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In writing my paper, I had difficulty in trying to figure out what we ought to mean by privatization. The label has been used to cover a wide array of proposals. It is not clear to me that all these proposals are similar in the sorts of effects they have. But all in some measure involve a farming out or a return to private hands of something government now does. We can talk later about whether it also involves simply reducing the number of dollars that government controls. The assumptions that underlie privatization proposals also vary. We may later discern to what extent those assumptions are valid, and to what extent they support particular proposals.

The parts of the paper that deal with legal constraints are parts that I might in retrospect have truncated substantially. For those constraints with real bite are largely legislative controls. And the legislature is, after all, where most privatization proposals will be debated as a matter of politics. There are potential controls on privatization from the way courts interpret statutory provisions and from constitutional doctrines that, if not clearly applicable, nonetheless could be used to constrain the extent to which current government practices are altered. As a practical matter, however, these legal-judicial controls do not seem terribly significant. We do not need to know much to see that constitutional doctrine is a possible, but improbable influence on the course of privatization.

The less obvious, and practically more important points, then, concern the legislature. We need to know how legislatures make their decisions, and what sort of things guide their likely response to privatization proposals. This led to the section of my paper dealing with the topic of how governments work as compared to markets. This covers so many diverse situations that it is impossible to generalize without being able to find some exception. Nevertheless, I am going to start with some generalities, because I think it is important, as we spend our time debating some of the more specific points, not to lose sight of the broader picture.

First, consider private markets. These are generally characterized by residual transferable rights and involve decentralized decisionmaking. Matters such as individual taste cannot easily be handled by a single decision maker. As a rule, private markets will serve both our interest in individual freedom and our interest in allocative efficiency better than will decision making by government.

Second, government is able to cure failure in these private markets because it can exercise coercive power. However, that same capacity to exercise coercive power also makes government a particularly good generator of
rents. Put differently, government can get things right that markets get wrong. But, by the same token, it can get things wrong that markets get right. More often than not I would expect government to get things wrong and to be systematically biased in favor of rent creation.

Third, when government responds to groups that seek to create rents, it ought to have an interest in providing those rents at the lowest possible cost. It ought to be in the interest of the group seeking the rent and the people providing the rent to try to find a way to produce rents efficiently. One of the curiosities of government is that it frequently does not do this. This leads me to my fourth general point. Because government so often uses government enterprises rather than private enterprises, and because government enterprises are predictably less efficient, there must be something else going on if we are to have a rational explanation for government behavior. It seems to me that a fairly good — though not complete — rationale for the frequent use of government enterprise is that rent-seeking is going on among different groups, and that the explicit beneficiaries of government programs are not the only beneficiaries. For instance, when we create public schools to educate young people who may not otherwise be able to afford education, we also benefit a group of people who will provide the education — public school teachers and administrators.

This brings me to my fifth point about privatization. If government creates and preserves rents, and creates rents at different levels including among agents of government, does privatization simply extend this process? Is privatization simply another case of government’s working badly and creating additional rents? Or is it an exceptional case where government works well? When government privatizes, does it in fact reduce rents? I suspect that government, when it privatizes, generally produces some rents, and that it also promotes more efficient decisionmaking and more individual freedom. The deregulation of airlines and trucking, energy and banking, all provide evidence for this.

But — and this is my final point — why does this happen? As my paper makes amply clear, I have no real explanation. There are many pieces that, put together, may yield a satisfactory explanation, but none exists yet. One relevant piece is the existence of slack in the governance system. If the system works to generate private rents, it does not work perfectly to that end. Plainly, too, whatever forces generally guide collective choices leave some room for representatives to follow their consciences at times, to shape constituent views, or to capitalize on the value of incumbency to depart from constituent preferences on a given issue. Also — and this is a point I do not discuss at any length in my paper — the development of technology outruns any system of regulation, and causes some of those systems to
break down. For example, technological developments spawned viable alternatives to banks. This had the consequence that some banking regulations, rather than producing good rents for banks, hampered them substantially. Much the same happened in telecommunications. This, however, is not a full explanation for deregulation because we see many rent recipients go kicking and screaming into deregulation — trucking, here, is a good example.

**KOMESAR:**
Privatization provides a good area for comparative institutional analysis. Privatization offers the choice between government and the market — each more or less imperfect. Since this choice is complex, and since privatization covers so much, one must ask: who will choose between them? And, in turn, what is the relationship between government and this entity which can choose to constrain it?

The term "legal constraints," as Ron Cass uses it, can have several meanings. Most commonly, the term means constraints imposed by the judiciary. I think that Ron Cass is probably correct that presently there are few judicial constraints on privatization. But I am not sure that this will always be the case. There is a great deal that the courts could do — within existing constitutional doctrines, and within their vast discretion. Legal constraints might come in various guises such as delegation, structural due process, equal protection, and substantive due process.

But will the courts actually wish to use these doctrines to constrain privatization — and if so, under what circumstances? These questions may be addressed either at a descriptive or at a normative level. Answering them will involve examining the characteristics not just of government but also of the judiciary. In these terms, one might expect that the courts would act if privatization were caused by or were to lead to severe forms of political malfunction. The courts might also act if they felt they could easily separate this particular type of governmental action from others and if they felt comfortable in their ability to remake the underlying policy determinations.

If legal constraints do not involve judicial constraints, what may they mean concerning governmental or legislative action? Where are the other sources of and reasons for constraint? I liked Ron Cass's discussion of public choice theory. But I do not think public choice theory has gone far enough. There has been an over-emphasis on minoritarian bias and special interests. But in some cases quite an opposite bias prevails. A dispersed majority may have unusual representation — consider the phrase "tyranny of the majority." One of the most interesting issues in legal analysis is the identification of those circumstances which make it more likely that a minoritarian bias will be present as opposed to a majoritarian bias. Both represent distortions
in the political process. What appear as unexplained elements in the economic theory of regulation become less problematic when seen from a public choice theory informed by both these models of political malfunction. Finally, as we discuss the underlying choice between market and government, we would be wise to recast the conventional analysis. Choosing between these imperfect forms of decision making can be dealt with by identifying various forms of "costs" — transaction costs, administrative costs, agency costs and so on.

Alternatively, we can examine the source of these costs — the characteristics of the institutions which cause distortions and require resources — such as advantages or disadvantages in gathering information and organizing activity. These problems which often relate to the concentration or dispersion of impacts occur in varying forms and degrees in markets, courts and legislatures. There are important biases in all forms of decision making which are linked to similar factors.

GILLETTE:
I want to highlight some obstacles to achieving the optimum level of privatization. It seems to me that Ron Cass is correct that groups receiving substantial benefits under the current allocation of resources are likely to resist efforts at reallocation. They will not wish to surrender rents they are receiving through governmental action and regulation. However, there may be other areas in which beneficiaries under the existing system of government control may be diffuse, while the potential beneficiaries of privatization would form a more privileged group. This might be the situation with asset sales, where certain assets held by the government might be coveted by those who could become purchasers. Here there might well be a risk of over-privatization.

There may be situations in which the two effects cancel each other out, so that, on average, we achieve an optimum level of privatization. Consider Conrail. Employees of Conrail may receive substantial benefits from the fact that it is currently government controlled. Nevertheless, certain rents may be obtainable by the purchasers, should such an enterprise be privatized. In such a case, perhaps we would have an ideal situation in which all the effects of decisions were internalized by decision makers. From such an adversary system of different rent-seekers, we might possibly get something closer to an optimum level of privatization.

Nevertheless, I want to suggest that the more common situation may be that we have tendencies either towards over-privatization or under-privatization. We would then get "skewed" decision making in the majority of cases, although the "skew" will not be unidirectional.
Second, I want to discuss the capacity of the public to serve as monitors of the over-privatization or the under-privatization of services, and the participatory value of public monitoring. Ron Cass discusses the possibility of exit as a monitoring mechanism. People may register disapproval with the current allocation of goods and services simply by leaving the locality. This is obviously easier at the local level than at the state or national level. Ron Cass suggests, quite accurately, that exit provides a less effective mechanism for registering disapproval than market mechanisms such as the possibility of takeovers. But public voice may also exist as a substantial monitoring mechanism when the stakes are high, when exit is difficult, and where free-riding is difficult because the service is divisible. For instance, if I am concerned about some public service that provides benefits to me, I may simply not wait for you to complain about the service.

In theory, the voice-option could be exercised by the public whether the service being complained about is rendered by the public sector or by the private. However, I wonder whether in practice people will exercise that voice option differently in the two cases. It could be argued that complaints about services provided by the public sector are often undertaken collectively, in part because the public sector provides some forum within which individuals may gather to engage in political activity. They may take to the streets, as it were. But the private sector typically does not do this. Stockholder meetings do not necessarily provide the functional equivalent of a public utility commission meeting to which the public is invited and at which it can express some of its concerns.

If there is anything to this distinction concerning the public's capacity to exercise its voice option, depending upon the identity of who provides the service, this may have two effects. First, on the value to individuals of acting collectively as a mechanism for expressing their political freedom — as a mechanism for acting as political people. Secondly, and perhaps more germane to our discussion, I am concerned about the effectiveness of the individual exercise of the voice-option — the atomistic exercise of that option as opposed to its collective exercise. If a forum is there, then perhaps collective action is an effective mechanism for voicing dissatisfaction with the provision of a service. If government alone provides such an opportunity, then perhaps that in itself is a reason for favoring the governmental provision of the service. Alternatively, if I am right, there may be a need in privatization to ensure that the private sector also creates some mechanism or forum for the communal or collective expression of the voice-option.

BUTLER:
I have divided my comments into three areas. First, some generalizations about the definitions in Ron Cass's paper; second, some observations about
the practical aspects of the legal issues that he raises; and finally, a discussion of what I feel to be two important gaps in the paper. These relate to legal issues emerging in the political field which I think should be gone into in greater depth.

First, the definition in the paper of privatization seems to me slightly confusing and a little inadequate. To say that privatization is a process to reduce the scope of government and yet to include in that contracting-out may lead to problems. I think our discussion will show that contracting-out led in many areas to an expansion of governmental activity. It would be hard to argue that the privatization of weapons procurement in this country, for example, has led to a reduction in the scale of governmental activity. Indeed, quite the reverse. On the other side, it is hard to argue that loan asset sales should be excluded. Such sales hardly increase the pressure on government to expand.

I think that the definition of privatization leaves great room for discussion and debate. My definition has always been that privatization is an activity that moves functions of government, either as a whole or in part, to the private sector.

In the practice of privatization we see a lot of activities that run parallel to Ron Cass's theoretical discussion. I can, however, think of cases where in practice some of the theoretical problems he raises have been resolved. Also, some other situations have arisen which I think will lead to legal concerns later on which he has ignored. In the case of the delegation of government responsibilities and public liabilities, for instance, there is not much indication that there have been major legal constraints, as Cass says. Moreover, it seems to me that privatization has developed in such a way that even to the degree that there are legal constraints, many of them have been finessed in practice. In my paper I raised the case of the police officer. He is clearly an agent of government. Yet his car is maintained by a private company and may be dispatched by a private dispatcher; his coffee is certainly provided by the private sector, and so forth. In other words, you see mixed forms of privatization where the areas that might run into problems in terms of the delegation of governmental functions are kept in the government sector, while ancillary activities are moved out to the private sector.

In the case of public guarantees of services, what we have seen clearly in Britain and in this country is the use of either regulation or covenants in privatization sales and contracts to ensure that such guarantees are met. Various convenants have been attached to sales to require certain services to be continued by the private sector. However, we also see the downside of this. Rent-seekers try to ensure that their private rents are guaranteed even
in the private sector. We certainly saw that in the case of Conrail and I think we will see it in many other cases.

In his paper, Ron Cass says that the extent of statutory restrictions on privatization is likely not to be very great. I am far less optimistic. I see a very clear trend — certainly in the Congress and to an extent at the municipal level — for groups affected by privatization in a negative way, such as public sector employees, to seek all kinds of statutory paraphernalia to frustrate or even prevent privatization. For example, the attempt by the federal government to sell the power marketing administration last year was stopped dead in its tracks by an amendment added to the bill, saying that the department was not allowed to spend money even to study methods of privatization. It is incorrect to say that the happy experience in the late seventies over deregulation suggests that we are not going to see major obstacles to privatization through the statutory process. Indeed, contracting out at the federal level through the A-76 program has been held back substantially by all kinds of statutory requirements.

Concerning public guarantees of services, there has been a good deal of debate among practitioners of privatization about over-dependence on the private sector. If you move a function out of government then you could become over-dependent upon a particular private contractor, which may mean that public guarantees may not be fulfilled, despite any contract or covenant. However, at the municipal level particularly, various devices have in practice been used to reduce that level of over-dependence. For example, multiple contracts and overlapping contracts have been used, so that there is no complete dependence on any one contractor. The pure economics and the efficiency of privatization may be slightly reduced by this, since extra costs are imposed by having multiple contractors, but in practice that can lead to success in dealing with over-dependence. Incidentally, this is nothing terribly new as a method; the private sector uses it routinely. Large manufacturing concerns very rarely depend upon a single supplier for key components.

One other area which merits attention is positive externalities. We find this discussed in the literature on the privatization of public lands and air traffic control, and in practice in the privatization of public housing.

There has also been significant progress in dealing with the problem of private entitlements associated with public ownership. In Britain, and to a lesser extent in this country, methods have been applied to deal with the de facto property rights of the public employees and beneficiaries. In Britain, for instance, such employees have received free stock and free shares. In order to buy out the private entitlements enjoyed by certain groups, there has been reliance on the fact that efficiency gains are so significant with
privatization that one can buy out these private entitlements and still gain enormous benefits for the government and taxpayer. This is very important because practical and political constraints posed by these private entitlements are severe. Devices that have been used to buy out these constituencies on a purely practical basis could therefore be extremely important.

Finally, I think that there are two other major areas we should discuss. The first is related to the issue of contracting-out. This form of privatization has led to the expansion of the scope of government — even if it has led to an increase in the efficiency of specific services. More important from the legal point of view, we see contractors seeking various kinds of legal and statutory instruments to protect themselves and to reduce competition in the private sector. This occurs significantly in the area of human services, but also elsewhere. Thus we are seeing privatization leading to very powerful legal action to secure monopoly rights in the private sector.

The second area is that of vouchers. Here there is a strong possibility that through an extensive use of vouchers as a means of privatization, government also may be extended, for it may lead to procedural regulation being extended into areas that are completely unrelated to government or even the provision of government services. Education is one such area, as illustrated by the Grove City case. It bothers me that there may be little discussion of the implications of that form of privatization in the future.

VELJANOVSKI:

As I read Ron Cass's paper it occurred to me that the terms of the debate in the United States are very different from those in Britain. A lot of the emphasis of the paper is on what could be called contracting-out rather than the sale of state assets which is the predominant form of privatization in Britain, France and Japan. In the sale of state-owned enterprises, Britain probably leads the world. Although the French privatization program is becoming extensive, it will not go as far as the British privatization program, which includes the sale of public utilities. There is also very little discussion in Britain about the type of constitutional constraints on the government which Ron Cass discusses, because of differences in the two political systems. The debate in Britain has centered around the rationales for privatization.

