In Review

A Useful, Frightening Book

REVIEWED BY JOHN HASNAS

Prosecutors in the Boardroom: Using Criminal Law to Regulate Corporate Conduct
Edited by Anthony S. Barkow and Rachel E. Barkow
297 pages; New York University Press, 2011

Here is a puzzle for the lay person: If the Federal government has been waging a decade-long war on white collar crime, why are federal prosecutors uninterested in convicting corporations of white collar offenses? If the Department of Justice has made it a priority to crack down on "crime in the suites," why do U.S. attorneys regularly let offending corporations off the hook? If there really is an upsurge of corporate fraud occurring, why is the number of cases in which the DOJ agrees not to prosecute corporations dramatically increasing?

The solution to this puzzle may be sought in *Prosecutors in the Boardroom*, a useful, if a bit uneven, collection of essays addressing contemporary corporate criminal law enforcement policy. In this book, editors Anthony S. and Rachel E. Barkow, both of New York University School of Law, have assembled contributions from highly knowledgeable authors that touch upon virtually every aspect of current prosecutorial practice. In doing so, they provide what is essentially one-stop shopping for information concerning the prosecution of corporations.

Prosecutors in the Boardroom is a useful book for both the lay person and the expert. For the lay person who is unfamiliar with how far removed the prosecution of corporations has become from the conventional *Law and Order* model of the criminal justice process, this book provides a means of getting quickly up to speed. By concentrating a wealth of information in one place, the editors make it possible for the non-expert reader to gain a coherent overview of the field. Yet the knowledgeable expert can benefit from the book as well because it will serve him or her as a useful research tool. Although the essays themselves are rather brief, the endnotes associated with each show the way to most of the relevant sources on the topic. As a result, this book can serve as a convenient starting point for research on virtually any aspect of current prosecutorial practice.

To be clear, the main value of this book is that it is a cache of useful information, not a source of normative arguments for policy reform. The focus of most of the essays is upon what prosecutors are actually doing. There is much discussion of the prospects of, and impediments to, using the criminal prosecution of corporations as a vehicle for regulation. There is little discussion of the normative justification for, or desirability of, doing so. Aside from Richard Epstein, none of the contributors to the volume even raise the question as to whether punishing collective entities for the offenses of individual employees is justified. The value of this book resides in the information it provides about the nuts and bolts of regulating corporate behavior through prosecution, not in any consideration of the appropriateness of doing so.

A look inside | The chief benefit of reviewing a collection of essays is to provide a quick index to the useful information that the essays contain. But before turning to that task, a comment on the literary quality of the essays is in order. With a few exceptions, these essays are surprisingly readable. Given the density of the factual information they contain, most of the essays are remarkably less eye-glazing than one might expect. Most of the authors have managed to present their account of prosecutorial practices in an at least somewhat engaging way that makes reading the entire collection much less of a chore than it otherwise might be.

The first essay in the collection, "The Causes of Corporate Crime: An Economic Perspective," by Cindy R. Alexander and Mark A. Cohen, constitutes one of the exceptions to my favorable assessment of the essays' readability. This essay provides an economic analysis of the incentives bearing on criminal activity in the corporate setting, and is precisely as boring to read as one would expect such an analysis to be. An interesting if not unexpected feature of such an economic analysis is its utter lack of concern with the moral aspect of the criminal sanction as evidenced by the authors' observation that "[t]he possibility of deterring crime by penalizing … an individual who does not directly engage in crime is thus apparent." From an economic perspective, punishing the innocent is merely a potentially effective tool for suppressing undesirable conduct.

The economic analysis and review of empirical evidence, which is thorough and professional, produces what appears to me to be the unsurprising and uninformative conclusion that 1) there is a relation-

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ship between corporate crime and factors such as the financial performance of the firm, the perceived gain from the crime, the perceived risk of detection and severity of punishment, the corporate culture, and the opportunity to commit crime and corporate internal governance, and 2) little is known about the nature of this relationship. In sum, to the extent that there is value in providing a detailed theoretical grounding for what most people already believe and for officially cataloging how little we know about the success of recent and contemporary law enforcement efforts, this essay does an excellent job of providing it.

The second essay, Richard Epstein's "Deferred Prosecution Agreements on Trial," is one of the more valuable ones, and the editors did well to position it early in the collection. Epstein provides an excellent synopsis of what gave rise to the "grand inversion": the situation in which "the state's decision to prosecute imposes greater burdens on individual defendants than conviction of the underlying offense." His account of the grand inversion includes a concise explanation of why imposing criminal punishment on corporations is misguided, and a useful reminder that the utilitarian objective of criminal punishment is not maximal, but optimal, deterrence. Although he may decry the grand inversion that gave rise to the use of corporate deferred prosecutorial agreements (DPAs), Epstein recognizes that such DPAs are here to stay and he explores what can be done to ensure that they are not abused. Employing the constitutional doctrine of unconstitutional conditions as an analog, Epstein argues that DPAs should not impose constraints on corporations that are unrelated to the goal of criminal prosecution, "which is to make the punishment match the severity of the wrong." Thus, in one concise essay, Epstein brings the reader up to speed on the nature of corporate prosecution and proposes a practical reform for one of its current abuses.

The next two essays, "Potentially Perverse Effects of Corporate Criminal Responsibility," by Samuel W. Buell, and "Inside-Out Enforcement," by Lisa Kern Griffin, are of a piece in that they address the effects of sharing law enforcement authority among criminal prosecutors, civil regulatory agencies, and the corporations themselves. Buell explores how the division of enforcement authority between DOJ prosecutors and regulatory agencies such as the Security and Exchange Commission can influence the effectiveness of government efforts to reduce corporate crime. He recognizes that, ideally, enforcement should be "pyramidal, with escalating layers of increasing sharp measures of control, starting at the bottom with self-regulation and capping off at the top with harsh forms of punishment." He argues that, because of weaknesses in civil enforcement, our current system has become an inverted pyramid as too many cases get pushed to the top for effective enforcement action. Buell discusses what he calls the civil-criminal gap that arises because of the practice of regulatory agencies such as the SEC of settling suits without stigmatizing admissions of guilt, and he calls for reform of civil regulatory practice so that it "has greater reputational consequences, decides more, and requires more of firms."

These essays are surprisingly readable. Given the density of the factual information they contain, most of the essays are remarkably less eye-glazing than one might expect.

