

## Essay

# “Public Utility” Regulation: Some Economic and Moral Analyses

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*This Essay analyzes various economic and moral issues that relate to the actual/alleged unregulated conduct of public-goods producers, public utilities, and “businesses affected with a public interest” (including businesses engaged in common callings and common carriers) as well as to government regulation of these categories of businesses. It begins by criticizing the conventional definitions of “public goods” and “public utilities” and explaining why, on its original definition, “businesses affected with a public interest” were not simply “businesses whose decisions affected the public interest.” It then explains why the fact that one or more of the goods that an otherwise-Pareto-perfect (oPp) economy could produce were “public goods” would result in economic inefficiency. Next, it analyzes how the economic-efficiency problem posed by public goods and the economically-efficient response to them are affected by the reality that the relevant economy is not oPp. The Essay proceeds to explain why “fair-rate-of-return public-utility-pricing regulation” renders it profitable for regulatees to make otherwise-unprofitable decisions and delineates the variety of such inherently-unprofitable choices that such regulation renders profitable. It then discusses how these so-called Averch-Johnson-Wellisz (AJW) effects of such pricing-regulation complicate the task of public-utility regulation and raise the possibility that government production of the goods produced by public utilities may be more desirable than the public regulation of private production of these goods. This Essay comments on the way in which the fact that the relevant economies are not oPp affects the economic efficiency of the various AJW effects and complicates the task of regulating public-utility pricing. After that, it provides short accounts of the different types of moral analysis that are relevant to the assessment of the moral character of the choices made by the types of businesses traditionally perceived to require regulation and of various regulatory responses that government could make to such businesses. It uses these accounts to assess various moral criticisms that have been made of such*

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*businesses and the moral desirability of the government’s regulating such businesses in different ways. The Essay concludes by listing some of the most important reasons why actual government business-regulations are less than optimal and outlining various policies that might improve the quality of government regulation of business.*<sup>1</sup>

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1. Key phrases: the Averch-Johnson-Wellisz (AJW) effect of “fair-rate-of-return public-utility regulation; the definition of “public goods,” “public utilities,” and “businesses affected with a public interest”; the distinction between the moral obligations of the government of and non-government actors in liberal, moral-rights-based States; the liberal conception of “justice,” “discrimination,” and “liberty”; non-liberal conceptions of the moral good; the Pareto-imperfectness of an economy and the economic inefficiency generated by public goods and AJW effects.

Introduction

The literature on “public utilities” and related commercial enterprises denominated “businesses affected with a public interest,” “common callings,” and “common carriers” (hereinafter “businesses traditionally perceived to require regulation”) provides a great deal of illuminating historical information and some useful economic and moral analyses. However, the existing literature is also deficient in several respects. It contains (1) some definitions of the individual enquoted categories of business that are not analytically useful and differ from each other in ways that their proponents fail to recognize, (2) some economic arguments that ignore or misanalyse some of the consequences of the conduct of or various public regulations of these categories of business because they implicitly incorporate unrealistic economic assumptions, and (3) some moral analyses and conclusions that are inadequately morally-grounded or conflate the moral and non-moral senses of salient terms. This Essay identifies and tries to remedy these deficiencies.

The Essay contains five parts. Part I discusses the respective definitions of “public goods,” “public utilities,” “businesses affected with a public interest,” “common callings,” and “common carriers.” Part II focuses on “public goods.” It begins by reviewing the conventional analysis of the economic-efficiency problems caused by “public goods.” Next, it explains that this analysis is based on an otherwise-Pareto-perfect (oPp) assumption that the only Pareto imperfection the relevant economy contains is the buyer surplus that would be generated by the supply of the public good if its supplier charged only a single per-unit price for the good—*i.e.*, that the economy contains no imperfections in seller competition, no imperfections in buyer competition, no (real) externalities, no taxes on the margin of income, no exemplars of resource-allocator non-sovereignty, and no exemplars of resource-allocator non-maximization. It concludes by examining how the reality that all economies are highly-Pareto-imperfect affects the analysis of the public-good problem.

Part III focuses on the Averch-Johnson-Wellisz (AJW)<sup>2</sup> effect of traditional “fair rate-of-return” public-utility-pricing regulation. It starts by explaining why conventional “fair-rate-of-return public-utility-pricing regulation” renders profitable otherwise-unprofitable regulatee-decisions. Next, it points out that the diversity of these AJW effects implies that public-utility regulators would have to control virtually all of the public utility’s decisions to prevent “fair-rate-of-return public-utility-pricing regulation” from generating such effects and any undesirable consequences that would be associated with them and suggests that the diversity of AJW effects raises the possibility that government production of the goods that public utilities produce might be more desirable than the

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2. See Harvey Averch & Leland H. Johnson, *Behavior of the Firm Under Regulatory Constraint*, 52 AM. ECON. REV. 1052 (1962); Stanislaw Wellisz, *Regulation of Natural Gas Pipeline Companies: An Economic Analysis*, 71 J. POL. ECON. 30 (1963).

combination of private production of those goods and government regulation of their private producers. Finally, it (1) demonstrates that the conventional implicit assumption that all AJW effects are economically inefficient is based on an oPp assumption and (2) briefly examines how the reality that all economies are highly-Pareto-imperfect complicates the analysis of the economic-efficiency consequences of AJW effects and the task of regulating public-utility pricing.

Part IV begins by stating my conclusions about a number of basic ethics positions and issues (moral skepticism and emotivism, the distinction between discourse about justice and discourse about the moral good, the different types of Foundationalist arguments that have been made for the existence of a universally-applicable concept of justice, the defining characteristics of various moral types of societies, the philosophically-informed empirical protocol for identifying the moral principle that a particular moral-rights-based society of moral integrity is committed to instantiating in the service of its conception of justice, the moral obligations and moral rights of the members of a *liberal*, moral rights-based society of moral integrity). It then analyzes the appropriate way to define “liberty” in a liberal, moral-rights-based society and the implications of that definition for the correctness of liberty-oriented criticisms of various government regulations of business in such a society. After that, it distinguishes two senses of “discrimination” and analyzes the implications of the discussion of “discrimination” for the claim that various types of “discrimination” in which businesses engage violate moral rights. Its last section considers the moral soundness of various other moral criticisms that have been directed at decisions of public utilities and other similar types of business enterprises.

Finally, Part V responds to the obvious reality that, even if the unregulated choices of businesses traditionally perceived to require regulation would be economically inefficient and morally undesirable, public regulation might not yield superior outcomes by briefly addressing the causes of sub-optimal government regulatory-performance and proposing some policies that might improve the quality of government business-regulations.

#### I. The Conventional Definition of Various Categories of Businesses Traditionally Perceived to Require Regulation

Part I discusses and in some instances criticizes the way in which the categories of commercial enterprises relevant to this discussion—“businesses traditionally perceived to require regulation”—have been defined in the literature. It begins with the concept of “a public good.” Economists usually equate “public goods” with goods whose marginal costs are zero or goods whose supply cannot be limited to potential buyers who have paid for them (goods whose consumers are in the above sense “non-excludable”).<sup>3</sup> However, the

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3. See, e.g., Gabriel Rauterberg & Andrew Verstein, *Index Theory: The Law, Promise and Failure of Financial Indices*, 30 YALE J. ON REG. 1, 38 (2013).

claims that economists make about the economic-efficiency problems posed by public goods imply that a good should be defined to be a "public good" if and only if two conditions are fulfilled: (1) its marginal cost curve (MC) is lower than its average total cost curve (ATC) at the output at which the demand curve for it (DD) cuts its marginal cost curve from above and (2) the average height of the demand curve for the good in question between output zero and the output at which its DD curve cuts its MC curve from above is higher than the height of its ATC curve at that output. This definition of "a public good" is less restrictive than either of the concept's two conventional definitions. Part II will explain the economic-efficiency problem any "public good" so defined would pose at least on the oPp assumption that conventional analyses of public goods implicitly adopt.

Typically, those economists who focus separately on "public utilities" equate them with natural monopolies—*i.e.*, businesses that operate in situations in which the quantity demand for their product at the price that equals the minimum average total cost of producing it can be supplied most cheaply if the product is produced by only one producer.<sup>4</sup> In fact, it would be more useful to define as public utilities any business operating in a situation in which significant economies of scale would have to be sacrificed for the number of producers in operation to be sufficiently large for price competition (and quality-or-variety-increasing-investment [QV-investment] competition<sup>5</sup>) to be perfect or (in some difficult-to-define sense) "acceptably strong from a policy perspective."

First articulated by the U.S. Supreme Court in 1877,<sup>6</sup> the legal concept of "a business affected with a public interest" has never been clearly defined. As originally conceived, businesses affected with a public interest" were businesses that, for some special reason, the State (the People) had an entitlement interest in regulating.<sup>7</sup> The concept was developed in a context in which government

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4. See, e.g., Yair Listokin, *Law and Macroeconomics: The Law and Economics of Recessions*, 34 YALE J. ON REG. 791, 846 (2017).

5. In my terminology, a quality-or-variety-increasing (QV) investment is an investment that creates an additional and perhaps superior product variant, an additional and perhaps superior distributive outlet, additional capacity, or additional inventory in a relevant (somewhat-) arbitrarily-defined portion of product-space (ARDEPPS). (When demand fluctuates through time, additional capacity or inventory will increase overall product-quality to the extent that it increases the average speed with which the non-delivery-time-defined product[s] in question will be delivered throughout the fluctuating-demand cycle.) In my terminology, "QV-investment competition" refers to the process through which investors reduce the supernormal profit-rates that would otherwise be generated on the QV investments in a given ARDEPPS by introducing additional QV investments into that ARDEPPS.

6. See *Munn v. Illinois*, 94 U.S. 113 (1877).

7. See *id.* Three types of interests or concerns can be distinguished. An individual has a "psychological interest" in something if the individual has a desire and proclivity to pay attention to it. An individual has a "material interest" in something (say, a particular act or social outcome) if that act or social outcome affects the individual materially. And an individual has a legal or moral entitlement interest in a decision or outcome if the individual has an interest in that decision or outcome that should be counted when deciding whether the decision or outcome violates a moral or moral-rights-derived legal right of the individual in question. To anticipate the text that follows, at least in the United States, the fact that someone has a psychological or even a material interest in something does not give him or her a moral-entitlement or legal-entitlement interest in it. Thus, the fact that I am psychologically interested in your

regulation of business was thought not generally to be morally (or constitutionally) permissible because it infringed the liberty interests of the owners of the regulated businesses. Hence, when, in 1934, the Supreme Court stated that “[t]he phrase ‘affected with a public interest’ can, in the nature of things, mean no more than that an industry, for adequate reason is subject to control for the public good,”<sup>8</sup> it was asserting a proposition that was not only linguistically incorrect but inconsistent with the moral premises of the original creators of the concept. I hasten to add that I agree with the 1934 Supreme Court’s conclusion that the State must surmount no special moral or constitutional bar to regulate businesses or business conduct in the public interest (because, for reasons that Part IV will explain, with one extremely-limited, contestable exception, business-persons have no liberty right properly so-called to make the decisions that such regulations would prohibit them from making).

