

A HEALTHY ENVIRONMENT AND ECONOMIC GROWTH: TRADEOFFS OR SYNERGIES?

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One of the enduring debates about environmental issues is the extent to which progress can be achieved without economic harm, either to a business or to society as a whole. The risk of such harm has frequently been used, often effectively, as a reason to oppose or delay actions to reduce pollution or to otherwise advance environmental protection goals. The apparent political persuasiveness of the argument has led to a counterargument: that there are usually win-win solutions and that environmental and economic goals need not be in conflict.

The organizing question for the Aspen Institute Forum convened to consider this “critical conundrum” was “How do business, government and media balance the competing values of economic growth and a healthy environment?”

The premise of the discussion was that dealing with environmental issues poses particular problems for three actors in the American society:

- public officials, who are constantly buffeted by conflicting pressures as they seek to develop and enforce policies that address environmental issues, while remaining mindful of the needs and demands of the business sector and the national economy that would be affected by any environmental policy. These conflicting pressures seem stronger in the U.S. than in most other industrialized countries.

- leaders of business enterprises, who need to balance various desires — to be good citizens, to solve environmental problems, to be forward-looking – with what our society currently considers the overriding task of a CEO – to increase shareholder value in the relatively short or middle term; and
- journalists, who want to report fairly and responsibly on complicated environmental issues while facing time and space constraints as well as conflicting opinions, vigorously promoted, about the science and the economics involved in their stories.

The participants asked two fundamental questions:

- How real are these conflicts? For example, is there really a conflict between enhancing shareholder value and taking steps to reduce a company's polluting emissions?
- What tools do we have to make the task of these actors easier?

The Public Official

When developing or advancing a policy, public officials struggle with three kinds of decisions: how to set the goals they want to achieve; how to achieve these goals in a cost-effective manner; and what processes to use to win political support for their efforts.

Taking these in reverse order, the participants developed a clear consensus that public officials had available procedural techniques or processes that would make their task easier and would reduce most political fallout.

- The first of these is to increase the transparency in their regulatory processes. The participants heard persuasive first-hand stories demonstrating that a transparent process increases the acceptability of a course of action, even by those who don't really agree with it.
- Second, being honest about costs and benefits of policies, and about successes and failures of past policies, is another way to provide citizens with greater confidence in, and reasons for supporting, regulatory measures.

- Last, focusing the regulatory regime on outcomes rather than on process was viewed as a particularly helpful step. Example: the public official who measures the success of his or her local air quality regulations by quantifiable improvements in local air quality rather than by the size and number of fines imposed will have an easier time.

We noted that the thirty-year history of environmental legislation has yielded some impressive success stories. One involves laws and regulations, such as the 1986 law creating the Toxics Release Inventory, that are based on the public's right to know. These can lead to better behavior on the part of businesses concerned about community concerns, more informed advocacy on the part of citizens, and better decision making by public officials.

Generally, however, success requires public officials to go beyond providing data. Various methods are available, including voluntary action (considered desirable but often clearly inadequate), command and control mechanisms, and market-based techniques.

Attention was focused on two laws: The Clean Air Act of 1970, which dramatically improved local and regional air quality, and the Clean Water Act of 1972, a similar success. Both laws employed techniques that, the group agreed, would be much more controversial today.

First is their use of "command and control" techniques. The two laws did not just set standards that industry and others had to meet, but they prescribed what had to be done – for example the emission characteristics or control technologies of new power plants.

Second, both laws used public health standards as the driver, as the determinant of the degree of improvement that had to be achieved. They did not qualify that by adding an economic or cost test.

The group asked to what extent it would be proper and wise for government to apply these techniques today. As to the first of these, there was a consensus that, while we could not and should not eliminate command and control requirements from our menu of public actions, public officials will often have more success when they use techniques that employ market forces. The emission trading

scheme for sulfur dioxide in the 1990 amendments to the Clean Air Act was considered by all as an example of regulatory form that worked.

As to the second, there was consensus that standard setting would and should remain the responsibility of public officials. Making such decisions is what they are elected to do. Failure to do so would mean either a delegation of this responsibility to unelected officials or relying for progress on the industrial sector's setting its own standards and then seeking to meet those standards by voluntary action. Neither was viewed as acceptable. However, when the question was raised to what extent it was appropriate for government, in setting those standards, to take into account economic considerations, finding consensus in the group proved more elusive.