Griffin explores the effects of exporting significant portions of the law enforcement function to the corporations themselves. She notes that limitations on prosecutorial resources require prosecutors to deputize "private-sector partners" to help them enforce the law. She then explores the ways in which the incentives of both prosecutors and their private partners tend to skew the enforcement away from the optimal outcome. She usefully explores the way DPAs are negotiated, the effect of appointing a compliance monitor, and the discrepancy between the current command-and-control approach and the "collaborative ideals of horizontal negotiation" to show how the results of prosecutorial practice stray from desirable regulation. Accordingly, she, like Buell, advocates more integration between civil regulators such as the SEC and criminal prosecutors.

Although the next two essays, "The Institutional Logic of Preventative Enforcement," by Mariano Florentino-Cuellar, and "Collaborative Organizational Prosecution," by Brandon C. Garrett, constitute the other exceptions to my positive assessment regarding readability, they nevertheless contain a valuable, if chilling, account of how the law enforcement imperative tends to eclipse all considerations of liberalism. In contrast to Buell, Florentino-Cuellar extols the virtue of the inverted pyramid. He details the greater autonomy and lesser political accountability that prosecutors enjoy in comparison with regulatory agencies, and how they benefit from the "perceived importance of their crime-fighting mission." He follows this with a wonderful account of what might be called a criminal enforcement "ratchet effect"—the process by which each expansion of criminal regulation leads to the next. In showing how the criminalization of regulatory violations stigmatizes them so that "the criminal law label becomes capable of changing the policy environment over time," Florentino-Cuellar explains how political incentives inevitably swell the top of the inverted pyramid. Garrett then follows with an account of how prosecutors and regulators can collaborate to divide labor and engage in mutually reinforcing actions to greatly increase the amount of control the government can exercise over businesses.

The next two essays, "The Prosecutor as Regulatory Agency," by Rachel E. Barkow, and "What Are the Rules If Everyone Wants to Play? Multiple Federal and State Prosecutors (Acting) as Regulators," by Sara Sun Beale, explore the effects of regulation through prosecution. Barkow provides a concise and useful account of the source of prosecutorial power and examples of how that power has been used to regulate businesses by federal and state prosecutors. She then evaluates the adequacy of prosecutorial regulation with regard to prosecutors' accountability, institutional competence, and procedural reliability. Although she finds little difference in accountability between prosecutors and regulators, she notes that regulation by prosecution has even fewer procedural safeguards than does agency regulation and prosecutors are not required to base their decisions on scientific data and expert opinion.

Beale then explores how the threat of prosecution in multiple jurisdictions affects the efficiency of prosecutorial regulation. Noting that corporations are simultaneously subject to prosecution by federal and several state authorities, she uses the prosecution of WorldCom to illustrate how multiple prosecutions can undermine the regulatory efficiency of each. She then details both the incentives and barriers to multijurisdictional prosecution. In doing so, she highlights how political incentives can skew the effects of such prosecutions away from an optimal regulatory outcome and toward governmental rent seeking, if not extortion. Beale ends her essay with a survey that demonstrates just how little protection current law provides against such unfortunate results.

In the final essay, "Reforming the Corporate Monitor," Vikramaditya Khanna tells you everything you wanted to know about corporate monitors, and more. Khanna begins with a historical overview of how the practice of assigning monitors as part of DPAs and non-prosecutorial agreements evolved. He then identifies the conditions under which the use of monitors makes sense: when there is a need for greater deterrence than can be provided by financial penalties. When the appointment of a monitor is appropriate, the monitor becomes part of the corporate governance structure. With this in mind, Khanna provides an excellent analysis of how monitors should be appointed (he recommends a market for monitors), what powers they may properly wield, and what duties they should owe to corporate shareholders and the judiciary. He follows this with a detailed list of reforms designed to regularize the processes of deciding whether to appoint a monitor, selecting the monitor, and assigning the monitor his or her powers. Finally, Khanna examines the amount of judicial oversight that should be applied to the selection and supervision of monitors (more before selection, less afterward) and considers whether the reports of corporate monitors should be made available to the public (generally they should).

Conclusion | In closing, *Prosecutors in the Boardroom* is both useful and frightening. It is useful because it supplies a wealth of empirical data about contemporary corporate law enforcement policy. It is frightening because it demonstrates what happens when well-intentioned, intelligent, dedicated law enforcement agents are freed from the constraints of liberalism—the prohibition on using those who are innocent of personal wrongdoing to achieve collective ends. R

The Economics of Takings

REVIEWED BY ILYA SOMIN

The Economic Theory of Eminent Domain: Private Property, Public Use
By Thomas Miceli
214 pages; Cambridge University Press, 2011

The Supreme Court's controversial 2005 decision in *Kelo v. City of New London* led to massive public controversy over an issue that previously had been of interest mostly to economists and legal scholars: the government's use of eminent domain to take private property and transfer it to other private parties. *Kelo* ruled that the Public Use Clause of the Fifth Amendment allowed the government to condemn property for transfer to private parties in order to promote "economic development." It concluded that virtually any claimed public benefit satisfies the constitutional requirement that eminent domain can only be employed for a "public use." In the aftermath of *Kelo*, polls revealed that some 80 percent of the public opposed the ruling, and 44 states passed eminent domain reform legislation.

Much of the debate over *Kelo* has focused on legal issues: whether the Supreme Court correctly interpreted the U.S. Constitution. But there are also important economic policy issues at stake. Do we really need private-to-private takings in order to facilitate economic growth and provide other public benefits, or do such condemnations generally do more harm than good? *Kelo* has also rekindled debate over other questions that were not directly involved in the case, such as the amount of compensation that government should pay to property owners whose land is condemned, and whether or not the state should be required to compensate owners for "regulatory takings"—situations where government regulations restrict property owners' rights without formally taking title to the land and usually without physically occupying it.

Thomas J. Miceli's *The Economic Theory of Eminent Domain* is one of the best and most thorough analyses of the economics of takings to date. It covers not only the public use questions directly addressed in *Kelo*, but also the related compensation and regulatory takings questions. The book will be of great value to economists, legal scholars, policymakers, and others interested in eminent domain.

At the same time, the book does sometimes underrate the dangers posed by the ability of government to use eminent domain for the benefit of influential private interests. Miceli also occasionally seems to overestimate the ability of judges to make complex economic judgments about the efficiency of various government policies.