I also am unaware of any formal definition of the concepts of “a public calling,” “a public service company,” or “a common carrier.” The list of types of businesses that were placed into one of these categories (that were in essence deemed to be “affected with a public interest” in the 1877 meaning of that phrase) grew from a short, early-common-law list (innkeepers, etc.) to include an astonishing array of business-types.<sup>9</sup> The determination of the types of businesses that belong in this list seems to have been based on an unexplained belief that the producers of particular goods and services had a moral obligation to supply them in acceptable quality at a fair or just, non-discriminatory price to all those who had the wherewithal and desire to buy them at that price (and to complete the supply of any good or service that the supplier had begun to supply). The preceding claim that these determinations were “unexplained” reflects the fact that no one ever justified the following conclusions: (1) all potential buyers have a moral right to buy or morally-ought to have the opportunity to buy at the same, fair price acceptably-good exemplars of certain goods and services but not of other goods or services; (2) the right to secure particular goods or services is a right to buy acceptable exemplars of them on non-discriminatory, fair terms rather than a right to be allocated them even if one cannot pay a non-discriminatory, fair price for them; or (3) any such moral right that does exist is a right against purveyors of the good or service in question rather than a right that the government secures that good or service for the right-holder.

## II. The Conventional Analysis of the Economic-Efficiency Problem Posed by

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sexual history does not in itself give me any moral-entitlement interest in obtaining information about that history. Or the fact that I would obtain buyer surplus by purchasing some product from you if you continued to produce and sell it does not give me a moral-entitlement interest in information about your relevant production-plans.

8. See *Nebbia v. New York*, 291 U.S. 502, 536 (1934).

9. See BRUCE WYMAN, *THE SPECIAL LAW GOVERNING PUBLIC SERVICE CORPORATIONS AND ALL OTHERS ENGAGED IN PUBLIC EMPLOYMENT* (1911).

Public Goods: Statement and Critique

A. *The Conventional Analysis*

The conventional economic analysis of the economic-efficiency problem posed by public goods proceeds on three implicit assumptions. First, the demand curve for the public good— $DD_{PG}$ —coincides with the marginal allocative value curve for the public good— $MLV_{PG}$ , which is the curve that indicates the net dollar allocative benefits that would be generated by the consumption as opposed to the allocative-costless destruction of successive units of the public good.<sup>10</sup> Second, the marginal cost curve for the public good ( $MC_{PG}$ ) coincides with the marginal allocative cost curve for the public good— $MLC_{PG}$ , which is the curve that indicates the net allocative benefits that the resources devoted to producing successive units of the public good would have generated had they been devoted to the alternative uses to which they would otherwise have been devoted.<sup>11</sup> Third and relatedly, the average total cost curve for the public good ( $ATC_{PG}$ ) coincides with the average total allocative cost curve for the public good— $ATLC_{PG}$ .

Here is the conventional analysis of the economic-efficiency problem that public goods pose:

First, if the prospective public-good producer is required to sell the public good once it creates it at the single per-unit price that will result in the production of the economically-efficient quantity of the public good (the price at which  $MLV_{PG}$  cuts  $MLC_{PG}$  from above and [on otherwise-Pareto-perfect assumptions] the price at which  $DD_{PG}$  cuts  $MC_{PG}$  from above), the public good will not be created. The single per-unit price that the public-good producer must charge for the economically-efficient quantity of the public good to be sold (the price at which  $DD_{PG}$  cuts  $MC_{PG}$  from above where, on the analysis' oPp assumptions,  $DD_{PG}$  coincides with  $MLV_{PG}$  and  $MC_{PG}$  coincides with  $MLC_{PG}$ ) will be lower than  $ATC_{PG}$  at the output in question. The resulting economic inefficiency will equal (the economically-efficient output of the public good) *times* (the difference between the average height of  $DD_{PG}=MLV_{PG}$  between output zero and the good's economically-efficient output and the height of  $ATC_{PG}=ATLC_{PG}$  at the good's economically-efficient output).

Second, if the prospective public-good producer is allowed to price the public good at the lowest single per-unit price it could charge for that good that would result in the height of  $ATC_{PG}$  at the associated output's equaling the price in question, the public good will be created, but it will be produced in an economically-inefficiently-low quantity. The fact that the price charged exceeds the marginal cost of producing the last unit of the public good that will be sold

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10. This assumption would be warranted if the economy were otherwise-Pareto-perfect and reductions in the per-unit price of the public good would not alter the dollar-value to their consumers of intra-marginal units of the public good by altering the real wealths of the consumers of those intra-marginal units.

11. This assumption would be warranted if the economy were otherwise-Pareto-perfect.

at that price implies that the height of  $DD_{PG}=MLV_{PG}$  will exceed the height of  $MC_{PG}=MLC_{PG}$  between the resulting output and the output at which  $MLV_{PG}$  cuts  $MLC_{PG}$  ( $DD_{PG}$  cuts  $MC_{PG}$ ) from above. The resulting economic inefficiency will equal the area between the  $DD_{PG}=MLV_{PG}$  and  $MC_{PG}=MLC_{PG}$  curves between the highest output of the public good at which the height of  $DD_{PG}$  equals the height of  $ATC_{PG}$  and the economically-efficient output of the public good (the output at which  $DD_{PG}=MLV_{PG}$  cuts  $MC_{PG}=MLC_{PG}$  from above).

Third, if the prospective producer of the public good is informed that (1) it will be required to sell the public good once it creates it at the sub-average-total-cost price at which  $DD_{PG}=MLV_{PG}$  cuts  $MC_{PG}=MLC_{PG}$  from above but (2) the government will provide a subsidy to the public-good producer equal to the loss the producer would otherwise sustain by creating the public good and selling it for a single per-unit price equal to the price at which  $DD_{PG}=MLV_{PG}$  cuts  $MC_{PG}=MLC_{PG}$  from above<sup>12</sup> or if the government creates the public good itself and sells it for the above per-unit price, economic inefficiency will be generated by the poll taxes or taxes on the margin of income that finance the subsidy to the non-government public-good producer or to cover the loss the government sustains by creating the public good and selling it on the stated terms. The relevant economic inefficiency equals the allocative transaction costs generated by the formulation, passage, and collection of the relevant taxes *plus* the economic inefficiency that the associated taxes on the margin of income will generate by rendering unprofitable economically-efficient decisions to supply market labor rather than consume leisure, to supply market labor rather than perform do-it-yourself labor, to save and invest rather than consume, perhaps to buy one good rather than another (depending on whether the relevant tax is a tax on earned income, a tax on unearned income, a tax on purchasing a good that varies from good to good, etc.).

Fourth, if the prospective public-good producer is informed that (1) once it creates the public good, it will have to sell the economically-efficient quantity of the public good but (2) it will be allowed to cover the loss it would sustain if the only price it charged for the public good were a per-unit price equal to the price at which  $DD_{PG}=MLV_{PG}$  cuts  $MC_{PG}=MLC_{PG}$  from above by charging higher per-unit prices for one or more intra-marginal units of the public good, by charging buyers that want to purchase more than one unit of the public good at the economically-efficient per-unit price a lump-sum fee for the right to do so, or by using tie-ins or reciprocity agreements to sell the public good, economic inefficiency will result for one or more of four reasons. First, all such pricing-techniques would be more allocative-transaction-costly to devise and implement than simple non-discriminatory per-unit pricing would be even if conventional price discrimination and the charging of lump-sum fees did not create an incentive for buyers to engage in arbitrage and the relevant tie-ins/reciprocity

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12. A subsidy equal to (the economically-efficient output of the public good) *times* (the difference between the heights of  $ATC_{PG}$  and  $DD_{PG}$  at that output).



agreements did not give one of the firms they involve an incentive to violate its contractual agreement to purchase its full requirements of one of the goods they involve from the other party to the agreement in question for a price that agreement specifies. Second, price discrimination tends to cause economic inefficiency by creating situations in which units of the good in question are allocated to buyers that place a lower dollar-value on them (that equals or exceeds the discriminatorily-low price they are charged for them) rather than to buyers that place a higher dollar-value on them (that is lower than the discriminatorily-high price these latter buyers would have to pay to purchase them). Third, the charging of discriminatory per-unit prices or lump-sum fees generates economic inefficiency by providing buyers with an incentive to engage in arbitrage. Some explanation is necessary. Such pricing provides buyers with an incentive to engage in arbitrage by reducing the price that some buyers would have to pay to purchase one or more units of the public good below the per-unit price or average-lump-sum-fee *plus* per-unit price that other buyers would have to pay the public-good producer for the units of the public good they could purchase from it. The creation of such arbitrage-incentives is allocative-costly (1) because the public-good producer will generate allocative costs to deter such arbitrage, (2) because efforts by the public-good producer to collect contract-damages from buyers that violate their contractual obligation not to engage in arbitrage will cause allocative costs to be generated by the public-good producer, the arbitrage-practicing buyer, and the State, and (3) because arbitrage-sales from an actual customer of the public-good producer to the buyer in the arbitrage-transaction will be more-allocative-costly (less-allocatively-efficient) than the public good producer's supplying the buyer in the arbitrage-transaction directly. Fourth, any tie-ins or reciprocity agreements that are used to overcome the public-good problem will generate economic inefficiency by providing the buyer/(one of the reciprocal traders) they involve with an incentive to violate its obligation to purchase its full requirements of one of the goods the contract involves from the other contract-partner on specified terms. Once more, some explanation is required. The relevant tie-ins/reciprocity agreements will provide one of their participants with an incentive not to fulfill its obligation to purchase its full requirements of one of the goods involved on specified terms because the full-requirements-purchasing obligation would be unprofitable for the relevant party if it were free-standing. This effect of the agreements in question is misallocative because it makes it profitable for the party that would profit from its contract-partner's fulfilling this contract obligation to generate allocative transaction costs (1) to detect and deter such contract violations and (2) to collect damages from contract partners that have failed to fulfill their full-requirements obligations.