At the heart of the debate was the tool of benefit-cost analysis in determining standards. All agreed that in principle it was simply a tool – albeit a very useful one – that could help in two ways: it could estimate whether the environmental benefits were likely to be sizeable enough to warrant the economic costs involved in complying with the law or regulation, and it could help guide regulations in a direction that would provide the most cost-efficient solutions.

The perceived weaknesses of this tool, particularly when used to set environmental goals, troubled some more than others. It is exceptionally difficult to quantify objectively such costs and benefits as the value of a human life and life expectancy, of life diminished by poor health, of species that might go extinct, of the existence of wilderness, and of benefits or costs occurring far in the future. Benefit-cost analysis also does not generally reveal the distributional inequities that may result from a regulation: the question of exactly who in the population pays and who benefits.

But the heart of the debate about benefit-cost analysis seemed to turn more on philosophical than on practical concerns. When public health is at stake, should we really tailor the degree of improvement to the costs of achieving it and, if so, to what extent?

The discussion dealt both with principle and practicalities. The practical concern was that in the reality of the political arena this would not be as neutral a tool in fact as it is in theory. The incentives to game the system are great, and

often irresistible. (For example, the predictions of the cost of reducing sulfur dioxide emissions that preceded the 1990 Clean Air Act Amendments were uniformly and significantly overestimated, either from an abundance of caution or suspicion, i.e. an unwillingness to count on technology improvements, or from an abundance of political gamesmanship.)

The dominant fear on the part of some participants was that the analysis would be used principally to fight against taking actions that had large public health benefits. This is a particular risk because the costs being measured are often borne by a firm or sector while the benefits are shared by society as a whole. Who would undertake the analysis, and how objectively it would be done, were also matters of concern to some. There was agreement, however, that an open and transparent process could alleviate many of these concerns.

The Corporate Executive

There was considerable sympathy for corporate executives who are caught between the demands of different stakeholders – specifically their obligations to shareholders, with their legitimate concern for share value – and the broader interests of the public.

The question was what drivers – other than government laws and regulations – are likely to yield good corporate environmental conduct. This conduct could come from several sources: a general desire to have the company “do the right thing”, which can be personal but can affect the company’s reputation and therefore have market value; pressure from foreign countries where the company does business; pressure from socially-minded shareholders; a personal desire by the CEO to be a member of a progressive group of leaders.

A perhaps surprising conclusion of the group was that treating the corporation as a “moral actor”, as one might a natural person, is not a useful way to approach the problem.

There are probably only few instances where corporations are justified in incurring major expenses when not required to by law. Environmental leadership can, of course, contribute to financial results by enhancing the company’s reputation among consumers, and also among investors who see good environmental

performance as a proxy for overall good management. There are obviously also instances where a change in the way a business operates would simultaneously yield an environmental benefit and improve the bottom line over a reasonable period. Often business executives, by reason of their background and relatively short tenure, are not able to see or willing to take advantage of these opportunities. That does not help, however, with the more frequent reality – that this coincidence of interests is often not to be found. The root of this larger problem is that generally the costs of environmental harms accrue to society as a whole and not directly to the firm, and therefore the executive's freedom to expend company monies to deal with them is quite limited. Only government action can solve this dilemma.

Such government action need not be inconsistent with the reliance on efficient market tools that most participants considered desirable. Getting the respective roles for government and the private sector right is crucial. Government should – indeed must – set the standards on behalf of society, the standards that all competitors must meet. Corporations should then be left relatively free to find the most efficient way to meet the standards. This clarity of roles should minimize the confusing and generally unrealistic expectation that corporations will voluntarily spend shareholders' money to achieve environmental improvements that society desires but has not required.

However, even in the absence of such mandatory standards, executives have some room for maneuver. One need only look at the different behavior of companies in the same business, such as the oil industry. One such area lies not so much in taking actions within the company beyond those required, but rather in the external positions the company takes on public policy questions. Here the company's aims need not differ from the public's. The group believed that, in order to be environmental leaders, executives need several things.

- A level playing field – no advantage to their competitors through regulations;
- Predictability – needed to raise capital for the business;
- Minimizing the “stroke of the pen” risk – a law or regulation or international treaty that suddenly changes the rules that govern the business and could, for example, make some sunk investments redundant or useless; and

- Help in their public relations – executives and their firms need to be rewarded with favorable comment for appropriate action.

When government acts in a way that takes into account these needs of the business community, progress should be more achievable.

