while at the same time providing a cost-effective mechanism for encouraging safety and quality in the marketplace. Of course there is room for reform of the judicial system. But that reform must be done on the basis of a careful, unbiased review of the facts, not on self-serving lies and half-truths.

Pamela Gilbert
Public Citizen

HAYWARD replies:

Pam Gilbert's letter is artful and clever—as artful and clever as many of the predatory trial lawyers that Public Citizen flacks for on capitol hill. The careful reader will note how she mixes and matches categories and arguments, all the while ignoring the main argument of my article concerning the slippery slope of tort jurisprudence.

Ms. Gilbert's cleverness is nowhere more apparent than in her attempt to appropriate the garments of market liberalism in describing our legal system as "a sound, market-based mechanism for ensuring high quality, safe goods and services ...[using] private incentives to make the marketplace safe." From this one might suppose that Ms.

Gilbert's membership dues for the Cato Institute must be lost in the mail somewhere. Of course the rule of law is the underpinning of a market economy, and it has been market liberals who have advocated a return to private law litigation as a more sensible alternative to government regulation in the area of environmental *and* consumer protection. But market liberals, unlike Naderites who prefer the stifling redundancy of *both* private litigation *and* onerous government regulation, understand that the rule of law is corrupted when the idea of individual responsibility—"contributory negligence" in legalese—is subsumed beneath an egalitarian legal doctrine that views tort liability as a scheme of wealth redistribution.

My article outlined four major types of tort litigation: personal injury, product liability, class action, and wrongful termination. Ms Gilbert is silent about wrongful termination suits (which have been the fastest-growing kind of tort suit in California) and class action suits (one of Public Citizen's leading donors is the pre-eminent class action vulture in California). Instead, she devotes most of her letter to defending product liability suits, which were the least discussed in my article.

But even in the case of product liability suits, where I partly agree with Ms. Gilbert's position, it is clear that the scales of justice are slumping to one side. Consider Ms. Gilbert's examples:

sure, the Dalkon Shield was a bad product, deserving of its fate. But what about the other, safe IUDs that were removed from the market because predatory lawyers were gearing up similar suits against other companies? What happened to consumer choice in that case? And the cases of asbestos and silicone-gel breast implants rank high among the worst abuses of junk science in the courtroom and scarcely require comment.

Ms. Gilbert is probably right in the abstract that strict product liability improves product quality and safety, but when it is taken too far it stifles product innovation and consumer choice. While McDonald's coffee is now starting to come with a warning label, Wendy's has discontinued selling hot chocolate completely, because the courts have decided that consumers cannot be expected to exercise the common sense of a toad. And so even if Ms. Gilbert's figure that product liability only adds .2 percent to the cost of retail sales is true, it does not calculate the loss of consumer choice and product development that the fear of lawsuits generates. The study Ms. Gilbert cites contrasts nicely with the RAND Corporation study on the cost of wrongful termination suits (a study commissioned, incidentally, by trial lawyers). To reiterate: the RAND study found that although wrongful termination litigation added only a very small cost to employment, it had the secondary effect of reducing

the overall employment level in California by as much as 5 percent, since wrongful termination law made employers more reluctant to hire new employees in the first place. A second order effect in the area of product liability is undoubtedly as large.

But the most important lacunae of Ms. Gilbert's letter is that she has nothing to say about the most serious and substantial part of my argument, which is that tort jurisprudence has been on a slippery slope away from any principled basis that sets intelligible limits to liability and negligence. The plaintiff bar and its advocates like Ms. Gilbert never want to discuss the jurisprudential principles of the issue, because when all the emotional slogans about "consumer protection" are stripped away, it is readily evident that the tort liability system has been slowly transformed into a social compensation system—think of it as a privatized welfare state. Like the rest of the welfare state, this feature has to be reformed. Ms. Gilbert closes her letter by acknowledging that "there is room for reform," but Public Citizen and other plaintiff bar advocates never spell out any reform they would support. If people could be held liable for insincerity, Public Citizen would get hit with one whopper of a class action suit.

Steven Hayward
Pacific Research Institute