On oPp assumptions, then, the fact that one of the goods an economy could produce is a "public good" will result in the generation of economic inefficiency, regardless of the response the relevant government makes to the situation.

*B. The Critique of the Conventional Analysis*

The conventional analysis of the economic-efficiency problem posed by public goods is valid on its implicit oPp assumption. However, its relevance is reduced by the inaccuracy of its (implicit) oPp assumption. This conclusion is warranted because economies are not oPp. Further, unless the effects of the other Pareto imperfections contained in a relevant economy perfectly counteract each other (as they will do only rarely and fortuitously), the economy's other Pareto imperfections will cause the relevant  $MLV_{PG}$  to diverge from the associated  $DD_{PG}$ , the relevant  $MLC_{PG}$  to diverge from the associated  $MC_{PG}$ , and the relevant  $ATLC_{PG}$  curve (the average total allocative cost curve for the relevant public good) to diverge from the associated  $ATC_{PG}$  (the average total [private] cost curve for that public good).

Whether the amount of economic inefficiency that an economy will generate because (say) one of the goods it could create was a public good will be greater or smaller than the amount predicted by the conventional oPp-assumption-based analysis depends on several factors: whether the curve-divergences just delineated (1) increase or decrease the economically-efficient output of the public good (cause the output at which  $MLV_{PG}$  cuts  $MLC_{PG}$  from above to be higher or lower than the output at which  $DD_{PG}$  cuts  $MC_{PG}$  from above), (2) cause the differences between the average heights of  $MLV_{PG}$  between output zero and various relevant outputs and the heights of  $ATLC_{PG}$  at those outputs to be higher or lower respectively than the differences between the average heights of  $DD_{PG}$  between the output zero and various relevant outputs and the heights of  $ATC_{PG}$  at those outputs, (3) increase or decrease the economic inefficiency that taxes that yield relevant amounts of revenue will generate by inducing resource allocators to make economically-inefficient choices, and (4) increase or decrease the ratio of the allocative to the private transaction costs that will be generated by the devising and implementation of a relevant tax, by the devising and implementation of pricing-techniques that involve price discrimination and/or the charging of lump-sum fees (arbitrage-problems aside), by arbitrage/(cheating on tie-in or reciprocity obligations), by efforts to prevent arbitrage or cheating on tie-in-agreement or reciprocity-agreement obligations, and/or by efforts to collect damages from buyers that violate their contractual obligations not to engage in arbitrage, to buy tied goods, or to fulfill their reciprocal-trading purchasing-obligations.

*C. The Likely Significance of the Critique*

I suspect that public goods are less problematic from the perspective of economic efficiency than the conventional oPp-assumption-based analysis of their economic-efficiency consequences concludes. However, I do not have

space here to establish all the relevant theoretical relationships<sup>13</sup> and to delineate and ground the empirical estimates/guesstimates that underlie this conclusion.

Nevertheless, I do think it worthwhile to explain six of the most important relevant theoretical relationships. First, since the demand curve in the standard public-good analysis indicates the quantity of the public good that will be sold at varying before-tax prices and the marginal allocative value of a unit of any product will equal the after-tax price its buyer paid for it (if the buyer is a sovereign, maximizing non-monopsonist whose consumption of the relevant unit generated no externalities and no buyer surplus), the height of  $MLV_{PG}$  at any output-quantity will exceed the height of  $DD_{PG}$  at that quantity by the sales/excise/value-added/consumption tax the buyer had to pay to purchase the unit in question if no Pareto imperfection of any type previously referenced were present.<sup>14</sup>

Second, *ceteris paribus*,  $MLC_{PG}$  for any public good will exceed  $MC_{PG}$  for that good by an amount equal to the external costs generated by the production of relevant units of the public good.<sup>15</sup>

Third, *ceteris paribus*,  $MC_{PG}$  for any public good will exceed  $MLC_{PG}$  for that good by an amount equal to the external costs that the resources that would be used to produce successive units of the public good would have generated in the sacrificed uses from which they were withdrawn. This conclusion reflects three "facts": (1) *ceteris paribus*, the private cost of any resource to the resource's user equals (actually, infinitesimally exceeds) the private benefits that the resource would have generated for its alternative user; (2) the allocative cost a resource-user generates by withdrawing a resource from an alternative use equals the net allocative benefits the resource would have generated in its alternative employ; and (3) the fact that a resource would have generated external costs in its sacrificed use implies that the private benefits it would have conferred on its alternative user exceed the net allocative benefits it would have generated in its alternative employ.<sup>16</sup>

Fourth, if the resources used to produce units of the public good (or to create the public good) are withdrawn from alternative uses to increase the unit output of an alternative good whose producer faced a downward-sloping demand curve

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13. For detailed analyses of the relevant theoretical relationships, see RICHARD S. MARKOVITS, TRUTH OR ECONOMICS: ON THE DEFINITION, PREDICTION, AND RELEVANCE OF ECONOMIC EFFICIENCY 89-137 (2008).

14. For explanations of the relevance of the previously-referenced Pareto imperfections, see *id.* at 129-30.

15. I should add that if "FC" stands for fixed costs, "AFC" for average fixed costs, "FLC" stands for fixed allocative costs, and "AFLC" stands for average fixed allocative costs,  $FC_{PG}$  and  $AFC_{PG}$  will be lower respectively than  $FLC_{PG}$  and  $AFLC_{PG}$  to the extent that the creation of the public good generates external costs.

16. For the same reason, *ceteris paribus*, the FC and AFC of creating a public good will be higher than respectively the FLC and AFLC of creating that good to the extent that the resources used to create the public good are withdrawn from alternative uses in which they would have generated external costs. I should add that, *ceteris paribus*, any difference between either  $MC_{PG}$  and  $MLC_{PG}$  or between  $FC_{PG}$  and  $FLC_{PG}$  will also create a divergence between  $ATC_{PG}$  and  $ATLC_{PG}$ .

and did not engage in price discrimination, did not engage in any form of lump-sum pricing, and did not use a relevant type of tie-in or reciprocity agreement, the imperfection in seller price-competition faced by the alternative user of the resources employed to produce units of the public good once it was created would cause  $MLC_{PG}$  to exceed  $MC_{PG}$ . The relevant imperfections in seller price-competition would generate this effect by reducing the marginal revenues the sale of the sacrificed units of output would have yielded below the prices for which those units could have been sold—*i.e.*, by reducing the marginal revenue products those resources would have yielded in their alternative uses (which equals the sum of the marginal revenues that the sale of the sacrificed units of output would have yielded their prospective producers and is infinitesimally below their cost to the public-good producer) below the marginal allocative products they would have generated in their alternative uses. This equals the sum of the prices that the prospective buyers of the units of the alternative products sacrificed to the production of units of the public good would have been willing to pay for the sacrificed units in question, which constitutes the marginal allocative cost of the units of the public good on oPp assumptions.<sup>17</sup>

Fifth, since the fact that an economy's other Pareto imperfections will usually cause the private benefits that any resource-use would yield to diverge from the net allocative benefits implies that these imperfections will usually cause the private value to an employer of a marginal unit of labor (and hence the gross wage that workers in the relevant category are paid) to diverge from the marginal allocative product of that labor, the fact that actual economies are not oPp will affect the economic-efficiency impact that any tax on the margin of earned income will have by making it profitable for workers to substitute leisure or do-it-yourself labor for market labor. To save space, I will focus on the effect that other types of Pareto imperfections have on the impact of an economy's taxes on the margin of earned income on the amount of market-labor/leisure misallocation generated in it. Six subpoints are relevant.

First, the amount of market-labor/leisure misallocation that a given potential worker generates will increase with the difference between the allocative product of the marginal unit of market labor he performed and the net wage he received for performing that marginal unit of market labor, where the net wage in question will equal the marginal allocative cost of his supplying that

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17. The text ignores the possibility that price-reductions may affect both the private value of intra-marginal units to their consumers and concomitantly the allocative value of those intra-marginal units by increasing relevant buyers' "wealths" (*i.e.*, by making them better-off). For the same reason,  $FC_{PG}$  will be lower than  $FLC_{PG}$  when the resources used to create the public good are withdrawn from unit-output production by an imperfect competitor that faces a downward-sloping demand curve and does not engage in price discrimination or use any other fancy pricing-technique. Similar arguments would be applicable when the resources used to produce units of the public good once it was created or the resources used to create the public good were/would be withdrawn from QV-investment-creating uses or production-process-research-executing uses by actors whose resource-uses would generate externalities, that would face imperfections in seller price-competition when selling the good/service their QV investment created or using the production process their production-process research discovered, etc. For a more comprehensive and detailed account, see MARKOVITS, *supra* note 13.

unit of labor (the allocative value of the marginal unit of leisure he had to forego to perform the marginal unit of labor) if he is a sovereign maximizer and his consumption of the foregone unit of leisure would have generated no net external benefits or costs.

Second, *ceteris paribus*, the amount of additional market-labor/leisure misallocation that will be associated with any given increase in the absolute value of the difference delineated in the first point of this list (if the sign of the relevant difference does not change) will increase with the absolute value of the original difference in question.

Third, if the worker's employer is a sovereign, maximizing non-monopsonist of labor, the gross wage the employer will pay the worker for his marginal unit of labor will equal the private value of that unit of labor to the employer (for example, the marginal revenue product of the labor if the worker performs unit-output-producing labor).

Fourth, in an oPp economy, the private value of a worker's marginal unit of labor to his employer will equal the marginal allocative product of that labor so that (1) the gross wage the worker obtains for supplying his marginal unit of labor will equal that labor-unit's marginal allocative product and (2) any taxes that are levied on the worker's marginal earned income will cause the net wage he obtains from performing his marginal unit of labor<sup>18</sup> to fall below the gross wage he was paid for supplying that labor (which on oPp assumptions equals the allocative product of his marginal unit of labor) by an amount equal to the taxes he had to pay on the income he earned by supplying his marginal unit of labor.

Fifth, in an economy that is not oPp, the other Pareto imperfections will always or virtually always independently create a difference between the allocative product of a worker's marginal unit of labor and the private value of that marginal unit of labor to his employer. Concomitantly, they will create a difference between the relevant marginal unit of labor's allocative product and the gross wage that the worker was paid for supplying that unit of labor.