One thing is certainly true: privatization has led to a great deal of institutional change within the area of public administration. It is not only privatization, but also the deregulation of our financial markets which has led to the rise of what could be called the regulatory agency in Britain. This is a relatively new phenomenon.

One thing that is striking in Britain is that lawyers do not seem particularly interested in these issues. There is no "law and economics" tradition in
Britain, and there have only been one or two articles on legal issues relating to privatization.

Much of the debate in Britain tends to surround the value of state assets, the pricing of the shares, and the conflict between privatization and competition — which is a serious conflict. In a nutshell, the argument a lot of people make is that privatization is the enemy of competition; that in order for the government to maximize the receipts from privatization, it has constrained competition.

Consider the recent British Gas sale. There was no serious enquiry into alternative methods of providing gas, or into permitting greater competition. That was the most blatant example. But this general point is important because the government is committed to selling all state assets if it returns to power after the election.

What are the objectives of the program? It does not really have a set of clearly defined objectives. In my paper I list about eight objectives that have been given for privatization at one time or another. One would have thought that by looking at these objectives, it might have been possible to develop a theory of privatization. Unfortunately, that is not the case because the government really stumbled into the area. Its objective was initially to decrease public expenditure. It found this very difficult to do, and it then looked at privatization as an alternative, and in a very incremental way.

The political opposition to privatization has been confused and largely ineffective. A similar thing happened when the British Labour government said it was going to nationalize many of these industries in 1945. The Conservatives, who were then the opposition party, were equally taken by surprise. It has taken the Labour Party over seven years to formulate a policy for what they now call social ownership (rather than public ownership). They agree with the government on one thing: that the British model of nationalization — the Morrisonian model of nationalized industries that are kept at arm's length from the government and are administered by professional technocrats — had failed.

That brings us to the contrast between state ownership and private ownership, and the whole problem of the mechanics of selling state-owned assets. The assets have been sold off cheaply. There may have been a pricing problem because of the difficulty of valuing some of these assets which have no market equivalents. British Telecom was an obvious example: all telecommunications companies in Western Europe are owned by governments.

Some of the more conceptual issues are difficult to deal with in the definition of privatization. In my book, I restricted privatization to the sale of state-owned assets. It seemed to me that the more generic definition of
privatization would be withdrawal of a government from production. That still leaves the area of regulation as one in which the government is heavily involved — as, for example, in the public utilities.

In Britain, privatization has led to regulation, and it is now hard to tell whether on balance the scope of government has increased or decreased. The nationalized industries were themselves regulators, and the central government also regulated them to a certain extent. Privatization has led to a qualitative change in the nature of state intervention. We have been setting up what you would call public utility commissions on an industry-by-industry basis in the U.K.

One can look at the economic literature on property rights for some assistance on the way privatization should be defined. What is happening is a change in the "bundle of property rights." The dichotomy between public and private ownership or state ownership and private ownership, is, in my view, misleading. You can privatize in a number of different ways which lead to different behavioral effects on the enterprises in question. The dichotomy does not seem to me very useful, except as a public relations exercise. However, it does mark a difference in ownership. One important difference is that after privatization, ownership rights in firms became tradeable and it is possible that ownership may change. In many cases, the British government still holds veto power over who can own the enterprise. It holds a "golden share," which is basically a veto over takeovers, and it also has decided that no one person can hold more than fifteen percent of the shares in many of these industries. This is interesting, because one of the major forces pushing for privatization was the capital constraints of the state-owned enterprises. Access to private capital, however, was looked at solely in terms of financing and not in terms of the economists' notion of a "market for corporate control."

Next, legal constraints. There are no legal constraints, and the courts have little role to play in England in determining the nature of privatization. I spoke to a number of public lawyers in England on these matters. Not only were they not interested, but they did not appreciate the significance of what has been happening. Moreover, judicial review in England is very low key. The courts will not intervene — and, of course, we have no written constitution. Parliament is sovereign and what it says goes.

The control of the new administrative agencies set up to regulate the privatized utilities raises some interesting legal issues. They are not really controllable by the courts, although judicial review in the form of the examination of administrative agencies is on the increase. As to the terms of the courts' intervention, English courts will not do what an American court does and get involved in the decision making process.
One major issue which it would be interesting to discuss is who and how one can control the regulators. This is something in which the United States has more experience.

Finally, the efficiency of government enterprises. A lot of work has been done on state-run enterprises. But the empirical evidence is equivocal because of the difficulty of testing the relevant claims here. What you have to test is not whether private enterprise is better than public enterprise, but whether public and private enterprises differ in their efficiency in similar circumstances.

Now, the lack of clear conclusions here can be used in two ways. One could say: well, there is no case for private enterprise! Or, one could say that there is no inefficiency created if you move to private enterprise from state ownership. So we could — to use Ron Cass's term — merely be changing the base lines concerning social and political decision making from the state to the individual.

CASS:

First of all, as Cento Veljanovski points out, there is a difference between the way the term privatization is used in most of the world and the way it is used in the United States. I think this reflects the fact that the government has intervened less here than it has in most of the world, and that it has intervened in a very different way. There are not that many state-owned assets here, other than land, compared to the extent of state-owned enterprises and assets in other nations. The way in which changes occur in how government does business, and in what government controls, are likely to be somewhat different. Here, you are going to have to talk about a lot of other things than simply the sale of government assets.

Stuart Butler mentioned, quite rightly, that in my paper I said that I think that to use the term "privatization" in talking about government selling its loans and its right to collect money from people is to stretch the term privatization — although these are assets listed on the government's books. What is really happening in the sale of the loan is not the government changing its function and form: it is not saying it will not want money in the future; it is not saying that some activity is going to be done very differently, that rights and responsibilities will be reallocated in any meaningful way; it generally is not selling these loans to other people so they can collect them more efficiently. The more realistic explanation of asset sales is that, under pressure to reduce its deficit today, government is engaging in a form of borrowing against the future. I think that such moves probably increase rather than decrease the effective size (ambit) of government and asset sales make very little difference to the government's operations.
Contracting out functions that the government previously performed, in contrast, does reduce some aspects of governmental decision making and often produces efficiency gains, notwithstanding the ostensible constancy in the range of activities formally subject to government control. If instead of the post office being government owned and operated, suppose that the government contracts for postal services, even if the contract is with a non-government monopoly provider. If that monopoly provider has the capacity to generate private profits, there will be a change in the way the service functions, and the change will resist at least some of the aspects of rent-creation that go on when the service is government run. It is not in the interest of a private monopolist to cross-subsidize users the same way it is in the interest of political decision makers. Where cross-subsidization currently takes place, it is usually the result of regulation. We are much more likely to see some relation between the prices charged and “Ramsey pricing” when a private entrepreneur is providing the service than when it is provided by government. One final point on this topic is that, if you move a monopoly from the public to the private sector, the range of arguments against its remaining a monopoly will increase.

Stuart Butler’s concern that contracting will extend government power seems exaggerated. The Grove City case, to which Stuart Butler refers, is somewhat exceptional. This case involves a clause in the Education Act providing grants to individual students who attended college. The Supreme Court said that the law and the history of that law are quite clear: the college, attended by grant recipients, was subject to the anti-discrimination requirements in the Act, but only with respect to one aspect of its operations, its decisions on financial aid. Two factors separate this case from the general run of government operations. First, discrimination has been treated differently from other areas by the courts. Courts have been much more expansive in this area in defining the scope of limits on government action, extending constraints to conduct that in other respects would be treated as “private.” Second, the statute in Grove City was quite clear. Moreover, if instead of contracting-out, the government provides education directly, that surely would not reduce constraints on how the education is provided or on how the financial aid is provided.

I do not mean to dismiss Stuart Butler’s point entirely. That Grove City is exceptional is not conclusive. It is hard to know exactly how the courts will behave in the future. Certainly, there will be opportunities for courts to engage in actions that would frustrate privatization. But I simply do not believe that the courts will do much here. I think they will continue to be generally non-interventionist.
In looking at the sort of regulatory programs with which I am familiar, it seems to me that rent-seeking provides a good explanation of how the programs developed. It takes account of the fact that sometimes rents are captured by a relatively small group, although a larger group also shares in the benefits of the program. Thus, concentrated groups have pushed some anti-discrimination programs through — even though the programs themselves benefit a wider group.

Clay Gillette asked whether there are significant differences between public and private decision makers — whether in a public context there is greater incentive for "voice." He contrasted the public utility hearing with stockholders' meetings. He argued that in the former you would expect more public participation than in the latter. I would agree that there are differences. But it seems to me that the same sort of forces operate in both, at least to some extent. Those who have the greatest interest are likely to attend both types of proceeding; there is no reason to think that in either forum the array of interests is fully representative. The biggest difference between Clay Gillette's two examples, however, is that the interest of those who show up at stockholders' meetings is likely to be more congruent with the interests of stockholders who do not turn up than is likely in the case of the public utility hearing.

Cento Veljanovski pointed out that the Morrisonian model was accepted in England for a very long time. However, of late there has been widespread dissatisfaction with it — not simply economists, but a large part of the public has become disenchanted and has recognized the costs that are associated with it. This suggests to me that one part of the movement toward privatization may have to do with the economics of information. When a group has a concentrated interest in some area, the cost of obtaining information about that area is much lower. That advantage dissipates over time, as people become more aware of the costs of the system, and of who is benefiting from it. This information will not be perfectly distributed. But the fact that it changes over time may help suggest why the hold those who obtain the rents have over the activity may diminish over time. Further, the change in the political atmosphere concerning privatization may be related to certain well-known problems about cartels. When regulatory bodies serve largely to promote cartel activity that depends on a public enforcement mechanism, it may become increasingly difficult to keep the cartel operating, for action may have to be taken at the political level to keep the regulatory mechanism in place. And members of the cartel may have their interest diverted from this. Airlines are a good illustration.
KOMESAR:
First, there is Ron Cass’s point about a bias towards the many. Suppose you try to explain activity in the public sector by using the hypothesis of rent-seeking by concentrated interests. Certain phenomena will not be explicable in these terms. It may look as if the public interest is winning out, or as though large, dispersed groups are gaining. How does one explain such things? People commonly say there are two models of the political world — public choice and public interest. Public choice is identified with a bias towards concentrated minorities. The public interest approach simply assumes public interest: it offers no underlying system of plausible behavioral assumptions and mechanisms which lead to this outcome.

Ron Cass suggests that a majoritarian bias may sometimes succeed in the face of special interests because of some “slippage” in the political forces. Legislators are seen as able to do things which are not consistent with the interests of the usually powerful special interest groups. These legislators are then able to collect economic rents in the form of activity they consider to be in the public interest.

Such an analysis, however, raises the following questions: first, when does this “slippage” in fact occur? Second, if the legislators are able to take rents, why should they take them in the form of public interest activity? Third, why should one suppose that most legislators take the same view of the public interest? As a general matter, the approach employs a sophisticated model focusing on systemwide interactions in connection with one set of results and a non-model for what does not fit.

It seems to me much simpler to adopt a public choice view which can recognize a broader set of systemwide forces, thereby integrating the full range of the observed results without recourse to ad hoc explanations. In some instances, it will be more likely that there is a bias in favor of a dispersed majority, and in others it will be more likely that there is a bias in favor of a concentrated minority.

It does not surprise me in the least that federal administrative law or administrative agency problems are characterized by minoritarian bias. That is where one would expect such bias. But there are instances even in that context where one might expect majoritarian bias.

BUTLER:
I would like to return to the definition of privatization. The term privatization has meanings which differ from place to place. As Cento Veljanovski pointed out, the meaning of the word in most European countries is different from that in the United States. But to define privatization as an activity in which the private sector is involved and which leads to reduction in the scope of government is very unsatisfactory. For example, the initial goal of
loan asset sales and other types of asset sales is to raise revenue to permit current expenditure to continue. Ruling out such sales from the definition would mean virtually all the British privatization measures would not meet Ron Cass’s definition. Also, there is very little evidence that the net effect of contracting-out is a reduction in the scope of governmental activity. After contracting-out, one typically sees different forms of rent-seeking and of cross-subsidization than occurred before, rather than their reduction. Instead of users of services cross-subsidizing one another, providers of services are subsidized by taxpayers. So the Cass definition eliminates almost every practical case of what most people consider as privatization.

Consider the two major areas of contracting-out in this country: defense procurement — which I have discussed already — and the provision of human services. From the 1960's onwards, the government has used contracts with non-profit service providers for the provision of human services. This has set in motion a very powerful lobby which has argued continuously for greater expenditure. One could not argue that the use of the private sector in the area of human services has led to reductions in the scope of government — quite the reverse. In addition, it has led not only to increased expenditure, but also to campaigns for government regulation on behalf of service providers. And these have had further implications in the market. Thus, if privatization really means a net reduction in the scope of governmental activity, I would find it difficult to think of an example of privatization.

I would also like to ask for some further guidance on the Grove City case. It still seems to me that the Supreme Court decision centered much more on the question of the intent of Congress than on any constitutional question. And Congress is now putting together a new bill dealing with civil rights which explicitly extends the scope of government in that area. In cases like Grove City, it would have the consequence that the recipient institution as a whole would be affected if one element of it was in receipt of government assistance. It seems to me that we are seeing pressure to use vouchers as a way of spreading the scope of government by this means.

GILLETTE:

The justification one gives for favoring privatization may have an effect on the areas in which one prefers privatization. One who favors privatization out of a belief that government should be minimized might take a broad view of where privatization would be desirable. On the other hand, one who endorses privatization in order to reduce public expenditure or government deficits might defer to government provision of goods and services conjoined with a different pricing system. There is currently a substantial effort at the federal level for services to be paid for through users’ fees
rather than from general revenues.\textsuperscript{1} The function of moving to a user fee is in part to reduce government expenditure, by having the beneficiaries of particular services bear the commensurate cost. If one moves to a user fee system, that does not necessarily lead to less governmental activity — simply to a different pricing mechanism for those goods and services.

VELJANOVSKI: I was interested in the information cost explanation of why privatization is popular. In Britain, it is often argued that Britain's economic problems are largely a result of an anti-enterprise culture, and one of the objectives of privatization is to try to change people's attitudes. I would turn the argument the other way round. People may have those attitudes because the opportunities are not there to make money.

Once the government is committed to privatization and decides to sell its assets, what form does privatization take? This brings us into the realm of pressure groups and bargains. However, it is not clear to me — in Britain at least — who these pressure groups are, and, especially, whether the electorate is a major pressure group. People often also speak of "technology" as a factor, but no one explains how this leads to changes in political outcomes.

