

## REGIONAL RESOURCE CONFLICTS

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The workshop format involved an opening presentation by Cliff Russell to establish the most important economic issues related to resource based interregional conflict. Cliff did not prepare a paper specifically for the workshop, but referred to his earlier writing on the topic. In particular, he relied on a paper "Externality, Conflict and Decision," which is published as a chapter of the recent RFF book, *Regional Conflict and National Policy* (1982). The workshop reached no consensus, nor was one attempted. The following points were developed by Russell and the workshop participants.

### Sources of Regional Conflict

The roots of regional resource conflict are clearly in the non-uniform distribution of physical resources among different parts of the U.S. These resources provide a key part of an area's competitive advantage. Familiar labels like "sun belt," "bread basket," "parch belt," "frost belt," are tossed out by writers and promoters to tout an area's physical attributes or to taunt an area for its lack.

Resource endowments define the character of a region, a major basis by which one area is distinguished from another. Garreau in his recent book *The Nine Nations of North America*, gives prominent mention to resources as the basis for regional definition. The energy crisis of the 1970s added further emphasis to resource differences. A popular bumper sticker on cars in energy rich sun-belt states during the late 1970s taunted, "Let the Bastards Freeze in the Dark." Thousands of residents of northern states joined the parade to southern climates where the living was easy. The retort from the Midwest — "Soil for Oil!"

The point is that regional resource differences do exist and are increasingly part of the popular culture. They are a major component of economic differences, as resources are converted to income and jobs, and their absence may require considerable import cost. Any regional differences are the basis for trade. Artificial scarcity of hydrocarbon fuels in the 1970s seems to have tipped the regional balance of trade,

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exaggerated the importance of resource endowments, and encouraged people to move to energy rich areas.

Even after the energy crisis, resource characteristics appear to be increasingly important to a region's economic and political character. To Montanans, economic development means coal development and rules to keep the coal revenue in Montana. Governors of the Great Lakes states have met frequently to explore ways to capitalize on the image and substance of the lakes, and to present a united front to other regions. Greater concentration in food production gives new advantage to those who manage the soils and water of the grain belt.

In addition to the general comparative economic advantage aspect of regional resource differences is the physical externality aspect of resource use. Coal burning in the industrial centers of the mid-Atlantic states is creating environmental problems in northern New England, the upper Great Lakes and several provinces of Canada. There are regional resource conflicts, as well. Oil shortages led to increased coal burning, including some of the high sulphur variety that produces noxious and dangerous air pollution.

National air quality standards produced higher and higher smoke stacks at the power plants to get the waste gases up and out of the local area. Good intentions there have produced acid rain in regions hundreds of miles from the pollution source.

### **Why Government Action?**

We have regional resource conflict — so what? Does the obvious fact that there are externality problems among regions necessarily mean that some government action is called for? Can or should all such conflict be resolved? Even if we agree that some government should respond, which government is appropriate and how should it respond? What are the basic criteria under which government action may be appropriate? Economics gives some guidance on this question, though is obviously not a sufficient guide to public action. Some attempt to understand the sources or nature of interregional conflict can help. Regional externalities (conflicts) may be pecuniary, real physical interactions, or political. Rationale for and nature of governmental actions differ by type of externality.

**Pecuniary:** Economists frequently argue that “mere pecuniary externalities” are inadequate bases for public action. They simply signal market interactions as when a competing source of supply drives down the price an existing firm can charge for its product. Such efforts are the stuff of economic growth and change. Relative prices and capitalization of asset values simply lead the market economy in new directions. Examples are the influence of western irrigated acreage on the price of eastern cotton and establishment of a mainland macadamia nut industry that may depress the price of the Hawaiian version.

The former case has a major element of political externality, however, since federal water and farm policies have facilitated and sometimes created western production. To attempt to resolve such regional resource conflict by publicly altering the terms of trade in any way might block economic adjustments that reflect valid shifts of tastes and preferences. Adjustments to pecuniary externalities are made by mobile firms and individuals responding to price signals. The general proposition is that pecuniary externalities take care of themselves as firms and individuals shift locations and activities.

For example people in a particular region may be satisfied with a lower level of environmental quality than people elsewhere are willing to tolerate. This is a regional difference. People and firms may select the combination of environmental quality, money wages, and cost of living offered by different states or regions. If a "low quality" region loses too many skilled people seeking a cleaner living environment, firms may follow despite lower operating costs often associated with lower environmental standards.

Residents of a region capture a portion of the economic rents associated with the unique resource endowment of that region. Massachusetts residents pay dearly for the fuel oil or coal produced in other regions. Montanans may affect the price by charging a high severance tax designed to retain economic rent from coal within the state boundaries. There is only so much rent available from Montana coal in the energy market. The high severance tax just keeps more of it in Montana. Further, no one is forced to live in Massachusetts. They do so for many reasons, including the unique natural amenity of Cape Cod and proximity to glorious mountains of northern New England. If Montanans want to capture coal rents, let them do so. There is little reason for government to get in the way.