There was unanimous agreement that if a company did voluntarily take steps in advance of any legal requirement, such early action needed to be recognized and rewarded.

However, perhaps a more effective stimulus to environmentally positive actions involves risk analysis and minimization. One participant noted the “stroke of the pen” risk would cause a forward looking executive to take steps in advance of such event. The possibility or likelihood of the entry into force of an international agreement (the Kyoto Protocol or otherwise) or a national law that puts a price on carbon emissions has shaped a number of business decisions that seek to reduce a firm’s carbon emissions.

The group considered whether pressure from investors could affect corporate environmental behavior. There is a clear and growing body of socially responsible investors who are committed to the notion that environmental criteria must be fundamentally integrated into the analysis of a company for possible inclusion in a portfolio. But how powerful is this development?

On balance, the group felt that these investors constituted a meaningful source of pressure for bringing about corporate environmental change, but are not yet a very strong source. There is evidence that attention to environmental performance can be translated to superior market performance. The evidence here, however, is anecdotal and not universally recognized. If that nexus could be established more persuasively, the investor would become a stronger instrument of change.

One point that was somewhat clearer was that investors will pay a premium for information; a corporation that discloses more fully will command a higher stock price. This should lead over time to greater inclusion in financial reports of hidden liabilities (e.g. the disposal costs of dirty circuit boards). Additionally, it

appears that some shareholders use evaluation of the way a company handles environmental concerns as a proxy for evaluating management more generally.

The Journalist

Publishers, editors, news directors and reporters face quite different pressures, as they seek to cover environmental stories.

- First, the market demands are real and growing – pressure to write stories that readers will want to read rather than those that are necessarily important.
- The issues to be covered are proliferating, they are becoming more and more complex, and they have long time horizons.
- The journalist covering these complex stories gets “help” – and needs help – from numerous sources, such as the government agencies in charge, corporate public affairs offices, environmental NGOs, and scientists of all kinds. However, all often have very specific axes to grind, and the burden of sorting through these inputs is substantial.

The journalists’ task is made tougher because, while we expect them to be objective, we place on them two special burdens that require them to make difficult and quite subjective decisions. First, we expect them to distinguish between the truly important and the routine story. Second, we expect them not merely to “report” but rather to synthesize a whole array of facts and views, rendering these complex issues more understandable to us.

The problem of conflicting scientific views presents a particularly sharp dilemma. On the one hand, there is an obligation to record conflicting scientific views when there is a valid scientific basis for that conflict. However, in doing so, the readers could be quite misled into believing that the differences are deep and somewhat evenly divided, when that may not at all be the case. This requires the journalist to distinguish between differing levels of scientific analysis.

The participants believed that, when there are conflicting scientific views, a diligent journalist needed to ask several questions:

- Is this an instance of a broad consensus of views versus some outlying views?
- Have the various positions undergone similar rigorous reviews – such as peer review in a credible journal?
- Is the independence of the scientists in question clear? Do any of them have financial ties to a party that has a stake in the outcome?

The group felt that editors and news directors, those who make long-term resource allocation decisions for the news media, need to be challenged to devote adequate resources to environmental issues and to insist that professional reporting adapt to reflect the importance and complexity of these issues.

Tradeoffs or Synergies?

On balance – a word used often during the Forum – the participants agreed that tradeoffs between economic growth and environmental protection can be real. Scarce economic resources must be used to tackle many environmental challenges, both at the level of the firm and of society. And while such expenditures may contribute economically through job creation, the advancement of technology, and international competitiveness, the same resources cannot be spent on other business or social priorities.

At the same time, there may be more win-win situations than have been discovered or acknowledged. In particular, avoiding the short-term time horizon that currently forces many corporate leaders, investors, and elected officials to weight short-term costs more heavily than long-term benefits may disclose many more instances of environmental improvements that have an economic benefit. The values of human health and natural resources, only sporadically and inadequately considered in many economic decisions and national accounts, need always to be included.

Environmental decisions will grow in importance in the future, especially as we face global problems that require long-term solutions. Business leaders, elected officials, investors and journalists will all be called on to evaluate the economic impact of action as well as inaction.

To help make these decisions wisely, we will need several things:

- a public better educated in both environment and economics,
- a commitment to transparent public processes and honest political debate,
- the use of cost-effective tools, and
- the acceptance of the importance of both environmental and economic values.

These are difficult but not impossible goals. The participants in the Forum agreed that a commitment by business, government, journalists, and individual citizens to achieve them is critical to our future and quality of life.