Sixth, in an economy that is not oPp, the other Pareto imperfections it contains will affect the impact that taxes on the margin of earned income have on the amount of market-labor/leisure misallocation any worker and all workers generate in two ways: (1) by affecting the impact that the tax on the margin of earned income has on the absolute difference between each worker's marginal allocative product and his net wage and (2) by affecting the pre-tax differences in question.

I derive the following three conclusions about the misallocative effects of taxes on the margin of income from the preceding six sub-points: (1) if, as I believe, the relevant Pareto imperfections other than taxes on the margin of earned income reduce the gross wage paid unit-output-producing workers and

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18. This will equal the marginal allocative cost of that unit of labor if the worker is a sovereign maximizer and his consumption of the sacrificed unit of leisure would have generated no net externalities.

production-process-research-executing workers below the marginal allocative products of their labor by reducing the private value of such labor to its employers below the labor's allocative product,<sup>19</sup> these realities will cause any taxes that are levied on the margin of the earned income of such workers to be more misallocative than they would otherwise be by causing the allocative products of such workers' marginal units of labor to exceed their gross wages; (2) if, as I believe, the relevant non-tax Pareto imperfections increase the gross wage paid workers who create QV investments above their marginal allocative products by increasing the private value of such labor to their employers above its allocative product,<sup>20</sup> these realities will reduce the misallocation caused by any taxes levied on the margin of such workers' earned income in most cases by causing such taxes to reduce the absolute value of the difference between such workers' marginal allocative products and their net wages (which pre-tax equaled their gross wages) or by reducing the amount by which such taxes increased this difference; and (3) the net effect of these complications on the amount of market-labor/leisure and market-labor/do-it-yourself-labor misallocation the government must generate to raise any given amount of revenue by levying taxes will depend *inter alia* on the percentages of the taxed workers that perform unit-output-increasing, production-process-research-executing, and QV-investment-creating labor and on the differences that the other Pareto imperfections create between the gross wages and the marginal allocative products of workers performing (different subsets) of these categories of labor.

Seventh and finally, the fact that actual economies are highly-Pareto-imperfect also affects the amount of economic inefficiency that results from one or more of an economy's potential products' being a public good by affecting the relationship between the allocative and private transaction costs that would be generated by given responses to the public-good problem. Economists have never recognized the difference between private and allocative transaction costs. However, in an economy in which Pareto imperfections cause the private benefits that the resources "consumed" as transaction costs would have generated for their alternative users to differ from the allocative benefits they would have generated in their alternative uses, private and allocative transaction costs are unlikely to be equal. The ratio between allocative and private transaction costs will depend not only on the incidence and magnitudes of the seven types of Pareto imperfections in the relevant economy<sup>21</sup> but also on the percentages of the resources used up as transaction costs that are withdrawn from the various alternative categories of uses and the ways in which the economy's

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19. See MARKOVITS, *supra* note 13, at 157-70, 172-204, for extensive but still-partial explanations.

20. See *id.* at 212-31 for an extensive but still-partial explanation.

21. *Viz.*, imperfections in seller competition, imperfections in buyer competition, (real) externalities, taxes on the margin of income, resource-allocator non-sovereignty, resource-allocator non-maximization, and buyer surplus.

Pareto imperfections interact to create divergences between the relevant private and allocative benefits those resources would have generated in each category of their sacrificed uses.

Obviously, the facts that (1) economies in which one or more public goods could be produced also contain many exemplars of all other types of Pareto imperfections and (2) *ceteris paribus*, these other Pareto imperfections would almost always cause the profitability of unit-output-producing, QV-investment-creating, and production-process-research-executing resource-uses<sup>22</sup> to diverge from their economic efficiency are relevant to this Issue's concerns. They imply that it will be far more complicated for the government to respond economic-efficiently to the reality that some of the goods its economy could produce are public goods than would otherwise be the case. Indeed, as I will point out in Part III, these facts are also relevant because they affect the economic-efficiency consequences of the AJW effects of "fair-rate-of-return" regulation of the pricing of public utilities.

### III. The AJW Effects of "Fair-Rate-of-Return" Public-Utility-Pricing Regulation

Historically, regulators have regulated not only entry into public-utility "markets" but also a wide range of public-utility decisions. Thus, regulators have required public utilities to provide goods and services of at least some minimum stated quality and have prohibited public utilities from practicing particular types of price discrimination. Regulators have also required public utilities to supply all buyers willing to pay the prices the public utilities are charging and have controlled certain aspects of the regulatee's accounting, contracting, financing, and personnel policies. Finally, regulators have attempted to prevent public utilities from incurring "imprudent expenses" either by prohibiting them from making the relevant expenditures or by refusing to allow them to raise their prices to cover such costs. However, possibly the most-important part of public-utility regulation has always been the regulation of the height of the prices that public utilities may charge.

The most common form of public-utility-pricing regulation is "fair-rate-of-return public-utility-pricing regulation." Under this approach, the regulator (1) estimates the replacement-cost of the investments that enable the public utility to produce and sell its regulated goods—the public utility's "rate base," (2) determines the rate-of-return that would be "fair" for the public utility to realize on those assets (in practice, a rate-of-return that is somewhat higher than what economists denominate the "normal rate-of-return" for the business in question), and (3) calculates the prices the public utility is permitted to charge for its

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22. The Pareto imperfections that all economies contain also cause the "profits" that prospective workers would realize by supplying various types of market labor to diverge from the economic efficiency of their supplying such labor.

regulated products by determining the set of prices for those products that will enable the public utility to realize the decided-upon “fair rate-of-return” on its rate-base. The AJW effect of such regulation focuses on the tendency of such price-regulation to render it profitable for the regulated public utility to make otherwise-unprofitable rate-base-increasing decisions.

Here is the story. To the extent that “fair-rate-of-return public-utility-pricing” regulation precludes the public utility from charging as high prices for its regulated goods as it would otherwise find profitable to charge, such regulation creates what might be called a “prevented-profit pool.” In so doing, such regulation renders it profitable for the public utility to make rate-base-expanding investments that are inherently unprofitable. Such pricing-regulations have this effect because—if any unprofitable investments the regulatee makes are not excluded from the regulatee’s rate-base on the ground that they were “imprudent”—those investments will enable the regulatee to persuade the regulators to allow it to make inherently-profitable price-increases on its original set of regulated products. Such unprofitable investments put the regulatee in a position to argue that such price-increases must be made if the regulatee is to realize the allowed “fair rate-of-return” on its expanded rate-base. I hasten to add that relevant regulatees will find it profitable to make the least-subnormally-profitable investments they can make: any such regulatee will want to earn the permitted, supernormal, “fair” rate-of-return on as much investment as it can and will maximize the amount of investment on which it earns that rate-of-return by making the least-subnormally-profitable investments it can make until the prevented-profit pool is exhausted.

Although this account of the AJW effect is essentially the same as the explanation for it that Averch & Johnson and Wellisz provided,<sup>23</sup> neither they nor anyone else (to my knowledge) has given a full account of the variety of inherently-unprofitable investments or decisions that “fair-rate-of-return public-utility-pricing regulation” renders profitable. The list includes decisions to make: (1) inherently-unprofitable investments that may or may not be knowledge-discovering that create superior or just different product or distributive variants or additional capacity or inventory, (2) less-inherently-profitable QV investments that create goods or services whose post-creation supply will be more-capital-intensive rather than more-inherently-profitable QV investments that create goods or services whose post-creation supply will be less-capital-intensive, (3) less-inherently-profitable investments in known, more-expensive but more-capital-intensive production processes rather than more-inherently-profitable investments in known, less-expensive but less-capital-intensive production processes, (4) investments in inherently-unprofitable production-process-research (PPR) projects, (5) investments in less-inherently-profitable PPR projects aimed at discovering more-capital-intensive production processes rather than in more-inherently-profitable PPR projects aimed at discovering less-

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23. See Averch & Johnson, *supra* note 2; Wellisz, *supra* note 2.



capital-intensive production processes, (6) investments in productive assets (machines, delivery trucks, production plants) that would have been cheaper to rent, and, relatedly, (7) decisions to pay workers, managers, or trustees fixed annual salaries (if such compensation-commitments are deemed to be investments that are part of the company's rate-base) that are less-inherently-profitable than decisions to pay hourly compensation with no guaranteed number of hours of employment would have been.

Obviously, this diversity of AJW effects vastly complicates the task of preventing them. I do not think that efforts of actual public-utility commissions to prevent public utilities from making "imprudent expenditures" were motivated by the regulators' understanding that the "fair-rate-of-return public-utility-pricing regulations" they were implementing incentivized various kinds of "imprudent expenditures." This conclusion is consistent with the fact that regulators' product-quality concerns have focused exclusively on the possibility that the quality of the products supplied by the public utilities they regulated might be too low—*i.e.*, have not included concerns that the regulators' price-regulations might induce the public utilities to offer an array of products that was too diverse and of too-high quality from the perspective of economic efficiency.

The diversity of AJW effects also increases the likelihood that the most-economically-efficient and morally-desirable government response to the existence of economies of scale relative to the extent of the "market" that make it allocatively costly to preserve the operation of enough competitors to achieve a socially-desirable amount of price (and QV-investment) competition might well be government production rather than a combination of private production and government price-regulation. If the price-regulation that would have to be effectuated to achieve relevant economic-efficiency and distributive-desirability goals would have to be combined with close government-supervision of virtually all of the regulated company's business-decisions to prevent the price-regulation from inducing the regulatee to make a wide variety of inherently-unprofitable and, more to the point, economically-inefficient and morally-undesirable business-decisions, might not public production be more desirable? Admittedly, as Part V of this Essay acknowledges, for a variety of reasons, one almost certainly cannot rely on government officials to run such businesses economic-efficiently or morally-desirably. Still, government decision-making would seem to be equally problematic when the government acts as regulator as when it acts as producer.

As indicated previously, I want to make another set of points about the AJW effects of "fair-rate-of-return public-utility-pricing regulation." These points relate to the implicit assumption of the AJW literature (which this Part has so far accepted) that the inherently-unprofitable decisions elicited by "fair-rate-of-return public-utility-pricing regulations" will reduce economic efficiency by the same amount by which they would lower their perpetrators' profits if they would

not give their perpetrators access to their prevented-profit pools.<sup>24</sup> This assumption is incorrect. Although these two amounts would equal each other in an otherwise-Pareto-perfect economy, in our actual, highly-Pareto-imperfect economy, they will do so only rarely and fortuitously. For the same reasons that, as Part II showed, the profits yielded by the production of successive units of any public good will equal the economic-efficiency gains that their production/consumption generated only rarely and fortuitously in our actual, highly-Pareto-imperfect economy, the direct profit-loss that AJW-effect-induced decisions will equal the economic inefficiency those decisions generate in our actual, highly-Pareto-imperfect economy only rarely and fortuitously.