One clearly defined interest group has been the existing management of the nationalized industries. Capture has occurred because those who are to be "privatized" are part of the state sector. They have been most influential in determining the way British Telecom and British Gas have been sold. They have exerted pressure so as to restrict competition and to prevent the breaking up of their companies.

However, pressure group politics is a two-way street. While the managements of the nationalized industries have been lobbying hard to restrict competition, the government has imposed all sorts of constraints on the ability of these nationalized industries to raise capital, so as to make privatization an attractive alternative.

CASS: First, how may a majoritarian bias come into play? Who are the operative players? That a majority shares a preference (a bias) does not mean that the preference will prevail and be translated into political action. The usual political action, I think, involves some people obtaining rents. A minority preference can prevail or a majority preference could. For the majority to win, all of the majority does not have to get rents. Rather, I would suggest the more frequent explanation is that there is some slack in the political

system and, consequently, some opportunity for individual politicians to take personal rents. They may do this by promoting their conception of the public interest. This does not require that all legislators have the same conception of the public interest, and take their rents the same way. It will be enough if a majority of legislators are indifferent on this issue and a very small number of political actors find this an appropriate way of capturing rents. They may act in this way simply because they think that this issue can promote them to a broader public; politicians may be especially likely to follow this route when they wish to change jobs. The interested politician's view of public good can become law so long as the coalition on the other side does not have sufficient votes because the rents derived from less publicly-interested legal rules are not sufficiently large or sufficiently easily collected to block that change.

Second, I would like to clarify some points raised by Stuart Butler. Asset sales are appropriately treated as cases of privatization. I also did not mean to say that the intent of the legislators is critical. Rather, I referred to their intent in connection with the sale of loan assets because these make no change to the external world. The government will simply have more cash in hand now to do things it wants to do. However, Stuart Butler was exactly right, in his discussion of contracting out, to focus on whether government activity is in fact being extended. I do not want to define privatization as the mechanical transfer of government functions because I do not think it very important whether we label a function as governmental or private. Rather, I care whether government is doing more or doing less.

KOMESAR:
First, majoritarian bias is not unrelated to rents. The question is, who captures rents, not whether there are rents. Majoritarian bias is another form of rent capture rather than an ideal state. It is itself a form of malfunction. Not all configurations of interest in which there are concentrated groups and dispersed groups are ones in which the dispersed group is dormant, and therefore weak. Not all dispersed majorities are dormant and, therefore, the bias does not always favor the concentrated minority. There are examples in which concentrated minorities may be disadvantaged. One such case is the local zoning decision in which the choice is whether or not to impose restrictions on a developer. Who will win such a political battle? If you use a pure public choice or a minoritarian bias view, the concentrated interest, the developer, should prevail. The developer has, as an individual, more at stake than do any of those who live close to the development. But this majority, though they have a lower per capita interest than the developer, are typically over-represented relative to the developer. Whether majoritarian or minoritarian bias is most likely depends on
the economics of information and the economics of organization. There are a number of factors at play here. For example, the larger the jurisdiction and the more people it contains, the more likely it is that the cost of obtaining information about a given issue and the cost of organization will be high enough to make minoritarian bias more likely.

As to Ron Cass's point about the influence of a few politicians, Ron may suppose that political competition has sufficient slippage so that there are a lot of legislators who will be indifferent to some issue. But if there is a concentrated group as is supposed by the public choice theory's minoritarian approach, the legislature will not be indifferent to their interest unless there is a reason why that bias towards the special interest isn’t operating. One explanation might be the presence of majoritarian bias.

It is quite true we observe situations in which a few legislators are able to pass legislation when no one else cares, but the question still remains: how do we explain this?

POOLE:

Both Ron Cass and Neil Komesar are taking public choice analysis as basically a descriptive system: as a way of explaining and understanding the tendency of minority interests to gain advantages — rents — by using the political process. If one takes such a deterministic approach, one must then consider cases where deregulation or privatization has occurred as exceptions to the public choice understanding of the world.

I think, however, that it would be more helpful to consider deregulation in the U.S. of the 1970's, and privatization in Britain in the 1980's, not as exceptions, but as examples in which a public choice analysis is used in a prescriptive way. It offers us a sophisticated understanding of interest groups by means of which we may figure out how to circumvent rent-seeking and build a coalition that can advance what we would consider to be the majority interest.

Consider the work that the Adam Smith Institute has done, analyzing the strategies used by Margaret Thatcher's government. The government bought off the interest groups. It gave shares of stock to the employees of British Telecom. It changed public housing tenants' incentives, giving them the opportunity to purchase public housing. These are ways of employing public choice analysis in a prescriptive manner. Such cases are not exceptions to public choice analysis. Rather than simply describing the status quo, public choice analysis is used as a tool for figuring out how to change the status quo. This perspective will be helpful in looking at where privatization should go in the future.
PAGE:
We are wasting our time in this discussion if normative analysis can have no effect on public policy. Yet the public choice view, which assigns decisive weight to interest group pressure in the formulation of public policy, appears to make just such an assertion.

Some ideologies are quite receptive to arguments that government action is in the public interest. Normative analysis, however, can show who gains and who loses as a result of government action. To the extent this kind of analysis is understood, it increases the costs of promoting special interest programs. This relates to Bob Poole's point that public choice analysis may act prescriptively. If arguments offered by special interests that their goals are in the public interest are less persuasive because of public choice analysis, we are not wasting our time.

MANNE:
I would like to discuss further Neil Komesar's points about the tyranny of the majority and majoritarian bias. A majoritarian bias seems almost of necessity to arise only where there is some kind of one issue vote — like a public referendum. In informal discussion, Clay Gillette suggested that a political entrepreneur may capitalize on a single issue in that way. Nonetheless, such cases are rare, and most cases of "majoritarian bias" fit the model of a minority with free-riders better than majoritarianism. My aim — as you can see — is to push us back to a public choice perspective.

WILLIAMS:
I agree with the assertion that participation is valuable, and that it is a communal value. But I would take issue with the idea that we should hesitate to privatize in order to safeguard opportunities for participation. I am reminded of Oscar Wilde's quip that the trouble with socialism is that it takes up too many evenings. There are only so many evenings, and the evenings spent at the local zoning authority, and at the local public utilities commission are evenings that people cannot spend informing themselves on real public goods issues — such as SDI. There are issues that are of real public importance, and the diversion of energy to other matters is unfortunate, and in part accounts for the low quality of the debate.

However, I do not want to take the naive position that every citizen who currently spends evenings at the zoning commission, demanding that the orchard next to his house be preserved, and not be developed into housing, would, if that avenue were blocked, turn his energies entirely towards genuine public goods.

A related point is that there is an important difference between a public utilities commission meeting and a shareholders' meeting. It is not that there is a difference as to the representative character of those who attend.
It is, rather, that the shareholders' meeting is a harmless event where nothing occurs. One does not need to go because if one objects to what goes on, one sells one's shares. And the threat that shareholders will sell their shares is an important constraint on management. However, at the public utilities commission, decisions can be made which can do a great deal of damage.

ELLICKSON:
I would like to identify three different varieties of privatization. First, there is the transfer from the public sector to the private sector of the production of specific goods and services. An example from Cento Veljanovski's paper is postal services. A second form of privatization involves government relinquishing regulatory functions, perhaps to trade associations, perhaps to private law and market forces. Third, government can transfer assets, such as public lands or loans, to the private sector. This last category is an interesting one because when government transfers assets, it may create rents and diminish some liberties. The disposal of public lands in the nineteenth century, a massive privatization effort, subdivided a commons among private owners and thereby created rents. Rent-seekers such as railroads were beneficiaries. These transfers curtailed some liberties by ending universal privileges to use the commons. Prior to privatization anyone could hunt beaver or cut down trees on the public domain. On balance, I applaud the privatization of federal lands, because it is likely to enhance the efficiency of resource allocation. But it is also rent-creating, and in some senses, liberty-reducing.

ALEXANDER:
I want to comment on the social vision that is embedded in Ron Cass's conceptual structure, and in the extant discourse about privatization. That conceptual structure, as I understand it, draws a dichotomy between the market and government. That dichotomy translates into a further one between the individual and the state, and between public and private — a distinction about which several of the papers seemed rather uneasy. But if the public/private distinction is dead, it seems clear from our discussion so far that it rules us from its grave.²

Privatization should not be treated monolithically or evaluated in either/or terms. One's judgment about privatization depends on what one means by privatization and the context in which one talks about privatization. There are at least two positive roles that government can play which would suggest that privatization is not beneficial. The first is the point that Clay Gillette mentioned in his discussion of over-privatization. Government

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² The phrase is, of course, Maitland's. See F. MAITLAND, EQUITY AND THE FORMS OF ACTION 296 (1932).
generates a language of politics — an opportunity for participation and socialization — a positive value of government that ought not be overlooked. The second positive value of government is the expression and realization of community identity. For example, if one discussed the movement in favor of historic preservation, there is a case to be made for government having a unique role as the vehicle for allowing a community’s sense of itself to be expressed and realized through the preservation of peculiar and unique assets or resources.

I do not want to praise government completely any more than I want to bury it completely. There are aspects of privatization that I find attractive — not because they promote, an atomistically individualistic social vision, but rather because they promote or at least are consistent with, a communal vision. It seems to me very important not to equate privatization with atomistic individualism, or to view privatization as the polar opposite of communitarianism. For example, the phenomenon of asset sales may illustrate how privatization can be compatible with a communal social vision. Consider the sale of public housing projects. If the development is given or sold (at an appropriately low price), then I favor this instance of privatization to the tenants. However, I would be less enthusiastic about the sale of public lands in wilderness areas.

Finally, privatization may be consistent with communitarianism in its potential to reduce bureaucracy. This may facilitate genuine participation by members of the community. But this is not inevitable. Bureaucracy is not limited to government. It is not unknown to the so-called private sector. But privatization does offer some potential for reducing bureaucracy. To that extent, one who is at least sympathetic to communal values should find some interest in privatization.

WITT:
Instead of looking at the opportunities for participation, I would like to look at the results of this participation. I agree with Clay Gillette that there are greater opportunities for participation in the public sector. I would disagree with Clay’s assumption that there is a positive relationship between the number of forums at which this dissatisfaction can be voiced and a positive response by policy makers. I would attribute this to the insulation from market forces that we have in the public sector. Aside from being able to express dissatisfaction occasionally at the ballot box, citizens really do not have much influence over decisions in the public sector. But in the private sector, you have the opportunity to sell your stock or seek the product or service from a competitor. This will have a direct relationship to profitability. You may, thus, expect more responsive actions in the private sector than in the public sector.
POOLE:
Clay Gillette's point about public voice applies at best to a very limited number of cases. In the United States, most privatization involves the contracting out of services. Where, say, a city contracts with a private firm to sweep the streets or pick up the garbage, there is just as much opportunity for public participation when the city council meets as there is when city government provides services directly. There may even be more accountability when a firm is the provider and has a three year contract which might not be renewed than there would be if a public bureaucracy provides the same service with an unlimited franchise, no matter what its performance. In that case—which represents the majority of cases—there is as much or more public voice in a contracting out situation as there is with direct government provision. If you look at vouchers and user fees, there is greater individual choice when services are provided by letting the citizen—the customer—directly choose which provider to use and how much service to obtain than if the services are paid for by taxes and are provided to everyone uniformly. In asset sales or loadshedding we can divest competitively. We have also had city governments getting out of the garbage collection business completely, and substituting not an exclusive franchise but free markets. In those cases, individuals may vote not by moving, but simply by changing their patronage to a different company, as in Fairfax County in Northern Virginia.

KOMESAR:
I would like to return to the issue of majoritarian bias. Could we observe outcomes consistent with self-interested behavior, which either: (a) appear to be in the public interest or (b) appear to be instances in which concentrated minorities seem to lose to a dispersed majority? Ron Cass noted that such cases do occur. Why do they occur? Often an entrepreneur is at work. That is, someone or some subgroup within that dispersed group can gather that group together, provide it with information and organize it, or threaten those within the political process that they will do this. However the mechanics operate, we do observe those situations and they seem to be consistent with self-interested political behavior. They are thus consistent with a public choice model which does not require good or altruistic intentions or motives. I do not want to dismiss humanitarian activities or altruism. But I do not want to base a descriptive model of political activity on these assumptions either.

KLAUSNER:
It is important for students of privatization to reflect on what Stuart Butler said about the perils of contracting out. Bob Ellickson suggested that when government relinquishes its role, the result may be a decrease in liberty.
For while once people could hunt on the commons, now the commons are privatized. I would suggest that when you change what was previously common into transferable property rights, you may well increase liberty. If there is a public beach where you have to queue, it may be hard to get a little place in the sun for yourself. You may well have an easier time of getting out to the beach if you privatize and allow property rights to be transferred. That also marks the difference between the stockholders meeting and the public utility commission hearing. For in the private sector you can sell your stock. However, in privatization, it is competition that is important, and we may be better off with competing public sector enterprises than with some form of contracting out that does not allow for competition.

GILLETTE:
An individual may be less effective in monitoring a privatized supply of public goods and services if the privatization is not combined with an opportunity for public redress. Typically, the private sector provides no opportunity for a disgruntled individual to determine the breadth of support for a particular program.

Contrast that situation with one in which a municipal planning commission holds hearings at which neighbors who wish to retain an orchard can complain about plans to develop the property. If the individuals who want to retain the orchard are simply rent-seeking, perhaps we do not want to provide a common forum for them. But if we are concerned with the provision of common goods, we may facilitate that end by providing a public forum that can help to overcome collective action obstacles to optimal provision. Now I am not saying that privatization cannot provide a public forum, it could. Indeed, the public utility commission, is itself an example of a public forum in which the public may voice complaints against a private entity. The question is: will it happen?

Finally, I think Bob Poole is completely correct when we are talking about a private entity that is engaged in enterprises under contract to a locality, such as street paving or private garbage collection. In such instances, theory suggests many opportunities will evolve to march down to city hall. But does the theory conjoin with the practice? May the individual not think, rather: "Oh, that's being done privately, therefore my complaint is directly with the private supplier."

The mindset of the individual is often that when you deal with private enterprise, you make your complaints through private channels as opposed to public ones — so that the theoretical possibility of private provision and a public forum is not in fact manifested.

If the opportunities for complaint, which will lead to optimum levels of public service provision, are either cut short because of lack of a public
forum or because of the mindset of the people who say, "I should be dealing just with the private provider," then Bob Poole's suggestions will not be realized. This is not to disagree with Steve Williams. If there are good reasons for privatization, this ought not to be an obstacle. It is instead a caveat. It says: in addition to privatizing, let us see if we can do something both to ensure that there are public forums for complaint and let us see if we can change the mindset of individuals so that they are aware of the theoretical possibilities about which Bob Poole has told us.

CASS:
I think that by the sale of the commons you can reduce social welfare and reduce the ambit of liberty in some circumstances. This may be the case if, before it was used in a more socially appropriate public fashion, and if there really was a common group that used it equally and the burden for that usage was spread across that group. Then, you will make the world worse by selling off the land. At the same time, my suspicion is that usually what happens is that a rather small group of people were using the land. If the land were privatized, a common facility still could be maintained for those people who, say, wanted to hunt — with their paying for it themselves on, say, a "pay for what you catch basis."