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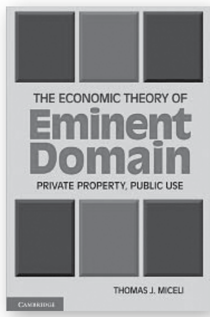
Public use and holdouts | Miceli devotes the first part of the book to the problem the Supreme Court considered in *Kelo*: When should the government be allowed to condemn private property? He argues convincingly that the use of eminent domain is only likely to be economically efficient in cases where there are "holdout" problems: situations where one or a small number of individual property owners who refuse to sell to a developer might block a project whose value exceeds that of the current uses of the land. In such cases, the market might fail to produce an efficient outcome because developers are unable to assemble the land they need.



For example, consider a situation in which a developer needs to acquire five square miles of land to build a factory that is worth $1 million more than the current uses of the property. But the land is currently divided up between 1,000 owners. If the developer tries to purchase the 1,000 parcels piecemeal, one or more of the owners might try to take advantage of the situation by asking for an exorbitant price, such as 90 percent of the expected value of the project. If even a few of the current owners try to hold out in this way, the project is likely to be scuttled, since the developer would end up paying more for the land than the expected profit. Like many other scholars, Miceli concludes that eminent domain is needed to overcome such holdouts.

On the other hand, Miceli effectively argues that eminent domain is not justified in most other situations. Many local governments and other defenders of the *Kelo* decision contend that eminent domain can be justified any time the new use of the condemned property might contribute to the local economy. But, absent holdout problems, private sector transactions should be able to achieve the most economically efficient uses of the land as well or better than the state. A developer who has a more productive use for a piece of land than the current owners can simply purchase it from them.

Some economists and legal scholars claim that eminent domain is also needed in order to produce public goods that might be underproduced by the market. But, as Miceli explains, subsidies for development or tax incentives can achieve the same goal and are less intrusive and coercive than eminent domain.

Miceli's holdout theory does have some shortcomings of its own. As he recognizes, the private sector has various mechanisms of overcoming holdout issues without resorting to eminent domain. The best-known is secret assembly, under which developers purchase the land they need from the current owners without letting them know that they are planning a large-scale development project. This is how the Disney Corp. was able to assemble the land for Walt Disney World, for example. In addition, even if a holdout problem is present, a proposed development project might still not be as valuable as the current uses of the condemned property. The taking could simply be the result of lobbying by powerful interest groups, such as a major corporation or influential developers. The *Kelo* taking itself was in part the result of lobbying by Pfizer Corp., a major pharmaceutical firm, which hoped to benefit from the condemnation. Interest group power also played a key role in the most famous pre-*Kelo* economic development taking: the 1981 *Poletown* case. Some 4,000 people in a Detroit neighborhood were forced out of their homes in order to transfer their property to General Motors so that the latter could build a new factory. In both cases, the measurable economic costs of the taking far outstripped the benefits, even discounting the psychological harm inflicted on homeowners.

Because of considerations like these, Miceli ultimately argues for "a balanced approach to public use under which courts would treat the holdout problem as a necessary, but not a sufficient, condition for extending the power of eminent domain to private parties" (p. 153). Unfortunately, he does not explain how the different factors should be weighed against each other. How can judges tell whether a given holdout really requires the use of eminent domain to overcome it?

Moreover, it is far from clear that judges have the specialized knowledge necessary to sort out cases where there are genuine holdout problems from those where the fear of holdouts is merely a pretext for a taking sought by influential interest groups. Similarly, judges might have difficulty telling the difference between owners who refuse to sell because they are trying to be strategic holdouts from those who refuse because they genuinely value the land more than the would-be developer does. If the latter is the case, using eminent domain is ill-advised even from the standpoint of policymakers whose only interest is economic efficiency. It is inefficient to forcibly transfer land from owners who value it more to those who value it less.

In some instances, Miceli also underrates the social costs inflicted by takings. For example, he argues that the use of eminent domain for purposes of "urban renewal" should be permitted because, otherwise, holdout problems might prevent the revitalization of depressed urban neighborhoods. However, the actual record of urban renewal takings is extremely dubious. Since World War II, hundreds of thousands of people have been forcibly displaced by such condemnations, inflicting tremendous harm on them, often for little or no economic gain. Urban renewal takings might be justified, in some cases, as a matter of economic theory. But the incentives of real-world governments led them to be used far more widely than any economic logic would justify.

Compensation | After the discussion of public use, Miceli considers the longstanding debate over the amount of compensation that should be provided to property owners whose land is condemned. Current legal doctrine interprets the Fifth Amendment's mandate of "just compensation" for takings as requiring the government to pay the "fair market value" of condemned property. However, some economists argue that the best policy is to pay zero compensation because, otherwise, landowners might overinvest in their land. Owners might discount the risk of condemnation if their losses are fully compensated by the government.

On the other hand, an opposing group of commentators fears that the zero compensation would lead to excessive condemnations because government bodies would not consider the costs that condemnation inflicts on property owners if governments did not have to pay for them. Miceli suggests that both arguments have some merit, which leaves him at something of an impasse. He notes that it is possible to square this circle through tax assessment policy, which in theory could compensate owners at exactly the right levels to optimize their incentives. However, this is only feasible under theoretical conditions that are unlikely to occur in the real world, such as a "benevolent" government that seeks only to maximize economic efficiency.

In my view, both Miceli and much previous literature overstate the zero compensation argument. Even if full compensation leads property owners to overinvest because they discount the possibility of a taking, the resulting inefficiency is likely to be small because most properties have a very low probability of being targeted for takings. In addition, if Miceli's analysis in the first part of the book is correct, the use of eminent domain by government should be strictly limited, which would further lower the risk of condemnation. The problem can also be at least partly mitigated by simply discounting the level of compensation slightly by a percentage equal to the likelihood of condemnation. That way, owners will diminish their investments at the margin to a degree that incorporates condemnation risk. This simple solution is unlikely to be perfect, but would take a bite out of an already modest problem.

In the real world, excessively high compensation is less common than the opposite. Miceli reviews recent empirical research suggesting that most owners of condemned property do not actually receive the fair market value compensation required by law. A comparatively fortunate few get more than fair market value, but a larger percentage gets less. Local governments can get away with lowballing owners who lack legal sophistication or simply do not have the time and money to fight it out in court.