I do not have the space here to analyze the relationship between the direct-profit loss and economic-efficiency loss generated by the seven types of inherently-unprofitable business decisions that “fair-rate-of-return public-utility-pricing regulations” will induce regulatees to make. Still, I think it may be informative for me to make seven related points.

First, because I think that the joint impact of an economy’s other Pareto imperfections (especially, the imperfections in seller price-competition economies contain) would cause QV investments to be more profitable than economically efficient,<sup>25</sup> AJW effects aside, I suspect that the economic inefficiency that will be generated by public-utility QV investments induced by “fair-rate-of-return public-utility-pricing regulation” will exceed the direct-profit losses those investments generate.

Second, I suspect that any decisions induced by “fair-rate-of-return public-utility-pricing regulation” to create less-inherently-profitable QV investments whose creation and use will be more-capital-intensive rather than more-inherently-profitable QV investments whose creation and use would be less-capital-intensive will be economically inefficient. However, I have no view on the ratio of the resulting economic inefficiency to the associated direct-profit loss.

Third, the conclusions expressed in Item (2) of this list also apply to any decisions such pricing regulation induces regulatees to make to use inherently-less-profitable, known, more-capital-intensive production processes rather than inherently-more-profitable, known, less-capital-intensive production processes.

Fourth, because I think that the joint impact of the other Pareto imperfections economies contain (especially, the imperfections in seller price-competition they contain) would cause PPR projects to be less profitable than economically efficient, AJW effects aside,<sup>26</sup> I expect that any additional PPR projects induced by “fair-rate-of-return public-utility-pricing regulations” will reduce economic efficiency by less than the direct-profit loss they generate

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24. See, e.g., Averch & Johnson, *supra* note 2; Wellisz, *supra* note 2; ALFRED E. KAHN, THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS, VOL. II at 49-59 (1971).

25. See MARKOVITS, *supra* note 13, at 172-202.

26. *Id.* at 212-31.

(indeed, I suspect that such AJW-effect-induced PPR projects might well be economically efficient across all cases).

Fifth, I suspect that any decisions induced by "fair-rate-of-return public-utility-pricing regulation" to substitute less-inherently-profitable PPR projects aiming to discover more-capital-intensive production processes for more-inherently-profitable PPR projects aiming to discover less-capital-intensive production processes will reduce economic efficiency as well as direct profits. However, I have no idea about the ratio of the economic-efficiency loss to the direct-profit loss.

Sixth, the conclusions expressed in Item (5) of this list will also apply to any inherently-unprofitable decisions that such pricing-regulation induces regulatees to make to buy rather than to lease productive assets.

Seventh, the conclusions expressed in Item (5) of this list will also apply to any inherently-unprofitable decisions that such pricing-regulation induces regulatees to make to pay workers, managers, and trustees guaranteed annual salaries rather than hourly wages with no guaranteed hours of employment.

The general point I have just made about the impact that an economy's other Pareto imperfections have on the economic-efficiency consequences of any AJW effects of "fair-rate-of-return public-utility-pricing regulation" is salient in the current context because it is relevant to (1) the economic efficiency/overall moral desirability of "fair-rate-of-return public-utility-pricing regulation," (2) the nature and allocative cost of the protocol that the public-utility commissions that implement such pricing-regulations should use to determine whether particular regulatee-expenditures should be excluded from its rate-base, and (3) the relative desirability of the government's responding to economies of scale that are troublingly large relative to the extent of the market by producing the goods in question itself, licensing private companies to do so and regulating their conduct, or allowing private companies to produce such goods without regulating them.

#### IV. Some Relevant Moral Observations

Various claims have been made about the moral undesirability of some of the choices that would be made by businesses affected with a public interest if they were unregulated and of the moral desirability of various types of government regulations of such commercial enterprises. Part IV comments on some of these moral claims.

*A. My Conclusions About Various Moral Positions and Issues*

## (1) Basic Ethics Positions

Several of the moral analyses this Essay contains reflect my subscription to one or more of the following seven basic ethics positions or sets of related ethics positions:

First, I reject moral skepticism and emotivism—*i.e.*, I believe that moral concepts and arguments are coherent and that moral conclusions are substantively important. (They do more than articulate the kind of preferences individuals have for such things as Baskin and Robbins' "Here Comes the Fudge" chocolate ice-cream and convey more than the fact that the communicator has strong feelings about the conclusion expressed.)

Second, I believe that the members of and governments of at least some societies engage in a bifurcated prescriptive-moral discourse in which a strong distinction is drawn between discourse about "the just"—*i.e.*, about moral rights and obligations—and discourse about "the moral good"—*i.e.*, about what morally-ought to be done from the perspective of some moral norm other than the norm that grounds the relevant society's conception of justice.

Third, I do not rule out the possibility that some "Foundationalist" argument can establish the "objective truth" and therefore universal applicability of a particular concept of "the just" (or a particular concept of "the moral good"). Further, I recognize that foundationalist (with a lower-case "f"), Aristotelian, Kantian, and Natural Rights philosophers have tried to derive such a concept of justice respectively from the concept of the moral, the concept of human flourishing, the concept of human freedom or what would be rational for a creature that can plan, and the concept of human nature. However, I have not been persuaded by any such argument. Although I believe that coherent, important distinctions can be drawn among "the moral," "the immoral," and "the non-moral," I do not believe that the "objective truth" of a particular concept of "the just" or of "the moral good" has yet been established.

Fourth, I believe that individual societies can be placed into different moral categories. They can be "moral-rights-based societies of moral integrity (societies that draw a strong distinction between the just and the moral good and are committed to maximizing the extent to which justice is obtained [moral-rights-related interests are secured] even when a universally-subscribed-to morally-defensible conception of the moral good must be substantially disserved to achieve a tiny increase in the extent to which moral-rights-related interests are secured), "immoral societies," or "amoral societies" (societies that base too many decisions weighted by their moral importance on non-moral criteria or that base enough moral decisions of sufficient importance on different morally-defensible criteria that are applied selectively on an *ad hoc* basis).

Fifth, I believe that philosophically-informed empirical analyses of (1) the moral discourse, moral conclusions, moral perceptions, and moral conduct of the

members and governments of the United States and the other nations whose relevant businesses' conduct and whose business-regulations are at issue as well as (2) various facts that reduce the damage that other facts that do not fit the following conclusion do to the argument for it imply that the countries in question are liberal, moral-rights-based societies of moral integrity.<sup>27</sup> The claim that these societies are *liberal*, moral-rights-based societies is a claim that the concept of justice they are committed to instantiating places a lexically-highest value on all creatures' that possess the neurological prerequisites for taking their lives morally seriously (by considering carefully and fulfilling their liberal moral obligations, by devoting a requisite amount of attention to choosing their personal conception of the moral good, and by making choices that conform at each point in time to the morally-defensible conception of the moral good to which they subscribe at that point in time) having an appropriate opportunity to lead such a life; and the claim that the societies in question are liberal, moral-rights-based societies of *moral integrity* is the claim that its members' and governments' moral discourse, conclusions, perceptions, and conduct fit that characterization sufficiently well (given the partially-exonerating explicability of those facts that do not fit it) to warrant the society's being characterized as a society of moral integrity.

Sixth, I believe that a liberal, moral-rights-based society's non-government actors have a basic moral duty to treat each other with appropriate, equal respect and to act in ways that manifest their appropriate concern for each other—in part for each other's welfare in the hedonic sense in which naïve utilitarians and many economists understand this concept but pre-eminently for their fellow society-members'/participants' having an appropriate opportunity to take their lives morally seriously. This basic moral duty encompasses a wide range of more specific moral duties: *inter alia* (1) not to discriminate against others (in most contexts), (2) not to slander or libel others, (3) not to deceive others in non-contractual contexts, (4) not to treat others disrespectfully in contractual contexts by deceiving them, (5) when acting as a party to a contract, to make the response to unforeseen contingencies that affect the dollar-value of contract-performance to the contract-partners that maximizes the joint dollar-interest of the contract-partners<sup>28</sup> and to compensate a contract-partner that has fulfilled the above obligation so as to restore the anticipated division of the expected joint dollar-gain between the contract-partners, (6) not to steal or improperly convert the property of others, (7) not to assault others when there is no moral justification for doing so, (8) to make appropriate moves to reduce the accident and pollution losses one imposes on others—roughly speaking, (A) when the loss that the actor

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27. For detailed accounts of the “fit” and “explicability of non-fits” protocols for identifying the moral principle that a particular moral-rights-based society of moral integrity is committed to instantiating in the service of its conception of justice, see RICHARD S. MARKOVITS, MATTERS OF PRINCIPLE: LEGITIMATE LEGAL ARGUMENT AND CONSTITUTIONAL INTERPRETATION 23-34 (1998).

28. For the liberal (in the relevant author's terms, “Kantian”) grounding of this obligation, see Daniel Markovits, *Contract and Collaboration*, 113 YALE L.J. 1417, 1448-63 (2004).

might cause is a “mere-utility loss” (is not life-of-moral-integrity-imperiling), to do the research into the identity of the avoidance-moves that are available and their prospective costs and benefits that one would find profitable to execute if one treated one’s prospective victims’ equivalent-dollar losses as if they were one’s own and to make all relevant avoidance-moves whose appropriately-perceived equivalent-dollar costs are lower than their appropriately-perceived equivalent-dollar benefits and (B) when the loss that the actor might cause is life-of-moral-integrity-imperiling, to do all avoidance-move-related research whose execution is life-of-moral-integrity-promoting on balance and to make all avoidance moves whose execution is life-of-moral-integrity-promoting on balance,<sup>29</sup> (9) put crudely,<sup>30</sup> to provide rescue-services to potential rescues whom one has not endangered and with whom one does not have a chosen intimate relationship or a status relationship that is usually associated with intimacy<sup>31</sup> when the potential rescuee faces a significant risk of substantial bodily harm or death and the potential rescuer is uniquely-well-placed to provide the rescue-service and can do so without incurring a significant risk of sustaining substantial bodily harm or death or devoting an inordinate amount of time to executing the rescue,<sup>32</sup> (10) not to confine others physically when there is no moral justification for doing so, (11) not to abuse others psychologically, (12) not to significantly reduce the ability of others to take their lives morally seriously by undermining their self-confidence, (13) not to prevent others from obtaining relevant intellectual skills, scientific/social/psychological information, and information about different moral positions, and (14) not to violate the

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29. For the liberal grounding of these conclusions, see Richard S. Markovits, *On the Content of the Corrective-Justice-Securing Tort Law of a Liberal, Rights-Based State*, 2006 ILL. L. REV. 243, 258-68, 271-76 (2006).