The logic against government corrections of pecuniary externalities assumes that markets can in fact adjust. A natural or legal monopolist could clearly exploit the system. If Montana were the only energy source, some protection of "the public good" would likely be necessary. Some states have created barriers to entry by outside firms, thus thwarting the adjustment process. Many poor people cannot afford to move, thus the forces of market adjustment may consistently hurt some people. Equity concerns also must be taken into account. But there is a real question as to whether government should sustain a particular population in an uneconomic environment, merely because that group refuses to respond to market signals.

Obviously, many of the regional resource conflicts discussed above are pecuniary in nature. Beyond the clear distortions of market control and problems of those people who lack basic response capability, many argue that government has no business tampering with the market adjustments that will inevitably occur.

**Real Externalities:** The adjective “real” suggests that one cannot dismiss this source of conflict as easily as pecuniary effects. It commonly is accepted that real externalities (nearly always) are proper matters for collective decision and action. Pollution of various types is the most common example, where actions by individuals or firms in one region impose costs or constrain alternatives for those in others, through direct, real physical impact. Agricultural erosion and run-off may reduce productivity of the farmer’s land. That should perhaps be the farmer’s problem — he/she can protect his interest with investment in conservation. But when the soil enters a stream and creates a problem for a fisherman or community downstream, that is another matter.

The farmer has no clear incentive to help out the downstream water user; government action is necessary if the conflict is to be resolved. The similar conditions apply when acid rain is the conflict, and different regions are involved. The real externality implies an inefficiency in that too much of a “bad” or too little of a “good” is being produced, given impacts on people not involved in the transaction. Thus government should correct for the inefficiency with public action. Decentralized bargaining among private firms or individuals cannot be counted upon to solve the problem.

Alternatives for government action to resolve these interregional conflicts based on real resource externalities include establishment of special organizations to facilitate bargaining, imposition of regulations, levying a tax on the firm producing an external “bad” or an incentive for the firm producing too little of a good thing.

A frequently cited example of regional bargaining is the multi-state river basin commission. The river basin is a physical entity that encompasses certain economic interrelationships. Those who cause pollution and those damaged by it are usually contained within its boundaries. But claims of success for these regional units are generally overdrawn. “Problem sheds” are difficult to define, particularly for resource issues like air pollution.

Pathways for pollutants causing acid rain are poorly defined. The U.S. - Canada International Joint Commission is concerned primarily with water quality in the Great Lakes, though its mission could conceivably be expanded to focus on the bi-national dimension of acid rain. There is real conflict on this matter, and some basis on which to address the issue is needed.

Courts are an alternative means for regional resource conflict resolution. But there are problems. One is that few judges understand the technical details of the conflict. Court procedures often depend upon delay which may become a *de facto* decision to let the problem continue. The Supreme Court is reluctant to get involved in this type of inter-state problem.

**Political Externalities:** Some resource disputes result from political decisions, and continue because political boundaries separate the combatants. The exclusionary power of jurisdictional boundaries may keep interested parties from having a voice in political decisions and thus create regional resource conflicts out of differences in tastes.

For example, federal tax codes, public credit sources, and direct public incentives have made irrigated agriculture attractive in some dry regions of the Great Plains. Resource decisions in that region affect water supplies available hundreds of miles away, create wind erosion felt in nearby states and have a pecuniary effect on crops grown elsewhere without public subsidy.

Governors of the Great Lakes states have joined forces to discourage and prohibit if possible diversion of water from the Great Lakes to the "Parch Belt." Thus, political action causes or at least exacerbates regional conflict on this point, and others like it, by sharpening the issues before they emerge on their own.

### Policy Implications

Several policy conclusions emerge. First, the nation must develop better ways to relieve the short run pain associated with pecuniary externalities. Resources, including human and financial, must be able to respond to economic opportunities but the side-effects of the adjustments may represent valid bases for public action. People can be hurt when a change in technology or world economy renders a way of life obsolete. The fact that such adjustments are inevitable in a dynamic economy is cold comfort to those affected.

We should not attempt to divert the adjustments, nor should we ignore their human consequences. This is particularly true when governments have actually created an artificial regional advantage that will be allowed to deteriorate. The public subsidy of irrigated agriculture in dry regions is a case in point. Water shortage or a change in water allocation rules could leave these farmers high and dry, to use a bad pun.

Michigan's auto industry has argued for domestic content legislation, tariffs, import restrictions, and voluntary import quotas to lessen the pecuniary effect of technology and labor practices in Japan that permit production of a better product at lower cost. Artificial barriers to trade would produce inefficiencies, yet the short term discomfort for Michigan auto workers cannot be ignored.

Most of the regional resource differences that produce conflicts discussed above are in fact pecuniary in nature, thus not a matter for government intervention. To attempt to alter the fact that Montana has coal that the eastern states must have, or that the Midwest has a significant economic advantage for food production would be frustrating, at best.

Government's role should be to facilitate the adjustments, and ameliorate the side effects, not attempt to hold back the tide of change. To do so could harm consumers for many generations to come.

If real externalities are to be reduced, government action is essential. There is little likelihood that private adjustments will solve these problems. There is little incentive for the firm imposing the external cost to bargain with those bearing the harm, so long as property rights are clear. If those harmed could get together and bribe the polluter to stop polluting and still come out ahead, then private solutions might work. The information and transaction costs involved usually make these solutions impossible.