SHEARMUR:
I would like to come back to Clay Gillette's point about public participation. There is something here that many people find attractive because of the influence of the "civic humanist" tradition, our ideas about town meetings, and so on. But I think we should be willing to let our attachment to this, and our recognition of its value, be tempered by a realistic appreciation of what public participation often actually means. There is much evidence from the work of political scientists that public participation often works as a kind of educated middle class scam, where a certain number of articulate people are able to pursue their particular private interests under the cloak of the defense of community values. They may, by this means, acquire or retain various sorts of privileges, and acquire goods they could not afford or would not be willing to pay for out of their own pockets.

Take the case of the orchard. The situation there was represented as involving two players: the developer and the other people round about who wanted the orchard to remain. Not only does one have these people using public participation to try to secure to their private use amenities for which they are not willing to pay, but the cost — the market price of the land — may give a good indication of the real public interest here — one that also takes into consideration the interest of people who might have had the chance of living in the houses, if development had taken place.
KOMESAR:
The question is not whether public choice could be used normatively, as Bob Poole suggested, so much as why government entities, or the constituencies who control them, would allow themselves to be privatized if it was not to their advantage?
The same kind of question could be asked about the notion of participation, picking up on Jeremy Shearmur's point. If Clay Gillette believes that the public choice model operates so strongly and that concentrated groups are over-represented, why is this not the case for participation as well?

AHRENS:
We have discussed whether the private sector can provide a forum in which people can express their views about common values, or create common values. We might also consider whether the public forum is really all that productive in these tasks. Very often it polarizes much more than producing a common view. We see this in community level decisions all the time. Concerning participation, it is important to draw a distinction between a situation where the aim of participation is a coercive transfer of some sort, as opposed to a communal effort involving just voluntary exchange. I would also be very uneasy about coercion merely to create participation.

NORTON:
Public participation is a form of socialization. In making a decision about socialization, we have to look at the forms of behavior we are encouraging. To a large extent, I think public participation in governmental decision making encourages behavior we wouldn't ordinarily think of as productive or desirable. For example, there was a proposal several years ago to formulate comprehensive programs to tell farmers what kinds of crops they should grow and what kinds of farming techniques they should use. The saving grace of this was supposed to be that this would all be decided at the county level, and so the county administrator of farm programs would be the key decision maker. But this means that it is the farmer who is sitting down at the local Department of Agriculture office talking to the county administrator who is going to get the type of program he wants. The better farmer who is back on his farm, doing the actual farming, is not going to have the system operate to his best advantage.

Government decision making also strongly encourages polarization on public land issues. In making decisions about use of public lands, oil and gas developers and environmentalists have every incentive to attack each other and to be as vocal as possible in their criticisms of each other's ideas. But in a private context, those groups have an incentive to cooperate and find a way of maximizing the ability of a tract of land to serve both types of goals.
KLAUSNER:
There are a lot of opportunities for public involvement in the private sector; the difference is that it is consensual. In Los Angeles, for example, in the Silver Lake area you will find in shops in a single supermarket chain, Ralph's Market, exquisite Mexican products that you won't find if you go to Ralph's in Beverly Hills. The owners of the markets have their own incentive to try to deliver what the public wants and it is all done consensually. If you approach a company with a problem, the company may be skeptical and not believe you. But if they believe you they will try to respond, because the incentive to do so is built in. If you go to public meetings concerning a government entity, people may often try to camouflage their true interests, in order to try to get the agreement of others.

WITT:
I also would like to focus on participation. We have been looking at the opportunities when we should have been looking at the outcomes. In looking at the examples of rubbish collection and the bus service, perhaps we should be looking at what are the incentives for the providers of the services to take corrective action. There is greater incentive for corrective action to be taken in the private sector rather than in the public.

CASS:
There are situations where we do have market forces but they will not be able to prevent rent creation, as there exists a natural monopoly. Can we get government action in those situations to improve matters? Or will government simply redistribute rents in a fashion that is no better? Or what of government action to promote efficiency? There are also, as Landes and Posner point out, some types of right that, if you allow them to be privatized, will result in supra-optimal investment in search. Also, as Easterbrook and Fischel point out in discussing the market for corporate control, some goods, such as information, by their nature have public goods aspects so you will get sub-optimal investment in production.

ALEXANDER:
I want to emphasize the need to distinguish between participation as an instrument, that is a means toward some other goal, such as John Ahrens' suggestion of consensus, and participation, as a non-instrumental value. I wish to stress the possibility and usefulness of thinking of participation not in instrumental terms, but as a value in itself. If we think of participation as

a non-instrumental value, we may find reason to believe that it is consistent with the realization of individual liberty.

POOLE:
I wanted to respond to Neil Komesar's point about the prescriptive use of public choice theory. Why would interest groups allow themselves to be out-maneuvered by the sophisticated prescriptive application of public-choice theory? It is not that they would be tricked so much as that their incentives would be changed, such that they benefit from privatization. Look at the U.S. Postal Service. The major obstacle there to considering privatization has always been the postal workers' unions. In Britain, Thatcher's brilliant idea of buying off the workers in nationalized industries by making them shareholders at a discount seems to have been quite effective in changing workers' views. It gave them an incentive to be for privatization rather than to oppose it. That is an illustration of the power of assessing and analyzing coalitions, and of figuring out how to change the incentives that are involved so that what was an impregnable status quo all of a sudden is open to the possibility of creative change.

CASS:
In looking at the relative efficiency of private and public provision of services, three aspects of the difference between them will determine the degree to which private provision is more efficient than public. One is scale. There are frequently either economies or diseconomies of scale, and private provision in general is much more likely than public provision to be tailored to the appropriate scale. When you have government provision there is often pressure to have a single source of supply for whatever the relevant politically defined area is, so you have a postal service that covers the whole of the United States. In any given geographic, political unit, one police force will cover that entire unit, and so on.

Second, there is competition. The tendency is again in private provision to have competition and in public provision not to have competition. Certainly, the private providers would rather, if they could, have a monopoly and in some areas they will press for this. Also, a monopoly need not be terribly inefficient, if you structure the contract appropriately. Unfortunately, in most cases where you have a single monopoly provider there is no incentive for the city or other government purchaser to make an appropriate contract. Generally, however, allowing private provision introduces some form of competition into the system, and that would help make the system run more effectively.

Third, the availability of a profit motive for private providers will cause them to behave differently. They will not have the same sort of personnel contracts and policies as do governments. The question I find most vexing is
why privatization happens and where would you expect it to happen? I would like to point to two different forms of pressure that might lead to privatization.

First, there are fiscal pressures on enterprises which increasingly make efficiency gains from privatization important. As people become more concerned about the amount of money the government takes out of their pockets, as you have restrictions that require certain states or localities to operate on a balanced budget, and as the federal government’s phenomenal budget deficit looms larger in people’s minds, there is an increasing incentive to try to find sources of efficiency gains.

Second, you would expect people to start looking for those gains in areas where rents are low. It will be cheapest to get an efficiency gain where you do not have a strong group that has pushed for and obtained a sizeable rent — although the gain will also be smallest in those cases.

BLUNDELL: I think that until one has freedom of entry, one is essentially dealing with a political process. In contracting out and in franchising, for example the bureaucrats, the contractors, and the politicians may all be trying to see the different ramifications of contracting out or franchising. But until you have freedom of entry, you have a political process, not a market process. Once you have freedom of entry, this will allow the market to act as a discovery procedure, finding different ways of doing things, and trying new things which are unimaginable and unknowable to the bureaucrat, the politician and the contractor who were previously sitting around trying to decide what to do. They may certainly replace an existing public service by contracting it out to the private sector. But when the thing goes out on contract, they will essentially replicate what was done before, little innovation goes on. If you have freedom of entry, people are able to come in and try new things; they may innovate and offer different services. It is market process versus political process that provides the litmus test; it is these ideas we should use when discussing the definition of privatization.

BUTLER: Why does privatization occur? I agree in part with what Ron Cass said, but I think things are a little more complex. The fiscal pressures he has mentioned are in practice a key factor in moving toward privatization in this country — certainly at the municipal level. It is also increasingly the case at the federal level. The only reason that Congress is looking seriously at privatization is because of the deficit.

CASS: As to John Blundell’s point, although freedom of entry is very important, it is not the whole ball game. For even if you merely substitute a private
monopolist for a public monopolist, you do change the way the system works. I will give you just one example: cable television. The common provision of this service is on a monopoly basis in any given political jurisdiction (although the Supreme Court has recently told us there may be some significant problems with that). The contracts that are made by the public bodies in question usually confer benefits on particular groups—notably city councilmen. They always insist on channels that cover city council and related activities, that are available on the basic (non-optional) systems, and that give the councilmen free publicity. The private contractor always knows that the viewership rate for these channels tends to be slightly less than that for random scanning across channels, as is viewership for nearly all public access programming. The history of these franchise agreements fits a fairly clear pattern. The suppliers of the service usually make lavish promises of things that the city councilmen or other well-entrenched groups wish to see. A year or so later the cable operators come back and say that their projections were wrong: some of these services are just too expensive, so they will have to drop some or else they will need a massive rate increase to stay in business. The services that there are pressures to drop, when there is a profit motive involved, tend to be the services that are least desirable from the consumer standpoint. This suggests that services that are provided directly to and paid for directly by consumers differ in kind from services that are provided on their behalf and which they do not have an opportunity to choose.

BLUNDELL:
I think the changes that one sees when one goes to contracting-out or to franchising are pretty marginal. What, for example, is the optimum size of the firm to be delivering a service? In a political process, the size of the firm is set by the political boundaries—the boundary of Fairfax County, of Wichita, or of Pima County, Tucson. It might be that garbage is more effectively removed by a huge company covering all of Virginia. We just do not know. Until you have moved to direct provision of services to consumers, with freedom of entry, you will not get major changes. A whole industry—say the garbage industry—might soon not exist in any recognizable form if this occurs. If it happened, there would be a huge incentive for entrepreneurs to find new ways of removing garbage. It could be that every American kitchen will eventually be fitted with a superb new machine which lasers the garbage away. We just do not know. It is unknowable and unimaginable to us. Without freedom of entry we are not going to get major changes. In many areas where there is no freedom of entry there is just no change. Take the design of the telephone. In Britain, the telephone company was a monopoly and for years the design of telephones didn't
change. They were the same color — black. Then barriers to entry were removed; within a year there was an explosion of designs, memory functions and who knows what else. Free entry is the key. Bureaucrats, politicians and contractors sitting around a table cannot make these discoveries. They can make some minor alterations. The pressures on them to do that were described in the case of cable television. But you do not get any major change without freedom of entry.

POOLE:

John Blundell is right that innovation is more likely with freedom of entry and true competition. But the case for time-limited franchises for services and delivery is more powerful than he is implying. In fire protection, significant innovations have been brought in by the handful of private, for-profit companies that exist primarily in the West. This is the one place in fire protection where entrepreneurs have had some freedom to try out new ideas. They have not faced a bureaucratic structure and long-standing traditions. Companies have thus come in with new technology and radically different ways of organizing people and equipment, — and they have cut costs by forty to fifty percent. In addition, in Arizona we see economies of scale. A firm such as Rural Metro may have contracts with a number of adjacent or nearby cities — so it is not limited to the boundaries of one jurisdiction. It is able to invest in certain procedures and equipment that can be shared by several areas. This would not be the case with a typical government operation. So, some of the features we would like to see in a strictly open entry system situation we do find occurring in situations of time-limited monopoly franchise within a geographic area.

As to Ron Cass's comments about fiscal pressures and what motivates privatization, fiscal pressures are necessary but not sufficient. A lot depends on other variables such as the political culture of an area. There were great fiscal pressures in New York City during the 1970's with the de facto bankruptcy of New York City. There were also great fiscal pressures in California once Proposition 13 was passed. In California, those fiscal pressures led to a significant degree of contracting-out and user fees. I am not aware of any significant increase in contracting-out or user fees — at least, legal ones — in New York City following the fiscal crunch and the restructuring of the mid-1970's. My explanation is that the political culture in New York City is much more rigid, and that decision making there is much more in the control of successful rent-seekers, such as the public employee unions, which are able to resist change. Those structures are not as deeply embedded in California. This is perhaps because of the shorter period of time involved: compare here Mancur Olson's argument about how societies be-
come encrusted over time with interest groups, which rigidly maintain their positions.

MANNE:
We have previously considered some of the advantages of privatization; we discussed free entry. Other issues that will come up include incentive and motivation. It seems to me, however, that there is another side of this coin — one that has not been adequately covered in the literature. Gordon Tullock's notion of "government failure" — introduced as a parallel to the popular notion of "market failure" — has not had the full exploration that it deserves. While direct incentive effects have been examined, and we have some theories about bureaucracy, almost all the standard economic literature about private markets has parallels in discussions about government. Take externalities. Everyone is familiar with the externality argument for market failure. But the same is true of government. One of the things that we never count up in assessing privatization is the fact that every accretion to government activity has external effects. It popularizes the idea of government activity it strengthens the political position of government employees and it conditions popular attitudes.

PAGE:
I would like to make a couple of observations about free entry. First of all, the mere fact that you have a single provider does not mean that you do not have competition or free entry. The market may be contestable, and that may provide an effective constraint by competition.5 Second, I fail to see why a monopolist does not have the incentive to minimize cost and maximize profit. The argument that John Blundell offered was similar to the old idea of x-inefficiency: that a monopolist, because he is not subject to competition, has a tendency to become slack, and that this is a source of inefficiency even greater than the allocational inefficiency associated with monopoly.6 I am persuaded by Stigler's attack on that idea;7 it seems to me that there is no good reason why the monopolist would not want to make as much money as possible. If a new idea is available for, say, a garbage pick-up, why it couldn't be sold to a monopolist for him to maximize his profit is unclear to me. It seems that the major difference is between the profit motive and the absence of it.

GILLETTE:
I am very sympathetic to Ron Cass’s notion that economies and diseconomies of scale are important in generating efficiency. But this does not necessarily lead me to a desire for privatization. If economies of scale seldom coincide with jurisdictional boundaries, then public provision of a service by a particular jurisdiction solely to the residents is almost certain to be inefficient. Thus, if privatization simply means that a particular locality contracts out with a particular contractor, then the jurisdictional boundaries for the provider are not necessarily altered.

On the other hand, governments may be able to realize certain economies of scale. This is a function of the growth of special districts which cross jurisdictional boundaries, such as school districts, firefighting districts, and park districts. If regional solutions are underused, then the appropriate solution may lie in more regional government rather than substitution of any government with bifurcated privatized services.

BUTLER:
Government failure and negative externalities have to be put into the debate if we are talking about privatization as opposed to government provision. One should also remember, however, that there is also significant potential for public objectives and positive externalities to be achieved through privatization. Examples include public lands and public housing.