Like many previous scholars, Miceli recognizes that even if owners succeed in getting fair market value compensation, they may not be fully compensated for their losses because many owners also attach a "subjective value" to their land over and above its market price. If they valued the property at its market value or less, they would likely have sold it on the open market even before the government sought to condemn it. The book provides a careful review of the various creative schemes economists and legal scholars have come up with to try to induce owners to reveal their true valuations and enable government to come up with a more accurate compensation formula. Miceli concludes that these ideas are largely impractical and unlikely to be implemented successfully. Ultimately, the difficulty of coming up with an accurate and efficient formula for measuring compensation is an additional argument for constraining the use of eminent domain in the first place.

In one of very few questionable conclusions in this part of the book, Miceli suggests that the problem of public use is only important because of inadequate compensation. If we could fully compensate the owners of condemned property, they would, presumably, have no reason to object to the loss of their rights.

But public use restrictions on takings might still have merit even if property owners are fully compensated, indeed even if they actually gain more from takings than they lose. The owners are not the only victims of ill-advised takings like *Poletown* and *Kelo*. The community at large also suffers because of the expenditure of public resources and the destruction of existing land uses that are often replaced with less valuable ones. Indeed, the higher the compensation payments to owners, the greater the loss to the taxpayers. As with many other constitutional rights, Fifth Amendment protections for property rights benefit more than just those who exercise these rights directly. The First Amendment right to free speech, for example, not only protects individual speakers but also helps the rest of society by ensuring open debate on political issues. Similarly, the Public Use Clause protects the general public as well as individual property owners.

The community at large also suffers because of the expenditure of public resources and the destruction of existing land uses that are often replaced with less valuable ones.

Regulatory takings | The last part of Miceli's book addresses the difficult problem of regulatory takings, cases where government regulations restrict owners' options and reduce the value of their property without actually taking over title. Advocates of a robust regulatory takings doctrine argue that the concept should be defined broadly in order to protect property owners and reduce harmful regulations. Opponents claim that requiring compensation would deter government from implementing beneficial regulations.

Miceli seeks to cut through this longstanding debate by proposing that compensation should be required when the regulation at issue is economically inefficient, but not when it is efficient—in the sense that it creates more economic value than it destroys. On the level of abstract economic theory, it is hard to quarrel with this view. Who could be in favor of inefficient regulations or against efficient ones? In practice, unfortunately, Miceli's proposal runs into serious problems. The most obvious is the enormous informational burden it imposes on courts. How are judges to determine whether a regulation is efficient or not? Most judges lack expertise in economics and regulatory policy. Even those that do have such knowledge might still lack the information necessary to evaluate a specific regulation. For the same reasons that the "subjective value" of property is difficult to estimate in the context of compensation payments, it is also often difficult or impossible to gauge the true costs of regulations that restrict land uses.

To his credit, Miceli anticipates this objection. He suggests that it is overstated because courts often make similar judgments in tort cases when determining what qualifies as negligent behavior. However, evaluating the efficiency of a regulatory regime that restricts thousands of landowners is a far more difficult task than evaluating the risks posed by a single individual's or firm's discrete decision—the sorts of questions decided by courts in most run-of-the-mill tort cases. When tort suits do address broad policy questions—as in mass tort cases involving the production practices of major industries—the judiciary's work has come in for heavy criticism by economists and legal scholars.

It would be a mistake to reject Miceli's idea out of hand. But the theory would be more persuasive if it were coupled with a better explanation of how courts can engage in the task of judging efficiency.

Miceli's argument also runs into an important legal and moral objection. The U.S. Constitution requires "just compensation" for *all* takings, not just inefficient ones. As a matter of distributional fairness, we may want to compensate property owners even for efficient restrictions of their property, so that the cost of regulations that benefit the entire community will not be imposed arbitrarily on one small group.

Conclusion | Miceli's *Economic Theory of Eminent Domain* is an excellent account of the major issues in its field and is likely to become a standard reference for scholars. But not all of its arguments are fully convincing. The debate over eminent domain that heated up after *Kelo* is likely to continue.

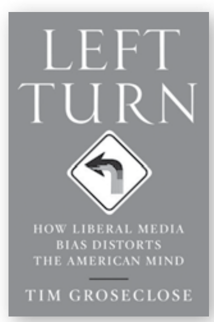
Unfair and Imbalanced

REVIEWED BY DAVID R. HENDERSON

Left Turn: How Liberal Media Bias Distorts the American Mind
By Tim Groseclose
292 pages; St. Martin's Press, 2011

Virtually all of us who identify ourselves as libertarians or conservatives (I'm the former) have believed, for as long as we have been paying attention, that the mainstream media, whether print or electronic, have a left-wing bias. The late columnist Edith Efron, in her 1971 book *The News Twisters*, documented that bias among the three major television networks of the time—ABC, CBS, and NBC. Now, University of California, Los Angeles political scientist Tim Groseclose has actually *measured* the bias, not just of the three traditional networks, but also their present-day network competitors and major newspapers.

Most of his findings will probably not surprise most readers of this publication. Groseclose concludes that, indeed, the mainstream media do tilt left. Why then do I review a book that tells us what we already "know"? There are four reasons: First, most of us don't know it to the extent Groseclose knows it—his argument is an empirical tour de force. Second, he is so numerate that he makes clear with the data just how extreme the left-wing bias is. Third, there are some surprises in the data, particularly about the *Fox News Channel* and the *Wall Street Journal*. Fourth and finally, Groseclose shows that the biased information people get causes them to vote to the left of their true positions.



Measuring bias | He introduces the idea of a political quotient (PQ) to measure politicians' and voters' place on the "liberal"/conservative spectrum. (I put "liberal" in quotation marks because so-called liberals are not liberal at all, but actually social democrats. As a libertarian, *I'm* a liberal.) He does it based on how politicians voted—and how you, as a prospective politician, would have voted—on 10 issues that the left-wing organization Americans for Democratic Action highlighted. If you voted the ADA's way on everything, you would earn a PQ of 100. If you voted against the ADA on everything, you would get a zero.

Groseclose shows that the average voter has a score of 50.4. Rep. Michele Bachmann (R, Minn.), the Tea Party darling, earns a –4.1 and, on the other end, Democratic Reps. Nancy Pelosi (Calif.), Barney Frank (Mass.), and Ron Dellums (Calif.) all score over 100. How could they go outside the expected 0–100 range? The reason, Groseclose explained in an interview, is that he needed to norm the data to make it comparable across time periods, and the result was some politicians with scores outside the 0–100 range.