Choice among alternative policy instruments to resolve the externality implies a distribution of burden among participants. A soil loss regulation, for example, implies that downstream users have a right to clean water, and that the farmer must do whatever it takes to eliminate the problem. A volunteer cost-sharing incentive, on the other hand, implies the farmers have the right to erode along with other land ownership rights. Policy options are selected based on the various consequences involved.

### **Implications for Extension Policy Education**

Policy education can focus on these alternatives, including expression of preference or judgment by the educator as to which alternatives show particular promise. Decision makers and others need to have definitive, defensible information on the economic and political consequence of different ways to solve the regional externality problems. Distribution of impact is often more critical than the nature of that impact.

Beyond this alternative-consequence stuff, policy educators can help clarify the nature of the interregional resource conflict. Is it largely pecuniary, or are there real technical bases involved? How has government action created the problem? Whose interests are at stake? What information needs are there? Is there really much utility in the distinctions among types of externality, or is the real issue to determine whose preferences make a difference in the decision?

It could be, for example, that some conflicts that appear to be "merely pecuniary," impose burdens deemed unacceptable by those with access to political power. To simply write these problems off as irrelevant would be risky, and probably costly. By the same token, some real externalities generate little interest among those affected. The right and capacity to have one's interests considered may not respect the economists' proclivity for granting more legitimacy to some policy problems than to others.

## Discussion Points

The primary topics of discussion among workshop participants, including Dr. Russell, concerned the conceptual framework for understanding or recommending public policy for regional resource conflicts. The substantive details of current resource conflicts received far less attention. The following points were raised:

1. The neoclassical economic construct of market failure/remedy may be unnecessarily restricting to a discussion of policy in any area, including regional resource conflict. To imply that our theory constitutes adequate or even necessary basis for supporting public action in one case or resisting it in another may be imposing too great a burden on the theory. Policies are undertaken for a variety of reasons usually associated with compelling evidence by those whose intents are damaged or insufficiently sustained that some changes in the current set of rules would be in “the public interest.”

The market failure/remedy paradigm may be a useful construct to help understand the nature of the policy problem and the set of policy choices. But it has little normative validity in terms of what should happen, where and when. Economics as a discipline and set of analytics can help sort out the positive and negative impacts of alternative policy actions as well as whose interests are damaged and whose expanded. Policy choices are then made among those options based on perceived validity or relevance of those observed impacts.

The policy economist should not allow himself or herself to be assigned only the uninteresting chore of defining externalities. The really interesting activity concerns the perception of economic consequence by those whose preferences count and subsequent battles over what to do about the “problem.” The economist should not be intimidated by his/her discipline. We have insights to offer on the nature of problems and consequence of solutions, insights that just may be better than those of other analysts.

2. The economist has a clear professional obligation to clarify the efficiency consequences of different policy proposals. Some proposals are simply bad policy. They substitute expensive bureaucratic rules for the relatively inexpensive functioning of a market. Many government interventions create costly disruptions in markets, disruptions that create more problems than they solve. Economists are in a good position, because of their professional training, to provide greater scrutiny of proposed market interventions to help assure that the long term net effect on citizens and taxpayers is positive. Too often governments have let good intentions replace good policy with results that are damaging to everyone.

This is particularly notable in cases of pecuniary externality where government provides incentives to certain businesses in the name of economic development or protecting the small farm or some other laud-

able cause. The frequent result is that the illusion of economic viability is created, suggesting that these enterprises are in the public interest and therefore should survive. Many do not in the longer run, at great cost to taxpayers and unrealized expectations by all involved. Economics and economists can be the source of critical scrutiny the system needs. Let's earn the label dismal science.

3. The conclusion that government should always be less concerned about pecuniary than real externalities involves an underlying value judgment which should be made explicit: it will tend to favor those with existing control over resources (property rights) or with the financial wherewithall to establish and protect such control. This recommendation also is unrealistic in that it ignores the necessary and proper (and inevitable) role of government involvement when issues arise from conflict over rights or distribution of externalities.

Finally, the recommendation ignores the fact that even if market solutions are politically preferable to authoritative institutions, there is an infinite variety of possible market solutions from which to choose — each involving the establishment of a property rights set underlying the bargained transactions. In other words, government is necessarily involved in setting the rules of the game which in turn give rise to pecuniary externalities.

4. All externalities are political, whether originating from public or private sector actions. All individual and collective action, whether public or private sector based, creates externalities — someone's opportunities are always affected, positively or negatively, by the actions of others.

It must be recognized that “no action” is a form of action that favors various interests and hurts others in the adjustment process. The orthodox stance on pecuniary externalities is not value free. In the face of pecuniary externalities, why shouldn't various interests work for collective action that enhances their position if they are organized and powerful enough to cause change? The issue is fundamentally one of political choice and power, not of economic efficiency and theory. The economist (or anyone) who argues otherwise is making a value judgment and taking a political stand, not an “objective, scientific” stand.



***THE POLICY EDUCATION PROCESS***