CASS:
I want to get back to the definition of privatization. I do not think anybody is arguing that if you have a monopoly provider who is chosen by the government, is told what to do by the government, and is regulated by the government, but gets to distribute whatever money is left over at the end of the day to a set of stockholders, that the world changes nearly so much as when you open up an activity to purely private provision. Nor do I think anyone is suggesting that user fees are identical to purely private provision. Clay Gillette is right that it is not necessary that contracts with a private producer give you the optimal scale. Nor is it necessary that public provision will give you a suboptimal scale. But it requires some effort to move from a political jurisdiction that is fixed for other purposes to the optimal scale. The minute you bring in private enterprise with a profit motive, and people are bidding for the franchise, someone who has a scale of operation that allows him to be more efficient will win out. In instances where municipalities have contracted out for power, or for cable, the franchise tends to go to a larger scale enterprise that operates in a number of other places. When other towns find their neighbors getting services for much less money, or better services for the same money, this leads to pressure to contract out in the adjacent areas.
VELJANOVSKI:
In the British debate, there has been a tendency to confuse three things. One is ownership, the second is monopoly, the third is scale. In Britain, nationalized industries cover the whole country. It is hard to disentangle whether inefficiencies are due to monopoly, to public ownership or to the particular structure of the nationalized industries — the controls on them. Nationalization usually means taking into public ownership and creating a monopoly at one and the same time. But it is not clear to me that a nationalized industry must operate more inefficiently. For the objectives of nationalized industries are quite different from the objectives of a private monopoly. The typical objective of a nationalized industry is the provision of a universal service. A nationalized industry may pursue this objective very efficiently. But this objective is not the same as maximizing profits, so we must look closely at what we mean by efficiency.

The crisis of nationalized industry was a question of controls. Financial or economic controls were placed on the nationalized industries because there was concern that if left to their own devices they would operate inefficiently. But nationalized industries, which were supposed to be separate from the central government, eventually became an instrument of macroeconomic policy. They had to keep their prices down to control inflation; they had to invest in the regions to check unemployment there in line with regional policy. They may have pursued these goals efficiently, but they were not the declared goals of nationalized industries. It is a messy picture when one looks at the reality of nationalized industries. And when making comparisons between public and private firms, we are talking about two organizations that have different objectives. To say that a nationalized industry is operating inefficiently because you are comparing it to a profit maximizer is not playing the game.

KOMESAR:
I am also concerned about the definitional problem. We have not yet made clear how we treat the removal of a service from the public sector, which is accompanied by substantially increased regulation. There may be a net loss here.

The issue, again, requires an understanding of government decision making. What political forces are operating and what protections exist when a service is handled directly by government, as opposed to contracting it out but then substantially controlling it through some regulatory agency? The public decision maker may shift from a more observable legislative entity to a less observable regulatory entity. Under those circumstances, special interests may operate even more effectively, making sure there is either too much
of a service provided or an inefficiently delivered service with substantial rents.

There is another form of decreasing government activity and decreasing the public budget which I think no one would consider an advance. It might be claimed that it is costing too much to provide high quality public housing, and that what we need is not public housing but rent control. Rent control is a way of allocating provision to the private sector in theory, and also providing a public service, seemingly at no cost to the government.

One other problem is posed by the fact that we are dealing with a wide range of public services. Some have easily defined purposes while for others these purposes are very difficult to define. The more complex the package, the more likely it is that one can provide a rationale for a complex regulatory scheme in which a lot of behavior is hidden.

ELLICKSON:

Have we any data on efficiency gains stemming from the privatization, say, of British Gas? I should caution that measurement of changes in the value of the shares in British Gas would not be dispositive because the initial sales price should reflect anticipated efficiency gains.

CASS:

Footnotes — and — in my paper list the sources of such information. The reason why there are two separate footnotes is because the studies cited come to different conclusions. The sources in footnote — conclude that the private provision of a whole range of services gives efficiency gains apart from changes in competition and scale. The studies in footnote — suggest, to the contrary, that most or all of those gains were accounted for by the introduction of competition. Intuitively, I am persuaded that both competition and the use of private sector incentives play a role.

The examples in which we can see a change from monopoly to competition are complicated because they are combined with changes in the regulatory regime. In this country we had an explosion of new technologies introduced in telecommunications. That was not simply the result of introducing competition into what was formerly a monopoly. One of the reasons why AT&T was so slow to introduce new types of phones was that the pressures from the FCC and other regulatory bodies to keep rates down for certain payers had forced AT&T to adopt a depreciation rate, which meant they were keeping on their books large amounts of equipment that was not worth its book value. Had they been able to write it off more quickly, they could have introduced new telephones and sold them. But as long as there was no competitor there, it was, under this regulatory regime, to the monopolist's advantage not to do so. As Bill Page argued, this does not show that the monopolist would have behaved in this way simply by virtue of
being a monopolist. Stigler and Posner have argued that the monopolist will capture all the efficiency gains that he could obtain by making improvements. But I am still not convinced that pushing things through a single funnel — through a single set of decision makers — does not restrict the decisions that you get at the end of the pipeline. The monopolist has an incentive to innovate. But there may simply be something in the process of having a thousand monkeys and typewriters that will give you some increased chance of having an innovation occur.

ALEXANDER:

We have assumed that privatization entails a shift from a property regime of government or state ownership to a property regime of individual ownership and that those two regimes exhaust the possibilities. We have neglected co-ownership. But which of individual ownership and co-ownership constitutes privatization? If both can fit within some satisfactory definition of privatization, which one of the two is more satisfactory?

Consider again the sale of public housing. Privatization could take one of two forms. It could involve the sale of the entire project to one individual or firm, or it could involve the sale of the entire project to all of the tenants under some financing arrangement. In choosing between those two, if one of the objectives of privatization is political — i.e., of reducing the risk of coercion of individuals — it seems to me that the latter form of privatization is more desirable. For under the former, all we have done is to substitute one arrangement which creates opportunities for coercion and lack of control by individuals over their own lives, for another.

We ought to avoid using caricatures here and assuming that government is bad. It is difficult to argue with Henry Manne, because government is fat and sassy. But individual ownership by one firm, or perhaps even one person, is not necessarily better because it may not be any more lean and mean than government ownership. Privatization could well take the form of co-ownership which, at least with respect to the political objectives of privatization, might be more desirable than individual ownership.

MANNE:

But this neglects one theme that Ron Cass emphasized earlier as underlying any notion of privatization: the creation of private property rights which must be transferable. Of the two situations you discussed, one is a case in which the housing project is transferred to a monopoly owner — in effect, for management but nothing else. In the other case it is transferred to a kind of ownership co-op or something of that sort, for management but nothing else. In either case, transaction costs aside, if you give transferable property rights, it will eventually end up in the same hands...
ALEXANDER:
Transaction costs aside is a very large caveat!

SHEARMUR:
It is not obvious to me that what we are looking for in appraising privatization is just efficiency. For one might also ask who are going to be the eventual gainers and losers. One issue that we have touched on before, but which I would like to bring out more fully, is the issue of those people who have, prior to privatization, been doing very nicely in extracting rents from the rest of us. Here we reach a problem. For those who advocate privatization often suggest that we should identify these people, and then buy them out, using the expected efficiency gains that one can get from privatization. But the motive for privatization might not be efficiency gains at all, so much as our thinking that we want to get off our backs people who have simply been exploiting us. If one takes this view, it is by no means acceptable that one should have to buy off these exploiters.

WITT:
I would like to follow up Ron Cass's point about deregulation resulting in a greater number of market participants, thereby unleashing innovation and efficiency gains. Consider the new economic freedoms of the transportation industry in the late 1970's and early 1980's. Following deregulation, there has been innovation in this industry. Critics had initially said that service to the small markets and rural areas would decline. But just the opposite occurred. In the trucking sector, 14,000 new firms sprang up and carved out a niche as a result of the relaxation of government regulation. In the airlines, the hub and spoke systems developed. This example may help us fill that void in Ron Cass's public-choice theory. Perhaps a prescriptive use of theory may here be made. There is a risk of re-regulation, particularly in the rail sector and also to a lesser degree in airlines. Shippers and carriers alike are banding together to hold the line and counter the efforts of vocal, well organized minorities who claim to be captive carriers and are seeking to re-regulate the railroads.

NORTON:
We need to look at the extent to which the goals and values of services being provided are governmentally selected. Many of the services we are talking about are going to be provided by private markets such as utilities and housing. Other services — such as historic preservation or preservation of the environment — might not be provided by a wholly private market to the same extent as they would by various governmental programs. The structure of privatization programs reflects the values with which those programs are established. For example, if the selected goal is efficiency, then it certainly makes sense to allow resources to be shifted out of the hands of
the least efficient and into the hands of the more efficient. If a program's goal is something other than efficiency, then the structure might disallow transfers. For example, much of the land in Alaska was transferred into the ownership of Alaskan native corporations. There is a major issue under consideration now whether to allow the individual natives who are stockholders in those corporations to sell that stock to other private individuals. If the goal is to protect Alaskan natives because of a governmental determination that those natives need protection, the program is not going to accomplish that as well by allowing them to transfer their stock ownership, as other adult human beings are allowed to do.

Another aspect of privatization that must be considered is the procedural requirements that are placed on a privatized operation. Government is inefficient in part because of procedures like the National Environmental Policy Act\(^8\) or the Administrative Procedures Act\(^9\) or various planning statutes. These require the government to go through elaborate processes for decision making when a private corporation could bypass all of those and just do what makes sense under the circumstances. If we apply those same procedures to the private companies or individuals that would be taking over governmental functions, we would not see the efficiency gains that we might see otherwise.

MANNE:

I would like to pursue further Gale Norton's suggestion, using the problem of housing. Like any other economic resource, housing is scarce; there is not an infinite supply. If you start from the status quo, you see that there is a problem: public housing doesn't work — it creates slums and bad domestic situations. You therefore get proposals that something be done about it. You might sell it to a corporation. You might give it to the tenants or sell it to them at a discount. Their interest might be transferable or not transferable. You might impose rent controls, or rules against the eviction of tenants for non-payment of rent. Squatters may be allowed to stay in abandoned or empty housing.

AHRENS:

In government programs or in decisions about privatization, there is often no clear conception of the program's goals. In the absence of some conception of what these goals are, it is very difficult to make any judgment about the merits of different privatization proposals. But this raises issues about the essential role of government as opposed to the private sector:

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mental philosophical issues that we cannot resolve in a two day or three day conference.

MANNE:
I think you are wrong when you say we do not know what our goals are. Everybody acting knows what his goal is. The people who live in housing units know exactly what they want. The politician who is trying to maximize votes knows exactly why he is doing what he does. The companies that bid to take over those housing units and run them know exactly what they are doing.

AHRENS:
Supposing you are right, while each of us individually may know what our goals are, what of when we are acting collectively?

MANNE:
My theory that people act out of individual self-interest explains a great deal more than if you assume that when people make these governmental decisions they in some sense collectivize their mentality. Now, I know they have to compromise with others, but that doesn’t mean...

AHRENS:
We are not acting collectively, we are acting in concert, very often for goals that are not compatible, and often convincing ourselves, perhaps, that we are acting for compatible goals. We are often acting in ways that will produce an outcome that is totally inconsistent with our individual goals. That is why we need some clear statement of what we are trying to accomplish with privatization. For it may not be acceptable to any of us.

GILLETTE:
I understood Ron Cass to be saying that one of the advantages of the private sector over the public is that the former has a more unitary conception of its goal than does the public. He suggests that, largely for that reason, the private sector is more capable of achieving its goal than is the public. That notion is appealing, as long as we assume that the goal that the private sector is seeking is profit maximization. But in talking about the experience in England, there was reference not to efficiency but to universal service. If profit maximization is not the sole goal, there may be an advantage to having decisions made through a sector in which different perspectives as to what ought to be done can be articulated. That internal debate may frustrate the achievement of any one of the goals. But it does suggest, and I think this is consistent with what John Ahrens is trying to get at, that there is some inherent value in the debate itself.

NORTON:
I would like to elaborate on the point I made earlier. We can arrive at goals and values outside of the governmental sphere. Individuals may choose
what they value and use their personal resources to provide it. When we were talking about the expansion of government through some types of so-called privatization, we were talking about the expansion of the ability to impose politically selected goals over and above those that private individuals select. In determining how privatization should be structured, we need to look for those ways in which governmental selection of goals and values — and thereby diminution of personal liberty — can best be avoided.

MANNE:

During the break, Neil Komesar suggested that the British may have moved to a more costly system. From a neat government agency that one could identify and complain about forever, they are now embroiled in a system of private ownership with monopoly, regulation, administrative lawyers, and so forth. It may not be worth it.

BUTLER:

Some people explicitly support the idea of privatization on the grounds that this would create lobbies for more spending by the federal government.

MANNE:

That, in turn, leads to another point. During the early heyday of deregulation, many people considered deregulation and privatization simply as instruments for government to use in the pursuit of its ends. They were regarded merely as one of the policies that government officials with power to decide things select from among. Deregulation got the support it did from some law professors because they thought: let's deregulate and make those sons of bitches suffer competition. It was a way of beating up on businesses.

POOLE:

I think there is a significant danger of creating constituencies to lobby for more government spending when contracting out, as we have seen with defense contractors. I find it interesting that in about ten years of speaking on the subject of privatization, it has only been in the last couple of years, particularly last year, that these problems have been raised. Perhaps more attention has been focused on defense costs, and scams and scandals. Questioners now regularly ask: If contracting out is so good, how come we have these $3,000 toilet seats, and $500 hammers in the Defense Department? There is a potential problem that contracting out can create such constituencies. As Stuart Butler has pointed out, some people in social services and health care are quite aware of this and think that may be a reason for the expansion of contracting-out.

On the other hand, I am not persuaded that John Blundell's model of free competition in garbage collection is really applicable in many areas of public service that local governments deal with on a daily basis. We have for
years tried to figure out a viable, totally free market alternative in, say, emergency ambulance service or fire protection in urban areas. Housekeeping services, such as street sweeping and park maintenance, seem to lend themselves much more readily to contracting out as opposed to the creation of a truly competitive market place with open entry, just because of the nature of the service. It is not that I have a preference for contracting out. I simply have not been able to see a practical pure privatization alternative in a number of services. Garbage collection and a few others are exceptions. In a great many things that state and local governments do, if we are going to have some sort of private sector involvement, contracting out seems the only way of trying to introduce efficiencies by harnessing the profit motive. This means competition for a limited time contract as opposed to open competition of the kind we can have in the provision of fast food, clothing and many other consumer goods.

One could certainly posit models of open competition in emergency ambulance response or fire service. But I cannot imagine how those propositions are politically feasible, how they are saleable in realistic terms. Even if we were all advocates of free markets, would we even then choose to have competing fire protection companies in an urban area or competing ambulance companies rushing to pick up the accident victims in the middle of an intersection? We simply do not have good working models of how to do that on the basis of open competition.