I took his test and scored a 20, receiving a "liberal" 10 points for voting to close down the Guantanamo Bay prison and another 10 points for voting for the Dorgan Amendment to allow Americans to buy prescription drugs from Canadian pharmacies. (I should note that Groseclose's description of the Dorgan Amendment in his survey was incomplete. While he did explain that the legislation would have allowed imports from foreign pharmacies, he didn't explain that it would also have restricted drug companies' ability to limit sales to Canada. That second provision would have been a clear-cut attack on firms' economic freedom. Had Groseclose stated the issue accurately, I would have voted no and my net PQ would have been 10.) On a more comprehensive 40-question survey on his website, *timgroseclose.com*, I earned a 4.2.

Once he computes PQs for various politicians, Groseclose then goes on to compute a slant quotient (SQ) for the media. He does so by measuring the frequency with which media articles (not editorials) quote various

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think tanks. The result, which I expected, is that the media are distinctly slanted to the left. The SQ for the *New York Times*, for example, is 74, about the same as that of Sen. Joe Lieberman (I, Conn.). A full 18 of 20 news outlets examined were to the political left of the average American voter, who, as noted above, was at about 50. Only two outlets were to the right: Fox News Channel's *Special Report with Brit Hume*, which scored an almost-moderate 39.7, and the *Washington Times*, with a 35.4. The *Jim Lehrer Newshour*, somewhat surprisingly, had only a mildly left SQ of 55.8.

One number that will surprise many people is the *Wall Street Journal's* SQ of 85.1, making it the furthest-left of all the media outlets Groseclose evaluates. I was surprised at how far left it was but, as a regular *Journal* reader for almost 40 years, I was only a little surprised.

The bias shouldn't be surprising given the political views of reporters. Surveys show that Washington correspondents vote for the Democratic candidate at a rate of 85 percent or more, Groseclose notes. Studies of contributions to presidential campaigns have found that more than 90 percent, and as many as 98.9 percent, of journalists who contribute to a presidential campaign give to the Democratic candidate. These overwhelming numbers mean, Groseclose says, that residents of left-wing academic communities like Cambridge, Mass. and Berkeley, Calif. are, on average, much more conservative than Washington media correspondents.

An example | Groseclose examines a few issues to show the bias at work. The first item he discusses is a *Los Angeles Times* article on the number of black students at UCLA. Groseclose dissects the story to show that the reporter, Rebecca Trounson, presents the data and reports interviews in a biased way. For instance, to buttress her case that the UCLA admissions process discriminates against black people, she cites six people, five of whom are on the political left, and only one of whom is conservative. Moreover, she pulls a favorite trick of left-wing reporters: identifying the ideology only of the conservative. Trounson's *L.A. Times* colleague, Ralph Vartabedian pulled the same trick on me—although, unlike Vartabedian, Trounson at least got the ideology right. (Vartabedian described me as a conservative. See my August 18, 2010 blog post, "Media Bias and the *L.A. Times*" for more.)

Currently, the average U.S. voter has the same political quotient as the average Iowa voter. But with no media bias, the average U.S. voter would, instead, be like the average voter in Kentucky or Texas.

I should note that the UCLA admissions process *is* racist. As Groseclose notes, UCLA discriminates, probably illegally, in favor of black applicants. One problem he identifies with Trounson's approach is that she missed the big story: the rising percentage of Asians at UCLA and the falling percentage of whites.

Groseclose had the guts to question Trounson, asking whether her political views affect the topics she writes about. She answered, "I don't know. Give me an example of a conservative topic."

So he gives the reader some great examples. One is a shocking story about how New Orleans mayor Ray Nagin refused a company's offer to haul away all the cars ruined by Hurricane Katrina within 15 weeks and pay $100 per car, or about $5 million, to the city coffers. Nagin turned down the offer and *spent* $23 million over six months to have the city government do the same job. Only one of the 20 media outlets covered the story: *Special Report with Brit Hume*.

Groseclose also tells of Katherine Kersten, a conservative reporter whom the *Minneapolis Star Tribune* hired as part of "an experiment." (The fact that hiring a conservative is an "experiment" in itself speaks volumes.) After six Muslim imams had acted suspiciously on a US Airways flight out of Minneapolis in 2006, some passengers complained and US Airways removed the imams. They sued. Kersten uncovered the fact, which no one else had reported, that the imams sued not only the airline, but also the complaining passengers. Much of the conservative media then took up the issue; the left-wing media pretty much missed it. The result was that Congress passed a law to protect the freedom of speech of the complaining passengers. (The dishonest way that Democrats in Congress tried to kill the law is worth reading about also.)

Effects of bias | But does the bias matter? On this issue, Groseclose shows himself to be a true academic in the best sense of that word: the data changed his mind. Early in his research, Groseclose believed that the media had no effect. But three studies that he cites convinced him otherwise: the left-wing bias of the media, he writes, affects how people vote. In one of the studies, Alan Gerber, Dean Karlan, and Daniel Bergan of Yale University sent out free 10-week newspaper subscriptions to randomly chosen households. Some got the left-leaning *Washington Post*; others got the right-leaning *Washington Times*. In the subsequent race for governor, those who got the *Post* voted 3.8 percentage points higher for the Democrat than those who got the *Times*. Information—whether biased or not—matters.

Interestingly, one person who believes the media have an effect is President Obama. In 2008, notes Groseclose, then-candidate Barack Obama told a reporter, "I am convinced that if there were no Fox News, I might be two or three points higher in the polls." This is actually about four times the effect that one of the studies cited by Groseclose finds.

He combines the three studies to find the net effect, not just of Fox News and other conservative outlets, but of all the media, including the left-wing media. The result is astonishing. Using basic algebra, he calculates that if the media had the same political quotient as voters, the average American voter would be more conservative because the media would not have tugged him or her to the left. How much more conservative? He illustrates with the 2008 presidential election. Rather than electing

Obama with a vote of 53 percent to John McCain's 46 percent, U.S. voters would have elected McCain with a vote of 56 percent to Obama's 42 percent. Can you say landslide?

In an interview with the Hoover Institution's Peter Robinson, Groseclose explained it another way: Currently, the average U.S. voter has the same political quotient as the average Iowa voter. But with no media bias, the average U.S. voter would, instead, be like the average voter in Kentucky or Texas.