30. For a more-completely-specified account of the duties to rescue of the members of and participants in a liberal, moral-rights-based society, see *id.* at 276-280.

31. Liberalism implies that individuals have more extensive positive duties to help chosen intimates and family-members than to help “strangers” because liberalism values intimate relationships (including those that family-membership fosters) on the ground that they contribute to their participants’ taking their lives morally seriously. Such relationships do so by disposing their participants to think about their moral identities and to analyze their moral duties to their relationship-partners and by creating situations in which they can act on their conclusions. The positive value that liberalism places on intimate relationships accounts for the fact that the basic moral duty of the members of and participants in a liberal, moral-rights-based society is, *inter alia*, a moral duty to manifest *appropriate* concern for each other as opposed to a moral duty to manifest *appropriate, equal* concern for each other: liberalism countenances favoritism for chosen intimates and family-members in some contexts (though it recognizes that this position should not be interpreted to allow choices that are motivated by prejudices against members of other groups) because it values the contribution that chosen intimate and family relationships can make to their participants’ leading lives of moral integrity.

32. My conclusion that liberalism does not imply that individuals have more extensive duties to provide rescue-services reflects the combination of my claim that liberalism places a lexically-highest value on individuals’ having and seizing the opportunity to take their lives morally seriously and my admittedly contestable assumption that the imposition of positive duties on individuals reduces the likelihood that they will take their lives morally seriously by militating against a self-perception of autonomy to a greater extent than does the imposition of otherwise-similarly-onerous negative duties toward others.

privacy rights of others or to prevent others in other ways from participating in relevant intimate relationship or having other sorts of experiences that would contribute significantly to their taking their lives morally seriously.

Finally, I believe that the governments of liberal, moral-rights-based States have a general duty to treat all moral-rights bearers for whom they are responsible with appropriate, equal respect and to make choices that are consistent with their having appropriate, *equal* concern for them as well (in part for their hedonic welfare but pre-eminently for their having meaningful opportunities to take their lives morally seriously). I also believe that this basic moral duty entails a moral duty to make all choices that will maximize the extent to which the moral-rights-related interests of the moral-rights bearers for whom they are morally responsible are secured. More concretely, I believe that this abstract duty entails *inter alia* moral duties (1) not to violate the negative moral rights of such individuals in any of the ways in which non-government actors can do so, (2) to provide moral-rights bearers whose negative moral rights have been violated with appropriate opportunities for redress, (3) to ensure that each moral-rights bearer has an appropriate, meaningful opportunity to take its life morally seriously—to secure for all such creatures the nutrition, clothing, housing, medical care, physical protection, protection against emotional abuse, protection against choice-capacity-diminishing psychological domination, emotional support, formal education that teaches the intellectual skills and inculcates the various kinds of knowledge that can contribute to individuals' making informed moral choices, opportunities to learn about and experience different moral positions/religious positions/life-styles, privacy, and opportunities to enter into and maintain intimate relationships that contribute to their taking their lives morally seriously, (4) to provide all (competent) citizens with a (hard-to-define) appropriate, equal opportunity to influence the content and implementation of the laws that will govern them, (5) to develop government decision-making institutions and decision-protocols that reduce appropriately the probability that legislative, administrative, and adjudicative decisions will be made mistakenly or inappropriately parochially, and perhaps (6) to ensure that government choices that are not fully determined by the government's liberal moral obligations are appropriately congruent with the personal moral-good convictions of the society's citizens or voters.

## (2) "Liberty"

Some regulations of the categories of businesses traditionally perceived to require regulation have been criticized for violating the "liberty interests" of the businesspersons whom they constrain. This subpart discusses the way in which "liberty" should be defined in liberal, moral-rights-based societies and the implications of that definition for the moral soundness of the liberty-oriented critiques of the regulations in question. Many conservative economists assert that any reduction in the set of choices available to an individual (in his or her

“opportunity set”) and perhaps any decision or natural event that makes a choice more costly to an individual reduces that individual’s “liberty.”<sup>33</sup> However, if the concept of liberty is to play the role that it actually plays in the moral discourse of liberal, moral-rights-based societies—*viz.*, if the conclusion that a decision restricts a moral-rights bearer’s “liberty” implies that the decision deserves that individual’s moral-rights-related interests and can be just only if it promotes other at-least-equally-weighty rights-related interests, the above liberty-definition and the liberty-conclusions to which it leads are incorrect. In a liberal, moral-rights-based society of perfect moral integrity (indeed, I suspect, in any type of society of perfect moral integrity), with one possible exception, individuals do not have a liberty-based moral right to commit any act that is moral-rights-violative: the possible exception is that the members of and participants in a liberal, moral-rights-based society may have a moral right to refuse to interact intimately with others against whom they are prejudiced. More positively, (1) the members of and participants in a liberal, moral-rights based society have a “liberty interest” properly so-called in doing something only to the extent that their doing it (A) contributes to their leading a life of moral integrity by contributing to their ability to take their moral obligations seriously, by enabling them to fulfill their moral obligations, by helping them to develop a personal conception of the moral good, and/or by helping them to conform their lives to their morally-defensible personal conception of the moral good or (B) increases their utility or some other component of their non-life-of-moral-integrity-related welfare and (2) a law that constrains one or more members of or participants in a liberal, moral-rights-based society violates the constraineed’s liberty-based moral right properly-so-called only if (A) the law reduces both that individual’s opportunity to take his or her life morally seriously and the extent to which (collectively) all members of and participants in the relevant society have this opportunity or (B) the law reduces the extent to which the various other liberal interests of the members of and participants in such a society are secured (including their interest in having equal, appropriate concern be shown for their utility).

In the United States, many regulations of business conduct have been criticized on the ground that they violate the liberty rights of businesspersons. That critique would be justified if the conservative-economist definition of liberty accurately described the concept of liberty our society is committed to instantiating. However, for four reasons, with the one limited, contestable refusal-to-deal-related exception previously articulated, the various types of business regulations that some have argued violate the liberty rights of the businesses they constrain (regulations of the height of the prices that can be charged for a product, regulations of the attributes that products must possess, prohibitions of price discrimination, and regulations that require businesses to supply all buyers who are willing to pay their standard price for their products)

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33. See, e.g., MILTON FRIEDMAN, *CAPITALISM AND FREEDOM* (1962).



do not violate the liberty rights of the regulated businesspersons and/or their shareholders if those rights are defined in the way they should be defined in a liberal, moral-rights-based society: (1) the freedom of businesspersons to determine the heights of their prices, to choose the attributes of the products they supply, to price discriminate, and (with the limited, contestable qualification articulated above) to choose the customers they will supply does not contribute to their ability to take their lives morally seriously; (2) the business regulations in question do not disserve any non-"mere-utility" interests of the constrained businesspersons and shareholders whose moral salience liberalism recognizes; (3) although business managers may find it intrinsically satisfying to run their businesses in the knowledgeable and skilled way that maximizes the profits those businesses generate, the constraints the above regulations impose on them do not reduce their opportunities to make use of their business knowledge and skills (think of the adjustments business managers can make to reduce the loss that traditional fair-rate-of-return public-utility-pricing regulation will impose on their businesses [the AJW effects of such pricing regulation]); and (4) although the business regulations in question may reduce the profits of the regulated businesses and hence the utility (salaries, dividends, capital gains) of their managers and owners, there is no reason to believe that such business regulations are more likely than law in general to manifest their promulgators' failure to have equal, appropriate concern for their losers. (Admittedly, laws requiring businesses to supply all buyers willing to pay the business' standard price for its product may violate the businessperson's liberty right if [1] the good in question is a service whose supply involves intimate interactions [*e.g.*, is massage services or psychological counseling], [2] the relevant businessperson must supply that service personally, and [3] the relevant businessperson is prejudiced against one or more of the buyers that would be willing to pay the business' standard price for its service.)

### (3) "Discrimination"

The term "discrimination" and its various cognates are used in two senses. In the first, morally-pejorative sense, a choice is said to be "discriminatory" if it is based on a morally-impermissible decision-criterion (say, that manifests a prejudice against Blacks, East Asians, the Irish, women, Muslims, Jews, etc.). In the second, morally-neutral sense, a choice is said to be "discriminating" if it manifests the chooser's possession of relevant information/capacities whose consideration/exercise is not morally opprobrious. Thus, a wine connoisseur may have a "discriminating" palate, which enables him to distinguish the good stuff from the plonk.

In the business-regulation context, the word "discrimination" is used to cover two types of business-conduct: "price discrimination" and choices to serve some but not all willing buyers. The issue is: are these types of business "discrimination" morally opprobrious or neutral? The answer depends on why

the business is treating certain individuals or groups differently. If the business is charging some buyers higher prices because those buyers place a higher dollar-value on the business' product than others do and it is profitable *inter alia* on that account for such decisions to be made, the price discrimination is not moral-rights-violative. It does not manifest the business' basing its choices on a criterion whose use is morally opprobrious (does not manifest any disrespect for either set of buyers). I hasten to add that, as I indicated earlier, price discrimination may be moral-ought undesirable even if it is not moral-rights-violative because the practice is economically inefficient<sup>34</sup> and does not redistribute income sufficiently desirably from any defensible, relevant distributive-norm perspective to promote any defensible, relevant conception of the moral good.