CASS:
John Ahrens earlier suggested that goals in government are not very well specified. He is right that even when we can predict what the various players in the system want individually, when they compromise they frequently adopt solutions that do not clearly settle on one goal but on some mix of goals. By so doing, they send signals to those who are going to implement the goals that are not very clear. That, of itself, provides additional opportunities for the implementers — the public employees — to follow goals of their own.

MANNE:
I do not think that enormously complicated procedures, including compromise, mean that you do not still have a minimax, optimizing strategy pursued by a lot of individuals. Everyone will attempt to identify his own interest with some broader general interest. But I think we will confuse ourselves if we address policymaking by talking as if the government had goals.

WITT:
From Bob Poole's perspective, the negative result of privatization is that in addition to creating constituencies of special interest groups, it also risks
solidifying the government's role as a provider. This is particularly the case with contracting out. Consider loan asset portfolio sales, where we contract out collection while doing nothing to reduce the role of the government as a lender. By doing this, we are creating a very powerful special interest among the Wall Street investment banks and other purchasers of the government loan portfolio. If they realize that there is money to be made from the sales, they will then apply pressure on government to expand its role as a lender. I believe we should exercise great caution in these "half-way" measures and should really be focusing on getting the government out of the business of making these loans, rather than merely improving the collection.

ELLICKSON:
I will attempt to answer a question that Henry Manne posed earlier: If one were to wish to privatize government housing, what route would one choose?
The simplest course would be to sell this housing in fee simple to the highest bidder. There are several ways to protect any reliance interests of current tenants. They could be given transportable housing vouchers equal to the value of their prior arrangement, rights to retain occupancy of their current units at a certain rent for a certain time, or financial assistance in purchasing their units.
We should recognize that property regimes have external effects on the structure of social and political life. Much of the debate over public housing thus rightly concerns whether collectivized ownership and management enhances or detracts from the social life of tenants. There is an important political side to these issues as well. One of the reasons that Social Democrats in Scandinavia have favored government and housing-association housing is that those who live in these collectives become more likely to cast votes for Social Democrats. Homeowners, by contrast, are more likely to adopt a conservative perspective on issues such as the level of property taxes. Margaret Thatcher, for example, knew that the sale of local council housing units in Britain would generate more Conservative votes. Thus, housing tenure policies feed back upon the political process.
Collectivists and individualists will disagree about the desirability of these second order social and political effects. Efficiency considerations, however, should matter to both groups. For me, the wastefulness of the public housing program is by itself decisive. Analysts have concluded that public housing authorities are inefficient producers of housing services and that housing
voucher assistance programs are more cost-effective. The federal government therefore should encourage public housing authorities to unload their public housing units.

MANNE:
What prospects are there for unloading public housing?

ELICKSON:
I'm pessimistic. The political momentum behind this idea seems to have peaked several years ago. When housing authorities tear down failed projects these days, they tend to replace them with new ones. They throw good money after bad. I know of no major public housing authority in the U.S. that has substantially liquidated its operations.

MANNE:
What would be the resistance to simply giving the property to the tenants who are there now? Where would the objection come from? It would not be immediately effective because you would have so many people who would benefit.

BUTLER:
It is relatively easy for public housing administrators to persuade tenants that this is against their interest, that they will be left with something that may be an enormous cost which they cannot bear. It is not in fact true in many instances, but the costs of ownership do frighten some tenants.

VELJANOVSKI:
A major criticism that has been made of the British privatization program is that it has multiple objectives. Some have claimed that it really has no coherent objectives at all, and that the government is just seizing on a number of objectives to justify its program. Some say it is about efficiency. But if we accept the self-interest model of politicians, we must ask: What are the payoffs in moving from nationalization to privatization?
Second, I think people are getting a bit carried away as to what will happen with regulation in the U.K. It is not going to be a profitable activity for lawyers because there are no public hearings. It will all be determined by the relevant Director Generals of regulatory commissions after some public consultations. However, the whole process of state intervention has become more apparent. For now a Director General will publish a report that explains why he has made some decision, and he will explain the basis on which it has been made. It will no longer be done by civil servants and the heads of nationalized industries behind closed doors.

One final point is that the threat of privatization has had a dramatic effect on a number of state-run enterprises. Previously, many of these industries did not have proper accounting procedures. The threat of privatization has forced them to put their accounts in order. British Telecom did not even know how much it cost to provide services to a particular area. But company law requires that you have to have five years trading accounts before a company can be publicly listed — so they have had to get their accounts in order. This has had a dramatic effect because now they really know where the money is going. The anticipation of privatization — getting everything in order — and doing battle with the government, civil servants and merchant bankers and being questioned very carefully, may have all had a very good effect. This may lose its momentum after a while, but a good accounting system will always be there.

MANNE:
Would you be confident that the American experience with judicial review and administrative action will not have any influence in England?

VELJANOVSKI:
This I would like to explore. But the scope of judicial review is very narrow in England compared to what I perceive it to be in this country.

BLUNDELL:
Henry Manne asked why we do not give public sector housing away. In England, when the Conservative Party was trying to decide how it could get rid of some six million public housing units, which constituted about one-third of the total of housing stock, the two most important reasons advanced were: first, the existing owner-occupiers. They had saved and paid mortgages for years and had also seen the people in public housing being very heavily subsidized for the whole period. To give these people their houses would be extremely galling, very unpopular politically. Second, an argument was advanced that the people should pay at least something, that people do not value what they get for nothing.

BUTLER:
I agree with you totally about the debate in Britain. I remember it well. But there have been U.S. housing programs which essentially almost gave housing to the people, under section 235. But they had no equity in it. That led to a lot of abandoned housing in the section 235 housing: roofs leaking and the owners without equity deciding they did not want to spend anything on them and just walking away.

In the case of federal contracting out under the A-76 program, agencies are required to look at services of a commercial nature, and to evaluate the cost of in-house provision as opposed to having an outside contractor. It is argued that even in those cases where the in-house services continue, there is
a reduction of cost because those providing the services in-house are forced to look at the efficiency of their operation and improve it.

POOLE:
I wanted to follow up a little on Stuart Butler's point about the threat value of privatization in this country. There are many examples of the threat to contract out a service being a force for lowering its cost in the public sector. I have been told many anecdotes of companies in the garbage collection and fire protection fields, lamenting, having spent a significant amount of money traveling to a city, and preparing and submitting a proposal, only to find out they were simply being used as a way to bash the union in order to get them to agree to a more reasonable settlement. There was not a serious intent of contracting the service out at all. But it was a wonderful threat, and produced cost savings that were otherwise unattainable.

Phoenix, Arizona has taken something like the federal A-76 contracting-out provisions, but instead of having the department itself doing the cost comparison study, the City of Phoenix has a separate accounting department. It produces what appears to be realistic cost studies of the department's operations, including an appropriate share of overall city overheads and all kinds of things that are often left out, and compares those with bids from outside firms. Over the last six or seven years they have had thirty-five or forty competitions between city employee work forces and outside bidders. Almost two-thirds have been won by outside firms. But the interesting thing is that one-third have been won by the work forces themselves. They have had the incentive to restructure their way of doing the work so as to lower the cost, in order to save their jobs from the threat of outside competition. This has been quite an experiment to see the scope for cost savings that exist within the public sector, given the spur of competition.

WITT:
This point about the threat of privatization resulting in some positive effects shows certain similarities to William Baumol's theory of contestable markets.

CASS:
It has been suggested that there are instances where a government operation is replaced by the combination of private operations and government regulation, and it makes the world much worse. Neil Komesar used the example of public housing — of the government getting out of public housing and substituting rent control. But has this ever happened? Or does not the existence of public housing help feed the incentives for rent control? Are not public housing and rent control more tied than substituted one for the other? Second, is there evidence of concrete situations where government has gone from a wholly-owned government operation to private contracting
and made things worse? We have heard about the ills of defense contracting. But I am not persuaded that we would be a lot better off if the government built all the weapons for us.

POOLE:
In answer to Ron Cass's question, the American Federation of State, County, and Municipal Employees (AFSCME), which is the largest public employee union at state and local government levels, has been collecting anecdotes about failures of contracting out over the last six or eight years. They have published two books containing some fifteen or twenty such anecdotes. Given the motivation and the resources available to AFSCME, these may be all the cases in which that sort of thing has happened. If they had large scale systematic evidence, they would certainly have included it in their books. I would suspect that the cases in which things actually do get worse, after service is contracted out, really are the exception rather than the rule, at least over a ten year time frame.

SHEARMUR:
In Britain the public service unions have assembled evidence about some problems, — especially where cleaning services have been contracted out. The clearest case, however, concerns one council which moved from running its own gardening services to having them contracted out to a company which had never actually done garden contracting before. More seriously, there has been quite a history of difficult cases where a particularly labor-intensive form of provision has been contracted out. There have been savings, but people have been employed only on a part-time basis and at not terribly good rates. They have also been given heavier work loads, and what have retrospectively been judged to be positive features of work practices have been cut out. These things can be, and have been remedied. But such cases are to be found.

GILLETTE:
If we have complete contracting out, we simply do not know how the public sector would have behaved in the same situation. What one would really hope for are situations in which the public and the private sectors compete — as might be the case where public and private schools coexist in the same jurisdiction. One situation which might provide a fruitful mode of analysis could be something like the check collection system. In this, the Federal Reserve System is in direct competition with local clearing houses. The Federal Reserve System comes out very well in inter-jurisdictional check collection. But in the exchange of in-town checks in larger cities, the banks will tend to use their own local clearing house rather than the Federal Reserve. What is more, the check collection system of the Federal Reserve
Bank operates at a profit, although it is possible that there are hidden subsidies.

MANNE:
We might now consider the different forms of privatization, perhaps starting with the denationalization of nationalized industries and working right down to the government staying out of the matter entirely and not caring what happens. Each of these has peculiar pluses and minuses. There are strong ideological issues here, and there are then peculiar externalities from the effect of an accumulation of government activities. It will also be useful to frame the question of whether there are legal barriers to the form of privatization that is being considered.

VELJANOVSKI:
The most common technique for the sale of state assets is the sale of shares to the public — the public flotation. That has taken place in two ways: by a public offer at a fixed price or by tender where the market sets the price. Shares are offered and people make bids and then they have a striking price. Tender offers have typically been undersubscribed. There has been one unique case of a workers buy out. In the National Freight Corporation, the workers and management got together with the backing of merchant banks. There have also been management buy outs, such as in the National Bus Company. This has been split up into regional areas and management has bought out many of the small bus companies. The Naval dockyards have been put out to tender. The technique with the highest political payoff has been the sale of shares at a fixed price. That has got the most publicity and has been responsible for the threefold increase in individual shareholding in the U.K. It has been one of the objectives of privatization to increase shareholding. Since 1979, the surveys indicate that there has been a threefold increase in the level of individual shareholding, largely due to privatization in British Telecom, British Gas and the Trustee Savings Bank. British Telecom brought in about two million new shareholders, many who had not owned shares before.

There has been much discussion as to whether that is a sensible way to introduce people to the stock market and about people selling their shares at a great profit. It is hard to tell whether the increase in shareholding will be lasting because various loyalty incentives have been offered to shareholders who hold onto their shares. For example, for British Gas shares you get gas vouchers that entitle you to a discount on your gas bill.

MANNE:
There are proposals here to only allow shares to be voted if they have been held for a year or two years. Irving Kristol has recently put that idea for-
ward in *The Wall Street Journal* as a way of stopping tender offers. For if votes cannot be transferred no one has any interest in the matter at all.

BUTLER:

We might consider further the implications of various forms of buy outs in Britain. These secure the acquiescence or support of rent-seekers in the public sector. They are persuaded to accept or endorse movement into the private sector by stock options and so forth. Vouchers might also be given to the users of electric power in, say, the Northwest, to secure their support for denationalization. Currently they have every reason to oppose it, on the grounds it will lead to more market-based rates — which generally mean higher rates.

It might be worth looking at the potential for bringing about improvement in the economics of a denationalized firm through the use of these buy outs. It is generally assumed that if you use part of the assets to buy out a constituency, that hampers the long run economics of its denationalized activity. In the case of National Freight Corporation, which Cento Veljanovski mentioned, by changing the ownership structure to bring in the employees, privatization changed the incentives and the attitudes in the workforce. In that particular case this led to a remarkable improvement in the performance of the company concerned.

One thing that has come to interest me concerns the less developed countries, especially in Central America. The sharing of privatized assets through the workforce builds up a vested interest in the performance of a capitalist economy. There has been growing interest in the idea of spreading capitalism through the workforce by means of some kind of ownership method like that in the National Freight Corporation. This is having a political impact when previously the only alternatives were corrupt centralized capitalism or various forms of socialism.

MANNE:

What you are saying is perfectly consistent with a description of a cooperative venture, but not of a corporation with freely transferable shares. A great many workers do not have a comparative advantage as capitalist investors. In a real free market system, these things will separate out. The improved workforce morale may be a fairly temporary effect. The cooperative system also builds in its own incentives for free-riding and shirking just as much as does external ownership.

If someone has some shares, he perhaps has an incentive to work a little differently. But the additional work may constitute a return on those shares of pennies, while the same individual's shirking may be worth thousands to him or her.
BUTLER:
I am not sure I agree. Certainly when we look at cooperative management, or the cooperative ownership of public housing, or the NFC in Britain, somebody's actions may have a very powerful benefit to themselves and yet may add very little one way or the other to the cooperative whole. Nevertheless, there tends to be enormous peer pressure on them . . . .

MANNE:
That is right. If the group is small enough for it to do self-monitoring, it is not such a problem.

SHEARMUR:
In Great Britain, the government is trying to encourage individual shareholders — in the hope of changing attitudes and as a barrier against renationalization. However, some British companies have at the very same time been trying actively to discourage small shareholders, as they find them an expensive nuisance.

A proliferation of naive small shareholders may also pose transaction cost problems for the market for corporate control.

POOLE:
I want to draw our attention to the tremendous opportunities for changing the boundaries of political feasibility that are suggested by some of the experiments that have been tried in Britain. If you look at the postal service in this country, for example, one of the major perceived barriers to any sort of privatization or denationalization has always been the opposition of the Postal Workers Union. This is one of the strongest lobbies in the country. Yet the postal service, with its strong unions, has always been in government hands. We may compare it with British Telecom. The telephone system in Britain was always a part of the post office structure. Four or five years ago it was reorganized to make two separate branches, the postal branch and what has now become British Telecom. British Telecom has now been successfully privatized, with the support of over ninety percent of the workforce who accepted the offer to become shareholders at a big discount, against the advice of an active union leadership and of the Labour Party. This device of giving them a say, giving them a piece of the action, totally changed what would have been seen as a political impossibility into not only a possibility, but a political actuality. There is much the same kind of potential in this country to expand the boundaries of what we can talk about as being politically feasible in getting enterprises out of government hands and into the private sector by using similar approaches.