To his credit, Groseclose believes in freedom of speech and of the press, and so does not advocate censorship to correct the bias. Instead, he suggests that reporters spend some time with average people in Kentucky or Texas. But don't look for that to happen soon.

Another of his proposals might have more traction. Groseclose advocates that various news outlets do what only *Slate* and talk radio have been willing to do: reveal the political leanings of their news people and other writers. He thinks this would start a healthy competition that would put pressure on more and more news organizations to reduce their bias. He could be right.

Left Turn's message is powerful, compelling, and—most important—based on empirical data. I do, though, have two small criticisms of the book:

First, I think Groseclose should have given credit to Efron for the fairly sophisticated method she developed over 40 years ago for doing content analysis of bias. It was much harder then, when the Internet didn't exist.

Second, he makes passing remarks that I think he would have trouble justifying. Two such lines particularly caught my attention: One was his quote from political scientist Keith Poole that pulling U.S. troops out of Iraq and Afghanistan could spell "the end of Western civilization." According to Poole, if you "just read Bernard Lewis," you'll realize what's at stake. The other is his statement at the book's end that it was Ronald Reagan who ended communism in Europe. Consider me strongly skeptical of both those claims.

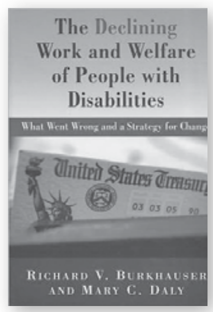
These small negatives do not undercut the power and importance of his message. I highly recommend *Left Turn*.

The Need for Disability Insurance Reform

REVIEWED BY GEORGE LEEF

The Declining Work and Welfare of People with Disabilities
By Richard V. Burkhauser and Mary C. Daly
American Enterprise Institute, 2011

This book focuses on two of the components of America's "safety net," Social Security Disability Insurance (SSDI) and Supplemental Security Income (SSI). Both are supposed to help disabled people, but their costs are growing far more rapidly than is the population of disabled Americans. The authors (Richard Burkhauser is the Sarah Gibson Blanding Professor of Public Policy at Cornell University; Mary Daly is the head of microeconomic research at the Federal Reserve Bank of San Francisco) conclude that SSDI and SSI costs are rising at an unsustainable rate and that the programs are drawing many people who could work into the dead end of living on government disability checks.



Burkhauser and Daly have identified a serious problem, but I don't think their solution is sufficiently radical. Let's go through their diagnosis first.

The problem | SSDI is a social insurance program that was established to provide cash benefits to men and women of working age who become disabled—that is, unable to perform "any substantial gainful activity." The amounts paid to them depend on their past labor earnings and funds to pay those benefits come from a flat-rate tax levied on employers and employees. The SSDI program is distinct from SSI, which is a mean-tested welfare program that pays benefits to adults and children who are disabled. The funds for SSI come from general tax revenues.

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Disability caseloads as a percentage of the population have been rising steadily for decades in both programs. That increase would make sense if it were true that disabilities are becoming more prevalent in society, but the authors show that they are not. The rising percentage of Americans receiving disability benefits is not due to increasing incidence of disability, but is instead due to changes in the administration of the programs—caused in part by a U.S. Supreme Court decision—that made it easier for people to get on and stay on them.

That, of course, is bad news for taxpayers, but Burkhauser and Daly argue that these trends have also been harmful to the disabled themselves. Over the last 30 years, the relative position of those on disability benefits has declined with respect to the rest of society. Easy money has been luring many people who might work into the disability world. However, disabled workers often find many opportunities for improving their circumstances if they stay in the ranks of the employed. What seems to be "compassionate" is often detrimental; SSDI and SSI are proof of that.

A telling piece of evidence in this regard is the fact that claims of disability filed under the categories most difficult to disprove—mental conditions and musculoskeletal problems—have been increasing the most rapidly. Apparently more and more Americans are discovering that they can get disability checks by claiming that they are suffering from, e.g., back problems or depression that keeps them from holding down a job. The system allows many who are not incapacitated to get away with it.

The situation with regard to disabled children under SSI is at least as disturbing. The rationale for SSI was that it would give families who have children with disabilities some additional income to compensate for the fact that one or both parents were kept from working because of the need to care for the child. Over time, however, this aspect of the program has evolved into an entitlement for any family that can claim to have a disabled child. Furthermore, the authors report, "a substantial fraction of children on the SSI-disabled children program move directly to the SSI-disabled adults program without attempting to enter the labor market." Once they are on disability relief, very few ever get off. Again, public policy encourages individuals who might have become self-supporting (at least in part) to become permanent wards of the state.

Once they are on disability relief, very few ever get off. Again, public policy encourages individuals who might have become self-supporting (at least in part) to become permanent wards of the state.

At the root of the mushrooming costs of SSDI and SSI are the subjective criteria that allow officials wide discretion in deciding whether to approve claims. Evidently, many officials are inclined to be generous and thus we are seeing more and more determinations that children and adults are disabled.

Burkhauser and Daly merely hint that the awarding of disability benefits is far more frequent than it should be due to the proclivity among Social Security Administration personnel to approve benefit claims and avoid having to turn people down. In an August 2000 Cato paper, "Facilitating Fraud: How SSDI Gives Benefits to the Able Bodied" (*Cato Policy Analysis* No. 377), James M. Taylor argued that this is a crucial part of the problem. Based on many cases he had studied, Taylor stated, "When a federal agency charged with disbursing federal dollars is derelict in enforcing its qualification standards, and instead seems extremely eager to hand out free money, the fault for the ensuing abuse lies more with the federal agency than with the individual claimants."

Personnel is policy, as the saying goes. When it comes to government agencies charged with deciding whether people who apply for benefits receive them or not, there is a natural inclination for people who want to feel helpful to apply for positions. Combine that with vague standards and no penalty for deciding cases in favor of the applicant and it is almost inevitable that the percentage of people who claim and receive disability benefits will rise.

Furthermore, the system is heavily stacked in favor of claimants. In cases where the SSA initially denies a claim (unfortunately, the book gives no figures on the frequency of denials or how that percentage has changed over time), the individual can request a reconsideration and, if that is not granted, then he can appeal to an administrative law judge (ALJ), where he can have legal representation and present witnesses. (If the SSA still contests the claim, it may not bring in lawyers and witnesses.) If the ALJ turns down the claim, the claimant can then appeal to federal district court. A decision in favor of the claimant at any stage is final. (For more on the appeals process, see "What Should We Do about Social Security Disability?" Fall 2011; "What We Should Do About Social Security Disability," p. 16.)