If the business charges different buyers different prices because the businessperson is prejudiced against some buyers and finds it more personally costly to deal with them, the price discrimination is moral-rights-violative unless the interaction between buyer and seller is sufficiently intimate to justify the conclusion that the seller has a moral right to act on the basis of his prejudice in the relevant context and one concludes (dubiously) that the associated right to discriminate entails not only the right not to supply the target of one's prejudice but the right to receive extra compensation for supplying a target of one's prejudice. If the business is charging some buyers higher prices because some of its other potential customers are prejudiced against those buyers and will withhold their patronage from the business if it supplies the targets of their prejudice or because some of its actual or potential employees are prejudiced against those buyers and will not work for the business or will demand higher wages if the business supplies the target of their prejudice, the moral status of the business' engaging in the relevant price discrimination will be at least contestable. Is it prejudiced or moral-rights-violative to do what is rendered profitable by the prejudice of others? Precisely the same analysis will apply *mutatis mutandis* when the relevant business-decision is a decision to supply some buyers but not others. The cited behavior of the prejudiced potential customers and employees of the business will be moral-rights-violative unless their interaction with the targets of the prejudice would be sufficiently intimate for the relevant customers/employees to have a moral right to indulge their prejudices in the relevant context. I assure you that I feel uncomfortable with the conditional in this last claim.

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34. This is because it is allocative-transaction-costly, creates an incentive for favored buyers to engage in allocative-costly arbitrage, and can result in goods' being allocated to buyers that place a lower dollar-value on them rather than to buyers that place a higher dollar-value on them.

*(B) Other Moral Claims*

I should now be able to address various other moral-rights and moral-good claims that have been made about different kinds of conduct in which businesses traditionally perceived to require regulation and their government regulators may engage.

(1) The Claim That a Relevant Business Is Charging Immorally-High Prices

Public utilities, pursuers of common callings, and common carriers are sometimes criticized for charging immorally-high prices. More specifically, such prices are sometimes condemned as “unjust,” “exploitative,” economic-opportunity-denying, unacceptably-welfare-disserving, inequalitarian, and undemocratic.

I do not think that the decision of any type of business to charge a high price for its product is moral-rights-violative. Although I know some will disagree, I believe that, in liberal, moral-rights-based societies, businesses are morally and legally obligated to price their products to maximize the interests of their shareholders/owners unless the law prohibits their doing so. The prices that are charged may be high relative to marginal or average total cost, may be “exploitative” in the sense that they yield the seller a high percentage of the transaction surplus its transactions generate, may deny some potential or actual buyers significant economic opportunities, may reduce utility or “welfare,” and may increase economic inequality. A business’ decisions to charge certain prices are certainly not democratic in that they are controlled by shareholders<sup>35</sup> rather than by the citizenry. However, even if the relevant pricing produces such undesirable results—indeed, even if it critically reduces the opportunity of some potential buyers to lead lives of moral integrity—and even if such pricing is “undemocratic,” those realities do not make the business’ pricing moral-rights-violative. In liberal, moral-rights-based societies, businesses have no moral obligation to benefit their customers and, I believe, morally ought not sacrifice their shareholders’ interest to do so. Admittedly, the high prices that businesses charge may morally obligate the governments of any liberal, moral-rights-based society in which they operate to take additional steps to secure some affected buyers an appropriate opportunity to lead a life of moral integrity and *may* make it moral-ought desirable for their governments to pass laws requiring the relevant businesses to charge lower prices than they would otherwise find profitable to charge.

(2) The Claim That a Relevant Business’ Practice of Price Discrimination

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35. Or by company-managers constrained by shareholders, boards of trustees, and the takeover market.

## Is Moral-Rights-Violative

Businesses affected with a public interest have also been morally criticized for price discrimination. Price discrimination has been assumed to reflect prejudices, has been characterized as *ipso facto* unfair regardless of whether it manifests prejudices, has been said to be “subordinating,” has been said to critically reduce the conventional welfare and significant opportunities of those buyers who are charged the higher prices when the good is “essential,” and has been asserted to be generally undesirable.<sup>36</sup>

I suspect that very little price discrimination manifests prejudice, though I acknowledge that it might be moral-rights-violative when it manifests the discriminator’s, customers’, or employees’ prejudices. I also recognize that the governments of a liberal, moral-rights-based society are morally obligated to combat such prejudices and to give the victims of prejudiced acts by such perpetrators who have no moral right to indulge their prejudices in the relevant context by practicing price discrimination appropriate opportunities to secure redress. I also believe that price discrimination that does not manifest prejudice is not unfair. Why should buyers who place a higher dollar-value on a good be able to obtain more buyer surplus by purchasing it than do buyers who place a lower dollar-value on that good? Why is it unfair for a seller to take advantage of the fact that a potential customer places a high dollar-value on its product—*i.e.*, why should the gain associated with that reality be secured by the buyer rather than by the seller? Moreover, in what morally-significant sense is price discrimination “subordinating”?

Finally, I believe that one cannot justify the conclusions that a seller’s price discrimination is/would be moral-rights-violative or the conclusion that it is/would be moral-ought desirable for the managers of a business to sacrifice its shareholders’ interests by foregoing price discrimination by proving that (1) the good on which price discrimination is/might be practiced is “essential” either in the sense that its consumption plays a critical role in the buyer’s having a meaningful opportunity to lead a life of moral integrity or in the sense that its availability on non-discriminatory terms would for some reason increase economic efficiency significantly by stimulating downstream activity or, contrary to what I suspect will usually be true, (2) the relevant price discrimination did/would not only disfavor poor buyers but deny poor people who need the good effective access to it and/or did/would decrease economic efficiency by reducing the “access” that some prospective downstream users of the good have to it as a class. Once more, however, if price discrimination did/would generate such effects, its practice may morally obligate the relevant society’s governments to do more to give relevant moral-rights holders a meaningful opportunity to lead a life of moral integrity or render it morally good for them to do something to promote downstream use of the seller’s product by

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36. See *supra* note **Error! Bookmark not defined.**

buyers who were/would be charged discriminatively-high prices. In fact, as I have already indicated, I suspect that it will often be morally good for governments to prohibit price discrimination even when the practice does not have any of the above effects.

### (3) The Claim That Refusals to Deal Are Moral-Rights-Violative

Businesses whose regulation has traditionally been deemed desirable have also been morally criticized for refusing to deal with particular potential buyers or categories of potential buyers. The criticisms of such refusals to deal range from assertions that the refusals manifest the refuser's prejudices to the claim that the refusals are moral-rights-violative when they violate the refused party's alleged moral right to have particular economic opportunities, to enjoy at least a minimum level of welfare, or to secure goods that are "essential" for some unstated reason.<sup>37</sup> If the refusal to deal manifests the business-owner's prejudice, it is moral-rights-violative (perhaps) unless the good was a service (say, psychological counseling or perhaps physical therapy) whose supply involved the kind of intimacy that entitled the business-owner to indulge his or her prejudices.

By contrast, if the business' refusal to deal is profit-driven (is rendered profitable by the prejudices of its actual/potential customers and/or employees), the moral status of its disfavoring the targets of their prejudice may be contestable. I hasten to add that the decisions of prejudiced potential customers or employees that would make it profitable for the business to refuse to deal with the target(s) of their prejudice would be moral-rights-violative unless patronizing the business or working for the business created a sufficient probability that the prejudiced potential buyers or potential employees would have to interact sufficiently intimately with the targets of their prejudice to give them the right to indulge their prejudice (as they would have the moral right not to marry someone or not to date someone or not to invite someone to dinner if they were prejudiced against the individual in question).

In any event, the governments of a liberal, moral-rights-based society would be morally obligated not only to combat such prejudices but also to give victims of such prejudices an appropriate opportunity to secure redress. I do not think that, absent prejudice, refused parties have a moral right that non-government actors provide them with the economic opportunities the refusals deny them. Moreover, although I agree that the governments of liberal, moral-rights-based societies are morally obligated to secure for refused parties the at-least-minimum amount of welfare and the other specific goods, services, and opportunities that contribute significantly to their having a meaningful opportunity to lead lives of moral integrity, I do not think that non-government

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37. See, e.g., Elizabeth Sepper, *Free Exercise Lochmerism*, 115 COLUM. L. REV. 1453 (2015).

actors' refusals to deal that would deny the refused parties the meaningful opportunity to lead a life of moral integrity if their governments did not prevent that outcome are moral-rights-violative on that account.

#### (4) The Claim That Relevant Businesses' Supplying "Unacceptably-Low-Quality" Goods Is Morally Wrong

Businesses whose regulation has traditionally been deemed appropriate have also been morally criticized for supplying goods of unacceptably-low quality. I should state at the outset that, unless these businesses are subjected to price-regulations that preclude them from raising their prices to recover the higher cost of supplying higher-quality products, the regulation of such businesses will not render it profitable for them to supply lower-quality goods when the relevant buyers would be willing to pay an amount for any increase in quality that covers the private cost of its supply. Nor do I see any reason to believe that buyers of the goods and services that are supplied by public utilities, businesses affected with a public interest, pursuers of common callings, or common carriers are unusually likely to misperceive the quality of the goods or services with which they are being supplied or to undervalue quality-increases.

Of course, if businesses in the above categories actively misrepresent or otherwise fail to reveal the negative attributes of the quality of the goods and services they are supplying when it would be morally incumbent on them to reveal such information, that conduct would be moral-rights-violative. A liberal, moral-rights-based society's governments would have moral obligations to deter such behavior and give its victims appropriate opportunities to obtain redress. I suspect, however, that much of the concern that moral critics of such businesses have about the quality of the goods and services manifests the critics' belief that the companies should supply increases in quality whose cost the buyers in question would not be willing to bear. I do not think that any moral-rights or moral-ought argument for this generic claim can bear scrutiny.

### V. Proposals for Improving Government Regulation

Both I and the other contributors to this Issue have recognized that the government can use different policy-instruments to respond to the problems caused by public goods, public utilities, businesses affected with a public interest more generally, businesses that pursue common callings, and common carriers.<sup>38</sup>

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38. See William Boyd, *Just Price, Public Utility, and the Long History of Economic Regulation in America*, 35 YALE J. ON REG. 721 (2018); James Ming Chen, *Speculative Undertakings: Rate Regulation as a Branch of Corporate Finance*, 35 YALE J. ON REG. 779 (2018); Prasad Krishnamurthy, *George Stigler on His Head: The Consequences of Restrictions on Competition in (Bank) Regulation*, 35 YALE J. ON REG. 823 (2018); K. Sabeel Rahman, *Infrastructural Regulation and the New Utilities*, 35 YALE J. ON REG. 911 (2018); Daniel Schwarcz, *Ending Public Utility Style Rate Regulation in Insurance*, 35 YALE J. ON REG. 941 (2018); Christopher S. Yoo, *Common Carriage's Domain*, 35 YALE J. ON REG. 991 (2018).