One other example is that the people at PERC in Montana have done a lot of work over the last six or seven years on trying to marry free-market economics and environmental concerns. They have made outreach efforts
to various organizations and have actually had some degree of success in getting some environmentalists to apply market principles.

CASS:

I want to divide up cases of the privatization of government assets into four groups. First, there is denationalization — the selling of a nationalized industry as a monopoly. A second case is denationalization in combination with opening up the company to competition. Third is the sale of a government business that isn't a monopoly. Fourth is the sale of assets that constitute less than an entire enterprise.

The first group involves a nationalized industry being sold as a monopoly. There are not all that many of these to discuss in the U.S. Probably the only industry which comes readily to mind is the postal service. It would be much more efficient if we were to sell it off and open it up to competition. But I am not sure that some of the suggestions that Bob Poole has of ways of softening political opposition would then work. If we open it up to a competitive market, we may have difficulty finding funds to buy off the existing workers. These are workers who are able to capture an enormous amount of money from their ability to exclude competition, and by excluding the rigors of private management. If you were a private entrepreneur, what would you pay to get a piece of the postal service that is no longer going to be a monopoly? You will not capture the welfare losses that are now being suffered. You will only be able to earn a competitive rate of return. You will have difficulty in figuring out what share of the market you will end up with. By and large it would be unlikely that you would find private buyers who would be willing to fund buy outs of the shares held by the postal workers. So I am not sure that we will be in a position to buy them out except by government action where the government itself would have to provide the funds.

WITT:

I would like to focus on the political and legal dynamics of labor protection provisions, particularly as they result in obstacles to privatization. I am confused as to when an employer/employee relationship transforms into an entitlement. I see a parallel between a firm shifting from the public sector to the private sector and a firm relocating from a unionized operation in the North to a non-unionized operation in the South. Labor unions try to attach labor protection provisions restricting the economic freedoms of private owners — an example is route abandonment restrictions for railroads. These firms are often compelled to engage in inefficient operations or incur great liabilities or enormous costs. Such political obstacles to privatization are typically means to pacify or to increase the attractiveness of privatiza-
tion to vocal rent-seeking special interests. When, legally, does a public sector employer/employee relationship constitute an entitlement?

MANNE:
Dan Witt articulated an undercurrent in much of our discussion that somehow the rents that unions are receiving because of constitutional political activity should not be protected as an entitlement, a property right. I do not see it that way. It is a reality of life that they do have it. Too much of our discussion related to the government selling off an asset at the right price or to someone’s not being benefited with a windfall. I think that misses the point. These are all political actions and the political response is going to reflect the power of whomever has those entitlements. We should not kid ourselves about finding some optimal price level for selling and then not providing benefits to the airline pilots or the railroad brotherhood or whomever.

VELJANOFSKI:
I agree with Henry Manne entirely. One has to recognize that one is in a political, not a commercial setting. The trade-offs are quite different. In Britain, the Labour opposition said that the government was ripping off the taxpayer. But the government decided that it is better to be accused of giving things away than for the program to be politically unappealing to the electorate.

GILLETTE:
Henry Manne is quite correct in his assumption that there is a strong political component to privatization. It is evident in Dan Witt’s justification for the movement in terms of the economic freedoms of the owners of productive resources. I take him to be suggesting that pursuit of economic freedom requires strong limits on governmental intervention. But someone on the other side of the privatization issue could argue in favor of governmental intervention by focusing on the economic freedoms of the employees. Let me give an example drawn from the current debate concerning plant closings. We are seeing a development of a substantial amount of legal theory by attorneys for labor unions. One of my colleagues at Boston University is currently writing an article on “The Reliance Interest in Property Law.”11 His work draws from existing common law principles about relationships and the duties that accompany relationships — from marriage relationships to employee relationships — to suggest how long-standing relationships can trigger certain entitlements that prevent the individuals from simply walking away. My guess is that in coming years we will see increasing development of such theories that advocate increased govern-

mental intervention in an attempt to limit plant closings, or to uphold statutes that run the entire gamut from pre-closing notification requirements to a substantial payment from the owners to the employees, or to a municipality that deems itself to be adversely affected by the closing. Each of these will be justified in terms of advancing economic freedom: not the freedom of the owners, but the freedom of the employees. I am not sure that we can short cut this discussion by moving to slogans, such as the economic freedom of the owners or the employees. We must instead ask ourselves whether any proposal — viewed from the perspective of the society as a whole — achieves some approximation of an optimal allocation of societal resources.

POOLE:
Several people have looked at the U.S. Postal Service as a potential corporation that could be sold through shares. The first thing we have to realize is that a restructuring would take place before any sale, figuring out what kind of shares would be given to the workers in order to gain their allegiance and what, if any, protections for rural areas would have to be part of the deal. Those factors would all be decided as part of the package prior to privatization. The market would then have to reflect the value of a postal corporation with those provisions attached. But people I have been talking to in this field think that, even with provisions like those attached, you have here practically an AT&T. It would have a giant head start on anybody else in the field, for the important reason that it has prime real estate in every city in the United States. No one else has an equivalent set of locations. The real estate also probably has a market value of ten or twelve billion dollars if it were sold off.

Second, given the freedom to operate as a business, albeit with competition allowed, there is a market value to being able to do things like get into electronic mail without the political restrictions Congress placed on the postal service. They had a brief foray into it, did badly, and were then forbidden by Congress to have any further involvement. In addition, unlike UPS or Federal Express, the postal service has never been allowed to purchase its own fleet of airplanes and build a central hub for overnight resorting of mail to new destinations. They were under a political constraint, for it was said that this would be damaging to the airlines or to AMTRAK. Free of such restrictions, the postal service as a private postal corporation would also be free to be a full-fledged competitor in overnight premium delivery in a way that it cannot be now. So there are a number of competitive freedoms that would go along with a competitive postal divestment that really do make it a viable proposition in which people would buy shares.
NORTON:
There are two types of restrictions upon privatization. The first are constitutional entitlements. I agree with Ron Cass that these are not severe impediments to privatization. Second are those procedural requirements that would be imposed, such as employee protection. Those, for the most part, could be dealt with by adjusting the price that would be paid for the business. Alternatively, Congress could deal with some of the statutory prohibitions and procedural requirements by means of overriding legislation. The political solution of having Congress state what would continue to apply to those businesses would be preferable.

I would also like to discuss the privatization of public land. One possible process is dividing up various interests in a piece of land and selling them separately. The subsurface interest could be sold separately from the grazing or hunting interests. Various private actors with interests in the land would preserve much of the same interests that government ownership was intended to preserve, since each owner could legally protect the reasonable exercise of his ownership interest. Another possibility is land exchange. It is one way of serving the interest of government in preserving environmentally sensitive lands yet trying to get some of the more productive lands into the private sector.

VELJANOVSKI:
Henry Manne has referred to the political bargain of privatization. This explains why major utilities have not been broken up, because one has to buy the agreement of management, and management is not about to give their agreement if their power and empire is going to be split up. That is one of the reasons why the privatization of these industries is really the enemy of more competitive pressures, at least in the short run. In the long run, of course, one can renege on the bargain.

MANNE:
I do not think it requires reneging. All it requires is recognizing the value of their claim currently and giving them a transferable interest. Over time, secondary markets develop and those things take care of themselves. Trouble will always arise if you try to make these political bargains look like a real commercial venture with correct pricing.

ALEXANDER:
I want simply to underscore the point made by Dan Witt and Clay Gillette concerning entitlements. It just will not do to say that if employees have entitlements, so be it. For the question then comes up: would you extend the same attitude to the private sector? Plant closing cases directly raise the question of legal constraints on employers — on their freedom of movement because of the existence of entitlements. Consider United Steelworkers
Union v. U.S. Steel Corporation. The plaintiffs in that case, two locals of the United Steel Workers Union in Youngstown, Ohio, brought an action seeking to enjoin U.S. Steel Corporation from shutting down and moving two of its plants in Youngstown. They ultimately lost, but it is very clear from the court's opinion that they lost only because, in the view of the court, the plaintiffs had not offered an established legal basis for an entitlement.

What is striking about the court's opinion, and the opinion of the district judge, was how they appealed to the plaintiffs' lawyers and to legal scholars to attempt to develop a legal foundation for such an entitlement on the part of the union and cities like Youngstown. Since then a number of lawyers and legal scholars like Joe Singer have attempted to develop such legal theories. Thus far, the legal theories seem to be proceeding along two lines. The first develops a notion of individual entitlements that are based or derived from contract law analogues, specifically the reliance interest or to adverse possession in property law. The second attempts to develop group entitlements. That is, an entitlement recognized as held by a group, as distinct from individuals who are members of the group. This line of reasoning is not nearly as well-developed as the former, but it is beginning to get a number of people's attention. It is based on a theory of existence values. It seems to me that if one is talking about legal impediments to privatization, Dan Witt and Clay Gillette are right that the question of entitlements is going to loom larger.

ELLICKSON: Our discussion is proceeding on the assumption that there is a clear-cut dichotomy between public and private enterprise. This may not be a useful way to conceptualize the problem. Dahl and Lindblom have argued that there is a spectrum of public and private involvement in institutions. In the case of a full-blown federal agency, for example, civil service rules would apply to its employees, the OMB would approve its forms, the GSA would buy its pencils, and its managers would be appointed by the President. Other federal institutions — Fannie Mae, perhaps CONRAIL as it is currently organized — have less "public" involvement. They buy their own pencils, can hire more freely, and so on. Advocates of privatization, rather than demanding a total public-to-private switch, can instead push for a partial relaxation of government control and involvement. The postal service is an example of partial privatization.

12. Local 1330, United Steel Workers v. U.S. Steel Corp., 631 F.2d 1264 (6th Cir. 1980).
13. See Singer, supra note 11.
There is also a danger of taking formalities such as title too seriously. Who holds title to public lands, for example, may signify little. Ski areas on public lands are under leases that are nominally short term but, in practice, the leases have always been renewed. To a great extent, the federal government has divested those lands. The story with grazing leases is largely the same. If the federal government were to sell these lands outright, but were simultaneously to step up its regulation of the use of those lands, the net effect could be less privatization.

PAGE:
In the context of government ownership, there may arise rents or political interests that must be recognized in any kind of privatization decision, whether or not they would be recognized in a private context by a court as property rights. The political calculus of how to bring about privatization would have to take account of them.

How, then, can privatization occur in a public choice world? Those who wish to bring about privatization are behaving in ways that can be illuminated by what public-choice has said about the dynamics of interest groups. For example, the underpricing of government assets is an instance of concentrating the benefits in a particular group and spreading the costs over a larger group. This is a classic device used by special interest groups in obtaining regulation. The direct buy out of those who are benefited by government regulation is another such device.

SHEARMUR:
I am very unhappy about this issue of entitlements prior to privatization. If people know that such pre-existing de facto "rights" will be recognized, and thus legitimated, that would seem to me to create enormous rent-seeking opportunities. Thus, in Britain, prior to the denationalization of the British Airports Authority, there was an enormous investment on the part of the managers of that company to avoid the major airports being broken up into competing concerns.

Second, the work referred to by Clay Gillette and Greg Alexander is most interesting. But suppose it is shown that arguments from common law imply that certain such rights should be recognized. Should we conclude that such rights should in fact be recognized? I do not see why we should expect ideas deriving from common law reasoning always to be compatible with what is in the public interest. To suppose that there is such a link is almost to appeal to a pre-established harmony between the wisdom of history or the law on the one side and the general interest on the other. If a case can be made out on common law grounds for "entitlements" in the Youngstown case, then I think that this would be a prime example in which common law should be overturned by a legislative body, if it can take such an action.
MANNE:
I suspect your remark reflects a certain cultural bifurcation between English and American law.

CASS:
I want to second what Bill Page said about legal and political entitlements being somewhat different. Legal entitlements may or may not exist in areas where political entitlements do.
I think this ties in with Henry Manne's comment on the question of whether we should be worrying about those entitlements, or just accept them for what they are and focus on what the correct price is. I am willing to accept them for what they are, but he is too sanguine. While there is a right price at which you can divest any government asset, the political question is whether the capitalized value of capturable gains is sufficient to pay off the capitalized value of rents. For the fact that there may be social gains that exceed the rents from the divestment of government assets does not mean that any group is going to control those gains in a way that will facilitate their action in the political process, unless we believe the political process works fairly well to maximize social welfare. What we really are looking for is a way to get the payoff, if there has to be a payoff, made in a form that does not affect future marginal costs. We have to look for someone who in the short term is willing to absorb, in a very visible way, the costs that have been incurred from past governmental and regulatory decisions. One of the few things that we can tell from observation of the political process is that relatively few politicians are willing to incur short-term, highly visible losses to establish greater, longer-term less visible gains for the general public.

This brings me to Jeremy Shearmur's point about the relation of positive law to political interest. Positive law does considerably affect political realities. The middle part of my paper, which was trying to explore what the law was, was also intended to examine whether people who disagree with privatization arguments are right in arguing, first, that government promotes social welfare; and, second, that privatization often reduces social welfare. If either of these claims were correct, we might expect to see a variety of inhibitions on privatization in the law. Or, at least, if there are constitutional inhibitions on privatization, they might be explicable by this sort of reasoning. The absence of significant legal (constitutional) constraints on privatization has some impact on the normative debate. I do not hold this out as strong proof of any normative proposition, but the absence of constitutional inhibitions upon privatization is at least possible evidence that there is not a strong consensus that privatization as a general rule is bad.
GILLETTE:
The possibility of renationalization might raise issues about the wisdom of engaging in privatization in the first place; at least it may lead us to distinguish between asset sales and the sale of services currently provided by government. This is especially important with respect to the ownership and use of public lands.

Many legal doctrines can be explained through a reference to a desire to reduce error costs. Often, when we engage in presumptions in the law it is out of a desire to reduce error costs. Now, one may link this with the desire to engage in privatization. This suggestion assumes that markets do not always work perfectly. If that is right, it is possible that we might someday find ourselves in a situation in which, after privatization, we decide that something has gone wrong and that some service was better provided under governmental provision than it is being done in the private sector. If there is a possibility of that kind of error arising, in a situation in which a government has sold off the provision of services, then the costs of getting it wrong are relatively small. Government could re-enter the field and the dead weight losses that would have arisen as a result of leaving the service in private hands could be readily corrected. If, on the other hand, we are talking about the sale of assets that are not easily replenishable — for instance, the sale of mineral exploration rights on public lands — and we somehow get it wrong (and if there is a lag between the time that something has gone awry and the time we discover it), it is much more difficult for government to intervene and return us to the status quo ante.

KLAUSNER:
If the government has the short-term horizon attributable to a term of office or the next campaign, it is hard to see why you could have a more optimal allocation of resources with government ownership.