While the book doesn't go into the effect of lawyers, there is good reason to believe that they (especially firms specializing in disability claims) often try to deceive the ALJ. The stakes are considerable since the lawyers are entitled to 25 percent of any back pay awards.

Reform | Burkhauser and Daly conclude that "antiwork incentives in SSDI/SSI have led to a disability system designed to enroll too many individuals for long-term cash benefits in lieu of work." They point to the 1996 welfare reforms that changed incentives away from dependency on government largesse and toward work and argue that disability programs can be reformed along similar lines. They would begin by separating the two programs and devolving SSI to the states. The states, they argue, would be more inclined to minimize its costs by creating programs to keep people in the labor force (or encourage them to get into it), as they did for single mothers when Congress replaced Aid to Families with Dependent Children with Temporary Assistance to Needy Families.

Regarding SSDI, their main policy change would be to make the payroll taxes on employers subject to "experience rating." What that means is that the more a company's employees become eligible for and draw SSDI disability benefits, the higher the company's tax rate would go. We have adopted that approach for unemployment insurance taxes—companies that rarely or never lay off a worker pay a minimum rate, while companies that often lay off workers pay the maximum. Burkhauser and Daly say that the change to experience rating would give employers an incentive to look for ways to accommodate or rehabilitate workers who suffer some disability but can still work, rather than allowing them to easily slide into the dead end of disability.

Those are not bad ideas. They would probably lead to marginal improvements: more people who have a disability would be working and fewer would be drawing benefit checks. The authors say that such a result would be consistent with the policy of the Americans with Disabilities Act (ADA).

When I first saw the title of the book, I assumed that one of its *targets* would be the ADA since many scholars who have analyzed the effects of the statute maintain that it has been detrimental to disabled people on the whole. For example, Thomas DeLeire, now the director of the La Follette School of Public Affairs at the University of Wisconsin, wrote in this magazine, "The burden of [the ADA's] cost has fallen especially hard on those workers least likely to have been accommodated voluntarily by firms in the absence of ADA, namely, less experienced and less-skilled workers and workers with mental disabilities"

("The Unintended Consequences of the Americans with Disabilities Act," Spring 2000). By making it costly—potentially very costly—to hire anyone who seems to have a disability, the statute creates a strong incentive for employers to avoid taking chances with them.

The authors acknowledge this line of criticism (mentioning DeLeire specifically) but downplay the effect of the ADA itself on lessening the employment prospects for people with disabilities. They suggest that we might amend the ADA to "exclude from harm" employers who hire workers with identifiable high risks. Such tinkering might marginally reduce the hazards of hiring the handicapped but it wouldn't eliminate them, and it introduces still more complexity into an already treacherous statute.

A good case can be made that the ADA creates far more costs than benefits in total, but putting that aside, the reforms Burkhauser and Daly propose don't seem to strike at some of the worst features of the status quo. Even with their reforms, we would still have a system that is stacked heavily in favor of claimants and a system in which politicians' favorite three villains (waste, fraud, and abuse) are widespread. (Taylor's paper noted above contains many examples, including instances in which workers have sued their employers under the ADA for not offering them workplace "accommodation" while at the same time collecting disability benefits.)

Summing up, this is an eye-opening book on a serious policy issue. It opens debate on how we should approach the problem of the disabled, but we should now hear from analysts who suggest more radical changes that don't rely on government. R

IN REVIEW | WORKING PAPERS

Below is a summary of some recent papers that may be of interest to *Regulation*'s readers.

BY PETER VAN DOREN

The Social Costs of Carbon Emissions

- "Estimates of the Social Cost of Carbon: Background and Results from the RICE-2011 Model," by William Nordhaus. October 2011. SSRN #1945844.

William Nordhaus estimates that the social cost for the emission of a ton of carbon dioxide in 2015 will be $11 in 2005 dollars, equal to about $12.50 in today's dollars. That amounts to about 12.5 cents of social cost per gallon of gasoline (which releases the equivalent of about 20 pounds of carbon dioxide) and 1 cent per kilowatt hour of non-baseload electricity (1.5 pounds) or 1.4 cents per kWh for coal-fired electricity (2.2 pounds). The variation we have experienced in gasoline and electricity prices in recent years dwarfs the increases from an optimal carbon tax. Thus incremental adjustments in behavior, rather than a radical alteration of energy infrastructure, would seem to be optimal in the near future.

This conclusion is reinforced by the introduction of equity considerations. The future generations who will be the beneficiaries of any investments we make now to reduce carbon emissions will be much richer than current generations. If current incomes were uniform, then the tax on today's "poor" to help tomorrow's "rich" should be lower than the $12.50 Nordhaus estimate. Tweaking this scenario to make it more realistic, assume the costs today are incurred by the richer countries like the United States, which are four times richer than other countries. The benefits will accrue to all countries 70 years from now. Further assume a 2 percent annual growth in consumption for all countries. The result of these assumptions is that consumption 70 years from now will be four times today's level. Under such assumptions there would be no equity adjustment to the optimal carbon tax because those taxed (the rich now) and those receiving the benefits (the future poor) would have the same income.

Should we weight the social cost of carbon results for those scenarios in which probabilistically the temperature change is high? Recent developments in insurance theory recommend that we take account of not just damages but also the relative income of the scenario in which the damages occur relative to the scenarios that would be charged a premium to prevent the damages. If the costs occur in the rich eras, then you would not want to "tax" the poor periods to smooth consumption. Nordhaus writes:

> Suppose all the damages came because more intense hurricanes flooded the beach houses of very rich people in states of the world where incomes were very high. The logic of the result is that we should not pay an insurance premium today (paid for by non-rich people today) to insure against floods of rich people's houses in the future. (p. 21)

Peter Van Doren is editor of *Regulation* and senior fellow at the Cato Institute.

Sports Stadium Subsidies

- "League Structure and Stadium Rent Seeking: The Role of Antitrust Revisited," by David Haddock, Tonja Jacobi, and Matthew Sag. January 2012. SSRN #1983447.

Public subsidies for new professional sports stadiums in the United States are a large and growing problem (see "The Stadium Gambit and Local Economic Development," Summer 2000). They occur because sports teams credibly threaten to move from their current city to a city that will subsidize them.

