



## **Polluters' Profits and Political Response: Direct Control versus Taxes: Reply**

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# Polluters' Profits and Political Response: Direct Control Versus Taxes: Reply

By JAMES M. BUCHANAN AND GORDON TULLOCK\*

Basically the three comments published above are improvements or extensions on our basic paper. We have only rather minor objections to them. The note by Robert Main and Charles Baird points out an error in our original exposition. We regret the error (which was first pointed out to us in private correspondence by Yew-Kwang Ng of Monash University, Australia) and are happy that it has no disastrous consequences for our basic argument. The other two comments, by Philip Coelho and by Gary Yohe, introduce institutional structures different from the ones which we discussed. This is no criticism; it is clearly desirable that many different institutional structures be examined. The Coelho comment considers a situation where once production quotas have been issued, they are freely purchased and sold. In a framework of analysis wholly consistent with Coelho's, the outcome derived from his process seems to represent transitional rather than a final equilibrium. With full divisibility of quotas, and with no transactions costs, smaller firms operating at their minimum average cost levels of production could purchase quotas at a higher price than his oversize firms. The real problem here, however, is the degree to which such quotas are salable and the administrative restrictions put upon transfer by the government agency administering the quota scheme. We return to this question below.

The Yohe note seems technically correct. However, it is not germane to our argument. The original producers would surely prefer quotas that are administratively assessed to the Dales-like licenses to pollute that Yohe discusses. His licenses are, in one sense, a different and highly efficient set of taxes.

Both the Coelho and Yohe notes raise

questions of methodology that transcend the discussion of pollution control alternatives. These questions involve the analyst's choice among models. What institutional constraints are to be imposed? What is to be allowed to vary? In a world where transactions costs are literally zero, efficiency always exists, and there is very little that the economist can offer. But we observe allocative results that seem to us to be inefficient. We try to "explain" these by applying our standard tools. Success or failure in such application depends on the plausibility of the constraints that are implicitly or explicitly introduced into the analytics. In our original paper, we sought to explain the widespread resort to quotas despite economists' preferences for taxes. We made no claim that the results observed describe a genuine "institutional equilibrium." In this, as in so much else, the ultimate choice and judgment must remain basically aesthetic.

None of the comments refers to the normative argument for quotas, an argument that was admittedly secondary in our analysis. Positively, observed quotas reflect the political power of regulatees, but this policy also has normative advantages in its own right, even if on other than efficiency criteria. The imposition of any pollution control scheme involves the taking of property from existing producers, presumably for the furtherance of the "public good." Arguments for compensation in this case seem on all fours with those involved when a person's house is destroyed for the construction of an interstate highway. We need not argue that a quota scheme is necessarily an efficient manner of making such compensations to producers. But, institutionally, it may represent a politically viable way-station between confiscation of values and a Wicksellian approach of efficient compensation. When and where possible, we should, of course, recom-

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mend the latter as a means of enhancing the efficiency of both our political and our economic process.

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