As economists in general and politically-conservative economists in particular recognize, regardless of the type of policy instrument that governments use to achieve any goal, government interventions in the economy are almost always less-economically-efficient and less-morally-desirable than they could be.

Government regulatory-interventions are sub-optimal for a large number of reasons. The available economic theory, natural-and-social-science theory, and empirical information are imperfect. The government's decisionmakers are not as skilled, well-informed, or able as would be economically efficient or morally desirable. Government decisionmakers do not have appropriate incentives to pursue the public interest. The decision-making processes that government business-regulators use are not ideal. The relevant countries' more general political processes have undesirable effects not only on the substance of the laws that regulators implement but also on the ways in which the regulators interpret, concretize, and apply those laws. This Part makes a few suggestions about how government economic-regulatory decisions might be improved. I fully recognize that its discussions are both partial and sketchy, that some proposals have already been implemented in certain countries, and that the merits of some recommendations are contestable.

My first set of proposals is directed at reducing the imperfections in the theoretical and empirical information that is available to government business-regulators. In my judgment, it would be both economically efficient and morally desirable for government to do or subsidize theoretical micro-economics, welfare-economics, natural-science, social-science and epidemiological research on the policy-relevant effects of various types of business conduct and of various business regulations. Such research could include studies of the amounts of various pollutants that different business-activities generate, of the cost of reducing such pollution, of the ways in which different pollutants interact to cause economic losses, of the dollar value of the losses that different combinations of pollutants generate, of the morally-relevant characteristics of the winners and losers of various possible anti-pollution policies, of the incidences and magnitudes of the relevant economy's imperfections in seller and buyer competition, taxes on the margin of income, human errors, and buyer surplus, of the various categories of economic inefficiency that can be generated in an economy, of the different ways in which relevant types of Pareto imperfections interact to cause each such category of economic inefficiency, and of the protocol that would be economically efficient to use to predict or post-dict the economic efficiency of any choice.<sup>39</sup> I also think that it would be desirable

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39. For an outline of the protocol for economic-efficiency analysis I now think would be economically efficient, see Richard S. Markovits, *The General Theory of Second Best and Economic-Efficiency Analysis: The Theory, Its Negative Corollaries, the Appropriate Response to It, and a Coda on the Economic Efficiency of Reducing Poverty and/or Income/Wealth Inequality*, 49 AKRON L. REV. 437 (2016). For a fuller, more detailed account, see MARKOVITS, *supra* note 13, at 73-237. For the most developed presentation of my position, see RICHARD S. MARKOVITS, WELFARE ECONOMICS AND

for the government to require polluters to measure and report the amounts of the various pollutants they generate and that it may be desirable for the government to require at least large businesses to report the prices they charge for and the marginal costs they must incur to produce their various products. Certainly, legislation and judicial decisions that provide polluters with a positive incentive to remain ignorant of the pollution they generate or that grant polluters the legal right to keep private the information they have on such matters (on the ground that the relevant businesses have a proprietary right to such information or sometimes on the ground that such information should not be made public for national-security reasons) should be reversed.<sup>40</sup>

My second set of recommendations focuses on the attributes of the personnel of government business-regulation institutions. To start, such institutions should have fewer political appointees: there may be good reason to have a politically-appointed cabinet-minister/agency-commissioner and (say) one deputy cabinet-minister/agency-commissioner in each agency/commission/department. But the U.S. practice of filling the top five or six levels of regulatory-institution positions with political appointees is unsound. Next, such institutions' civil servants should be better-paid. Moreover, the relevant civil servants should be selected not only on the basis of their demonstrated intellectual ability but also on the basis of their possession of relevant theoretical and empirical skills and knowledge. Alternatively, civil servants who occupy business-regulation-decision-making positions should be given substantial post-hiring training in relevant micro-economics, welfare economics, natural science, social science, moral theory, research design, data collection, and statistics/econometrics.

My third set of recommendations relates to the incentives of the civil servants who engage in business regulation. Government regulators should be provided with appropriate incentives to pursue a defensible conception of the public interest not only by remunerating them well but also by making their promotions depend on the quality of their job-performance. Better incentives could also be provided by prohibiting regulators both from accepting emoluments while performing their civil-service jobs and from becoming employees of, consulting for, or giving profitably-remunerated lectures paid for by the businesses they regulated after they leave their government positions. Indeed, given the difficulty of preventing businesses from benefitting each other's regulators and from subsidizing speeches or making charitable contributions to academic institutions or charities, it may well be desirable to place a more-encompassing set of restrictions on civil servants' post-government-service remunerative activities.

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SECOND-BEST THEORY: A THIRD-BEST-ECONOMICALLY-EFFICIENT DISTORTION-ANALYSIS PROTOCOL FOR ECONOMIC-EFFICIENCY ANALYSIS (forthcoming 2019).

40. For a fuller discussion of U.S. laws and judicial rulings of these kinds, see Wendy E. Wagner, *Commons Ignorance: The Failure of Environmental Law to Produce Needed Information on Health and the Environment*, 53 DUKE L.J. 1619 (2004).



My fourth set of recommendations focuses on the government-business-regulation decision-protocol. I will limit myself here to three proposals. First, although actors (including public-interest groups) with substantial interests in a regulatory decision should be provided with notices of proposed regulations and given an opportunity to comment on them, strict limitations should be placed on comment-submission time and comment length. Further, regulators should be empowered to penalize parties who intentionally or perhaps (possibly) negligently make inaccurate, misleading, or even irrelevant comments. Regulators also should not be required to respond to all components of all comments they receive. These last proposals militate against well-financed regulatees' having undue power over regulatory decisions. Second, regulators should be legally obligated to provide written justifications for their decisions, indicating the moral-rights-related interests they were designed to secure and/or the conception of the moral good they were designed to instantiate as well as the non-moral theoretical and empirical conclusions on which they were based.

Third, laws should be passed obligating courts to adjust the degree of deference they show to regulators when assessing, on the agency record, whether to uphold the agency interpretation and application of laws to the reviewing court's assessment of the care the regulators took and the skill they manifested when making the regulatory decision.<sup>41</sup> I admit that I would be more optimistic about the effects of this third proposal if law students were better-trained (as they should be) in economic analysis, moral analysis, scientific method, research design, fact-gathering, and statistics and econometrics.

My fifth and final set of recommendations relates to the more general political environment in which business-regulation decisions are made. I have already addressed the problems posed by the disproportionate power of special interests by proposing that political appointees play a smaller role, that civil servants be better-paid and better-trained, that civil servants be precluded from accepting compensation from regulatees during and after their period of government service, that comments provided during the rulemaking process be limited, that regulators be authorized to penalize improper participation in the decisional process, and that business-regulators be required to provide detailed written justifications for the decisions they have made. I recognize that the following additional proposals are tremendously underspecified and contestable, both politically and legally. I believe that businesses, industry peak-associations, labor unions, and public-interest groups should not be allowed to contribute to political parties or political campaigns and that strong constraints should be placed on the ability of such groups to provide information or to make arguments to legislators and members of the executive branch outside of public purview. I also favor laws that strongly constrain the size of the financial contributions that individuals can make to political parties and particular political campaigns, laws making prisoners and convicted felons eligible to vote, laws making it easier for

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41. Such a regime already exists in the United States.

eligible voters to register to vote, laws facilitating the voting of eligible voters by permitting absentee balloting and providing more and better polling-places, and laws creating and enforcing a legal obligation on all eligible voters to vote or cast a none-of-the-above ballot in local, state, and federal elections. In my judgment, all these admittedly-underspecified recommendations would improve the quality of government regulations of business not only by improving the quality of the laws that executive-branch authorities are given to implement but also the quality of their administration (given the fact that the relevant departments' and commissions' budgets are controlled by the relevant country's President/Prime-Minister/Chancellor and legislative bodies).

I recognize that a full discussion of political-process reform would have to address the relative economic efficiency and moral desirability of (1) parliamentary *versus* congressional systems, (2) centralized *versus* decentralized governmental regimes, (3) proportional representation *versus* elections by plurality vote in individual electoral districts *versus* something like the German system that secures proportional representation of political parties (whose vote constitutes at least some minimum percentage of the total votes cast) while preserving some single-constituency representation based on plurality votes, (4) bicameral *versus* unicameral legislative structure, (5) longer *versus* shorter terms of legislative office, (6) legislative regimes in which key posts are assigned randomly *versus* legislative regimes in which key posts are assigned through seniority, (7) legislative regimes in which omnibus bills are permitted *versus* legislative regimes in which each bill must address a related set of issues, (8) legislative regimes in which any legislation supported by a majority of the legislators or some lower percentage of the legislators must be brought to a vote *versus* legislative regimes in which only those bills supported by a supermajority of the legislature or a majority of the majority party (or coalition or the leader of the majority party or coalition) can be brought to a vote, (9) legislative regimes in which supermajorities are required for a bill to pass *versus* regimes in which majority votes suffice, and (10) governmental systems in which moral rights are protected by a constitution and the constitutionality of governmental acts is determined by an independent judiciary *versus* governmental regimes in which legislators and executive-branch officials are not subjected to such constraints, *etc.* However, consideration of these and other important political-process issues is beyond the scope of this Essay.

## Conclusion

This Essay begins by criticizing the conventional definitions of “public goods,” “public utilities,” and “businesses affected with a public interest.” It then explains why public goods would pose an economic-efficiency problem in an otherwise-Pareto-perfect (oPp) economy and analyzes how that problem and the appropriate response to it are affected by the reality that relevant economies are not oPp. After that, it explains (1) that “fair-rate-of-return public-utility-pricing

regulation” renders it profitable for regulatees to make a wide variety of otherwise-unprofitable business-decisions (generates AJW effects), (2) how this reality complicates the task of regulating public utilities in the public interest, (3) why this reality may favor government operation of public utilities over government regulation of privately-owned public utilities, and (4) how the fact that the relevant economies are not oPp affects the economic efficiency of the AJW effects such price-regulations generate and further complicates the identification of the most-economically-efficient regulatory scheme for privately-owned public utilities and decision-guides for publicly-owned public utilities. The Essay proceeds to examine various concepts that play an important role in prescriptive-moral analysis, to assess various moral criticisms directed against public utilities, to explain why government regulations do not have to surmount significant hurdles to be morally desirable, and to analyze the possible moral desirability of various types of government-responses to such business-decisions. The last part of the Essay makes various proposals designed to improve the economic efficiency and overall moral desirability of government regulation of businesses that have traditionally been deemed to require regulation and of government interventions in the economy more generally.