In contrast, English soccer stadiums are private, older, and frequently renovated rather than torn down and rebuilt with enormous infusions of public money.

According to the authors of this paper, there is an important difference between professional sports in the United States and England: the promotion and relegation system used in the latter. Top-finishing teams in a professional league are promoted to a more prestigious league the following year, while bottom-finishing teams are relegated to a lower league. Teams are geographically fixed but leagues, in effect, reform every year. So entry into the major leagues is much easier than in the United States and threats to move an English team to gain subsidies are not credible.

Shadow Banking and Bankruptcy

- "A Dialogue on the Costs and Benefits of Automatic Stays for Derivatives and Repurchase Agreements," by Darrell Duffie and David Skeel. January 2012. SSRN #1982095.

In previous columns I have described the development of the "shadow banking system," the replacement of the traditional deposit and loan system with an alternative in which overnight cash deposits were transformed into packages of securitized loans. By the mid 2000s this system accounted for two-thirds of lending in the United States, while traditional bank loans accounted for the other third. In the fall of 2008, because of the downturn in housing values and the resulting defaults on mortgage debt and mortgage securities packages, the cash depositors in this system lost confidence. They fled the entire securitized loan system and instead purchased safe Treasury debt.

An important policy change leading to the development of the shadow banking system was the exemption from the automatic stay in bankruptcy of Qualified Financial Contracts (QFCs), including derivative and asset repurchase agreements. Bankruptcy normally freezes all transactions until a judge determines the market value of assets and divides them equally among all creditors. QFCs have been exempt from the automatic freeze. Originally the exemption applied only to asset repurchase agreements ("repos") involving Treasury debt. In 2005 the safe harbor exemption was extended to repurchase agreements involving mortgage securities and other repurchase agreements that were the heart of the shadow banking system.

The bankruptcy exemption has five costs:

- The cash depositors have much less incentive to monitor the securities given to them as collateral because they can get their cash back just by giving back the collateral.
- A financial institution has incentive to have a very large repo "deposit" base so that it will be bailed out if it fails.
- Repos involve inefficient substitution away from traditional banking.
- The sale of illiquid repo assets to raise cash demanded by skittish depositors exacerbates the lack of confidence in the system by investors.
- Financial institutions financed by exempt repos have much less incentive to file for bankruptcy because bankruptcy would not prevent a run and demands for cash. For example, AIG spiraled down rather than file for bankruptcy because the Goldman margin calls could not be retrieved by AIG like all other unusual payments in normal bankruptcy proceedings.

The authors of this paper recommend a return to the pre-2005 rules in which only repos involving liquid Treasury securities are exempt from the bankruptcy automatic stay. No purpose is served by delaying access to liquid securities (like treasuries) because, by definition, they are easily converted to cash. The authors believe that the 2005 expansion of the safe harbor to include repos involving mortgage-related securities and other illiquid assets was a mistake.

Economic Consequences of *Citizens United*

- "Corporate Politics, Governance, and Value Before and After *Citizens United*," by John C. Coates, IV. December 2011. SSRN #1975421.

While the *Citizens United* Supreme Court decision has been good for free speech, has it been good for shareholder value? John Cotes examines data for the S&P 500 from 1998–2004, 2008, and 2010. He finds that corporate political activity is more frequent in those corporations that use corporate jets and whose chief executive officers later take political jobs. He finds that firms that were politically active in 2008 experienced a significant decline in shareholder value in 2010 relative to firms that were not politically active in 2008. In general, political engagement is negatively correlated with shareholder value. The exceptions include the most heavily regulated industries and the defense sector in which political activity helps shareholders.

These results remind me of Robert Sitkoff's ("Politics and the Business Corporation," Winter 2003–2004) revisionist description of the origins of the restriction on direct corporate donations to political campaigns, enacted in 1907. Corporations play a prisoners' dilemma game with respect to participating in the political system. All corporations collectively would be better off if none of them sought advantages from the public sector, but each of them individually has incentives to defect, particularly when politicians seek money from them and threaten them with adverse policy decisions unless they contribute. Sitkoff argued that the 1907 ban on corporate contributions was sought by corporations to prevent them from being "held up" by politicians.

Nuclear and Renewable Electricity Costs

- "The Private and Public Economics of Renewable Electricity Generation," by Severin Borenstein. December 2011. NBER #17695.
- "Prospects for Nuclear Power," by Lucas W. Davis. December 2011. NBER #17674.

These two papers provide readers with concise non-technical summaries of the costs of many of the non–fossil fuel sources of electricity. The levelized cost of electricity is defined as the price of electricity that equates the present value of plant costs with the present value of its output over the lifetime of the plant. Plant costs are usually known. The unknowns are fuel costs, interest rates, and outage rates. Even though they are widely used, levelized costs are misleading because they ignore the time-varying value of electricity and do not distinguish between generation that is dispatchable and generation that is not. For example, solar is more valuable than wind because solar's peak output coincides with peak demand in the afternoon while wind's peak output is at night in the winter, a time of low demand.

Subsidies to fossil fuels are not really that distortionary because they amount to only 0.11 cents per kWh even if environmentalists' high estimates are used. The levelized cost of residential solar panels is about 24 cents per kWh while natural gas combined-cycle generation is below 8 cents per kWh. Even taking local pollution into account, natural gas–fired electricity is at least 15.8 cents less expensive per kWh. Thus the appropriate charge for the externalities from natural gas carbon emissions would have to be at least $316 a ton for solar to be competitive. And remember that Nordhaus, above, calculates that the optimal charge for the emission of one ton of carbon dioxide is only $12.50. Thus subsidies to renewable generation technologies are not a cost-effective substitute for optimal carbon taxes that are not politically acceptable.

Nuclear power's primary challenge is also its cost. The French have the most nuclear intensive electricity generation system in the world. If any country were to reduce costs because of learning-by-doing, it would be France. But French costs have escalated over time from $1,000 per kW of capacity in the 1970s to $2,300 per kW in the 1990s. The plants currently under construction in Finland and France have also experienced cost increases. A Finish plant, begun in 2005, was supposed to cost $2,800 per kW and be finished in 2009. It will now not come online before 2015 and cost $5,600 per kW. A French plant was supposed to cost $2,900 per kW and is now 50 percent over that and completion has been delayed by three years. The current best estimates of levelized costs are 10.5 cents per kWh for nuclear, 7.4 cents per kWh for coal, and 5.2 cents per kWh for natural gas.