MANNE:
Bob Ellickson suggested that transferable property rights subject to restrictive government regulation may be less desirable than non-transferable rights which the government is managing by, say, allowing private operators to run ski slopes under contract or graziers to use government land. I think this is a very important point. The only point on which my feeling runs counter to Bob Ellickson's is in my broader sense of the importance of alienability. There is a tendency to look at the picture at the moment: one sees hillsides covered with snow, happy skiers going down them, and happy ski slope managers taking in money just like private entrepreneurs. The problem comes if gold is discovered under that mountain fifty or one hundred years from now. There is no device whatever for adjusting to the new circumstances. There is an enormous cost whenever we politicize such
things, even if the current result of the political operation would be considered optimal by positive economists.

Second, if you recognize claims such as those of the Youngstown steelworkers, you are making a reallocation of wealth. As long as you have a status quo and people understand it and you allow transferability, the market works things out — barring transaction cost problems. The difficulty comes when you change the law. The question here is: are we creating something new, or are we properly recognizing something that already existed? I think we have to say that it did not already exist in the U.S. Steel case. The question then is: who should be required to pay, if in fact we are going to recognize something new here?

GILLETTE:

Let me turn to the issue of attention to the long-term and Henry Manne's example of discovering gold under the ski slope in one hundred years. Implicit in Henry Manne's comment was that the skier's association might block a more publicly beneficial use of that land. The public choice literature argues that the time horizon of political actors is limited to the next election. But the question is — with whom are we comparing them? A burgeoning literature has argued that middle management decision makers also have a relatively short-term view — often even shorter than the next election. It has been argued that their time horizon is limited to the next quarter's balance sheet. If that is true, I am not sure what leads us to believe that political actors will have a shorter time horizon than private middle managers. The issue really is, does anyone discount to the future very well? If we are talking about the future effects of current activity, then the closer we get the easier it is for even short-term decision makers to adjust prices for what will happen in the future. But if there are discontinuities — if we do something today with the ski slope that prevents us from taking advantage of the gold under the ski slope which will not be discovered for one hundred years — then, of course, the time horizon issue becomes more important.

One thing must be added to this, which goes back to Ron Cass's point in his paper about the multivariant versus the unitary objective of the private and public sectors. I take it that within certain public sector departments, such as the Interior, there is, in fact, a multivariant analysis of what it is we ought to be doing. Some people in Gale Norton's department believe that you should preserve — not just conserve — the environment; retain it as God made it in its pristine beauty. Their concern is not for the maximization of profits, as it would be in the private sector. If that is correct, the ongoing debate within the public sector may lead to the possibility of reducing error costs in the future. Those who argue that we should not develop
wilderness lands because they have an ideological concern for preservation would presumably exclude development in the long term as well. Such a position may lead to under-utilization of social resources. But if we are concerned about making errors in situations where undoing a choice would be costly, it may be desirable to make an initial choice — i.e., not develop — that reduces the costs of “getting it wrong.” Perhaps we should take this into account in the initial decision whether or not to privatize in particular cases. It would be most compelling in the case of asset sales of non-replenishable natural resources, as opposed to services provided by government.

KOMESAR:
Since the 1930’s most people would agree that the courts have stayed away from controlling governmental decisions which increase regulation. These decisions have, for the most part, been given very little scrutiny. The one exception has been the courts’ recent interest in commercial speech. In reality, this is a return to the examination of a sliver of special interest legislation.

The courts’ interest in commercial speech reflects a distrust of special interests. Why then doesn’t the court return to review commercial regulation as a whole? One answer is that the area is too immense. The lesson from commercial speech is that if the courts could shave off part of an old problem and address it — that is, special interests in the political process — they may be willing to do so. Could the courts be convinced that a form of privatization was rare enough — and dangerous enough — that they could handle it by reviving a doctrine like delegation? It is unlikely that the courts would overlook attempts to privatize which closed conventional public forums like airports for first amendment activity. They could handle such a case of privatization under traditional doctrine, and, in that way, limit their role. So, I would not be completely certain that the courts would take no role reviewing privatization.

ELLICKSON:
Henry Manne was right in the ski slope example. Transfers in such cases are incomplete in a variety of ways. The leases may not be freely alienable and they are not leases in fee but rather leases for partial uses. In theory, however, the federal government could lease in fee simple, transferring for the term of the lease mineral rights, the rights to operate a ski resort, and the rest of the bundle of sticks. These leases could, in theory, also be freely alienable. If leases were in fee simple, freely alienable, and infinitely renewable, in practice the system would be much like fee simple land tenure.

ALEXANDER:
Concerning positive law, it seems to me that we ought not to be too sanguine about the strength of the legal policy of alienability. It is the conven-
tional picture, the picture that property lawyers conventionally draw. But in terms of both legal history and extant legal doctrine, there are many examples of inalienability, imposed directly or indirectly through tolerance of nominally privately imposed inalienabilities. So, the legal policy of alienability is not all monolithic and there is no clear linear trend strongly favoring alienability.

Second, the justification for inalienability. The legal system does not always tolerate or itself impose inalienabilities on the basis of paternalism. Paternalism is, of course, probably the most familiar justification for inalienabilities. But it is not the only one. Another justification, developed by a number of property lawyers in recent years, is what we might call the preservation of self-identity. This, I take it, is in large measure what Margaret Jane Radin has been attempting to work on.\(^1\) In the context of public lands, the argument can well be made that there are benefits from inalienability, with respect to the protection of the community's sense of itself — of what its character is, what its heritage is, and of what our popular culture is. These benefits may not be adequately reflected in the conventional market process. This presents a proper role for government to impose inalienabilities in order to preserve and protect those benefits of self-identity. Now that justification is at least not nominally a justification derived from paternalism. It seems to me extremely important to keep the two strands separate when one is attempting to mount an argument against inalienability.

CASS:

Clay Gillette made the point that political managers may in fact have longer-term goals than do private managers, because private managers will focus on the next quarter whereas political managers will focus on the next election. It may be true that private managers often have a short-term focus. But whatever their focus, it is likely to be quite congruent with the focus of other people in the same enterprise. Now private enterprise is characterized by a lot of institutions that make it much more likely that all the diverse interests will fit together and that the managers will serve them than is true in public enterprise. Just because private enterprise does not work perfectly to harmonize the interests of managers with those of investors or employees, I would not go to the assumption that we can find a general advantage in the political system. In the political system, ideology plays a role. In part, that reflects the failure of mechanisms that harmonize diverse interests in political enterprises to do so nearly so well as they do in private enterprise. It is difficult to imagine a meeting of a board of directors

of a publicly held company that operates for profit at which someone says: I know this may cost us a billion dollars, but I think it is important to invest in this particular enterprise in order to show our commitment to poor people. Rather, that would be grounds for removing somebody from the board, unless he can tie his proposal to some additional payoff for the company, in terms of dollars and cents. This is not to say that people in business do not have ideologies. But the much greater role that ideology plays in government traces to the fact that government exercises coercive power and resolves disputes in public, whereas in the private sector, by and large, there is the opportunity for less public dollar trade-offs which enable us to harmonize diverse private interests.

A second question is whether in some instances the private actors who might be given responsibilities over some class of decisions really have some interests that are not congruent with social welfare. Are there systematic incentives to engage in behavior that is publicly bad? It may be that the risks are externalized, or resources are used too freely because more valuable uses are not captured in a form that allows for competition for those resources, and so on. This brings us back to some of the public interest rationales for government operations. I am certainly willing to credit those as being good reasons in principle for government to be engaged in certain types of asset management or other activities. I just have some doubts as to whether in fact government operations will prove consistent with those aims.

KLAUSNER:
There are two resources available within the private sector that are not available to government. One is the existence of privately held companies that do not have the same kind of concern for short-term earnings as do publicly quoted companies. The other relates directly to the issue of alienability. It is the existence of corporate raiders. For while they cannot realize the assets of public corporations, they certainly can do so if they are held by a private company where stock is publicly traded. This changes the whole argument; it isn’t enough just to look at middle managers’ incentives.

MANNE:
There is plenty of evidence that there is all the difference in the world between the planning horizon of private property owners and their agents in a well functioning system that monitors them and, on the other hand, government or political planners. You cannot find a utility function for the government official that will give any kind of logical interest beyond the next election, or something very close to that, whereas the private owner who does not take the real discounted value of future events into account simply
loses money. It makes no sense, and it invites takeovers, unless the managers’ compensation is tied to current accounting measures.

CASS:
I would like to come to Clay Gillette’s defense, for I think that Henry Manne overstates the case. Take a look at a President in his last term. He knows that for him there is no next election. Quite clearly, he is worrying about his place in history, and is looking at how people will discuss his actions when he is gone. He is not making unconstrained individual decisions, but he is able to have an effect. There are people in the political system who have a long time horizon, although they may have quite peculiar individual conceptions of what the social interest is over the long term.

NORTON:
One of the things that Clay Gillette was talking about is trying to introduce long-term predictability into the process of land preservation. Looking at this from the perspective of the Department of the Interior, there are many ways in which the political decision making process tends to go against long-term predictability. Clearly we have our strong preservationists within the Department of the Interior. But we also have the Bureau of Reclamation and the Bureau of Land Management, people who manage oil and gas leasing, and several other groups that are often opposed to the preservationists. So we have our own internal political battles over the policies of the Department. One would tend to think that this would bring us to a balanced outcome. In fact, the issues become fragmented. The Bureau of Reclamation goes forward with its development projects and the National Park Service goes forward with its preservation projects — each has its own group of projects.

Transferability is certainly one way to allow reality to enter into our decisions on how to utilize resources. But the system could be designed to allow for transferability and yet have some brake on the process, so that we do not have a jump from full preservation as wilderness or full historic preservation to full development for commercial purposes. At one extreme, covenants could absolutely prohibit the use of land other than for preservation. But we could, for example, have an easement to the Sierra Club or an environmental group that could be bought out if the economic incentives were high enough. We could have tax incentives that would encourage preservation and yet allow strong enough developmental pressures to override preservation. The idea of long-term leases as opposed to transfers is very attractive. It is politically more saleable than actual transfer, and if it allowed for the weighting of various interests it could be very attractive politically. Another mechanism that has been studied is the trusteeship concept, which is described in several articles by John Baden and Rick
For example, environmental groups appointed as public lands trustees could have responsibility for taking into account economic pressures on those lands, and could perhaps decide when it is time to develop.

POOLE:

On time horizons, I think it is hard for non-economists, unless they have been immersed in literature on efficient markets, to understand how markets really do take into account these best guesses at future values. It may help to mention some current empirical evidence that supports that general conclusion. People who looked at recent targets of takeovers tried to test Robert Reich's theory that what you are seeing is a function of short time horizons and too much focus being placed on the next quarter's profits. It had been claimed that American firms are not investing enough in R & D because the managers are so afraid of takeovers that they skimp on R & D in order to have current profits looking good, so they will not be targets for takeovers. It turned out that the firms that were targeted for takeovers in the last few years were the ones with lower than average R & D expenditures. Firms with robust R & D expenditures have not been takeover targets at all. The market values their shares higher because they are thought to be making the right kinds of investment for the future. This is one illustration of the kind of thing that Henry Manne was talking about. The market may not work perfectly, but you have to ask: compared to what? When discussing making guesses about the future, we must ask: are the guesses of government managers better than the whole messy set of guesses made by people concerning their future money invested in shares?

Another piece of evidence on this comes from PERC. They look specifically at the time horizons involved in managing renewable resources such as timber. They have looked at the differences between timber cutting firms when they operate on leases on government lands, where they have a short-term right to cut timber, as compared to how they conduct their timber harvesting on lands that they own and which show up as assets on their balance sheet. We see much greater stewardship of the long-term value of that land as timberland when it is on the balance sheet of the timber company as opposed to where they have a short-term contractual right to grab as much as they can. Again, if there is a transferable right to the property, each piece of timber shows up as an asset on the balance sheet. There is then an immediate response in terms of the value of that company if they practice environmentally destructive practices, rather than maximizing the long-term value of that valuable resource as a source of future income.

GILLETTE:
I would be surprised to hear evidence contrary to what Bob Poole just suggested about timberland, in large part because there the environmental concerns coincide with the profit concerns. The question is, to what extent do the two coincide? The problem arises most concretely where there is not a continuous curve in which you are steadily depleting resources that may be replenished, or where one can invest in substitutes for them so that R & D becomes important. Now discounting by any standard discount rate, e.g., ten percent, by and large ignores everything that is going to happen more than twenty to twenty-five years ahead. The problems really arise if what we are engaging in today produces adverse effects with a long latency period. Assume something like toxic waste disposal in which, if the drums in which the toxic waste is disposed corrode, this will not happen for a substantial period of time.
Are they going to be taken into account by the current managers at all? Would you rather have such matters handled by the public sector or the private sector if you were looking at the incentives for taking into account such long-term effects? Certainly managers twenty years from now, or even ten years from now will want to take these things into account, because past acts may now be sufficiently salient to affect the value of their company's shares. Within a time horizon that currently affects the value of the shares they may engage in a search to try to reduce their potential liability. But if the risk, once created, is like a time bomb that cannot be defused, then even the managers who prudently wish to address the issue may be unable to do anything meaningful about it.

The concerns that I am addressing may affect only a very narrow range of activities; but they are, nonetheless, very real. With increasing technology, my guess is that we will see increased numbers of situations in which these theoretical concerns could materialize.

KLAUSNER:
As to market fallibilities versus government fallibilities, which works better and which worse? I think the key is a developed system of property rights. The use of covenants can be very effective in giving an entry to ability. I also think that it is the optimum system for protecting against the evils of toxic waste disposal. There is a very good anecdotal example to help illustrate that point — the infamous case of Love Canal. Love Canal was a case where many believe that the real villain was the private sector. Hooker Chemical used Love Canal to store toxic waste. Later, development occurred and a lot of people who bought homes in the area were very distressed to find out that there were these horrible things in the ground beneath them. Who was the villain? It turns out that the villain was not
Hooker Chemical. They operated in a very responsible way; environmentalists should applaud what was done. Knowing that there were toxic wastes on the property, Hooker Chemical gave the property to the school board with a covenant running with the land stating that portions of the property should never be used for development.

POOLE:
It wasn't Hooker's idea in the first place to deed the land. They did so under the threat of condemnation. They sold the land for one dollar and with the covenant running.

KLAUSNER:
It was the school board that had its eye on this land. If the land had been condemned, the government would take title with no constraints running with it. The company, rather, sold it for a buck so they could impose a covenant preventing its use for development. There were subsequent hearings, when the school board wanted to sell off the property to developers. Hooker — surprising as this may sound to those who think these things do not happen in the private sector — actually sent representatives to meetings of the zoning board to protest any transfer of that property to a developer for the reason that there were severe environmental hazards. Notwithstanding Hooker’s opposition to it, the school board transferred the land to a private developer.

POOLE:
The most outrageous thing was that the city subsequently put storm sewer lines right through the walls of the canal. This created a leachline system to spread the toxic chemicals throughout the surrounding neighborhood — as if they were designing a septic tank leachline system.