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FEDERAL PERMITTING IS BROKEN



Reform Should be Guided by Common Law Principles

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Executive Summary

This paper outlines critiques of the current federal permitting system. It analyzes the recent attempts at reform, discusses the American philosophy of governance to show the place of permitting within the broader scope of regulation, and explores the history of the regulation of three industries. We aim to provide a principled groundwork that can guide future examination of permitting reform.

This analysis begins with this overall presumption: Whenever possible, the private sector should not have to wait on the government in order to act. As will be demonstrated, this is the fundamental advantage of common law, which relies upon enforcement, over civil law, which relies upon permission. Common law principles yield both increased economic progress and better compliance with prevailing standards.

Criticisms of the Permitting Process

There is a growing bipartisan consensus that the federal permitting system is broken.² In the latest survey by the National Association of Manufacturers, more than 74% said

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² From the left: Rayan Sud, Sanjay Patnaik and Robert L. Glicksman, "How to Reform Federal Permitting to Accelerate Clean Energy Infrastructure: A nonpartisan Way Forward," Brookings, Feb. 14 2023. <https://www.brookings.edu/research/how-to-reform-federal-permitting-to-accelerate-clean-energy-infrastructure-a-nonpartisan-way-forward/>.

that simplifying and speeding up the federal approval process for new projects would help them hire more workers, expand their business, or increase wages and benefits.³ Even bedfellows as strange as the Fossil Fuel and Green Energy industries are both calling for reform.⁴

Critics argue that the federal permitting process is slow, expensive, opaque, arbitrary, corrupt, and contradictory:

Slow. The National Environmental Policy Act (NEPA), is the poster child for reform.⁵ Across all federal agencies, on average, an environmental impact statement (EIS) exceeds 600 pages in length⁶ and takes 4.5 years to produce.⁷ This average obscures the facts that large or complex projects take much longer, and that many projects just never occur because the uncertainty of time to permit makes financing difficult.

Permit delays are unseen killers of economic activity.⁸ Deferred economic activity is lost economic growth, making us all poorer in the future.

And the right: Mario Loyola, "Make Federal Red Tape Part of the Debt-Ceiling Fight," Competitive Enterprise Institute, May 2, 2023. https://cei.org/opeds_articles/make-federal-red-tape-part-of-the-debt-ceiling-fight/.

³ "2023 First Quarter Manufacturers' Outlook Survey," National Association of Manufacturers, March 31, 2023. [https://www.nam.org/2023-first-quarter-manufacturers-outlook-survey/#:~:text=Nearly%20three%2Dquarters%20of%20respondents,%25\)%20the%20next%20biggest%20impediments.](https://www.nam.org/2023-first-quarter-manufacturers-outlook-survey/#:~:text=Nearly%20three%2Dquarters%20of%20respondents,%25)%20the%20next%20biggest%20impediments.) .

⁴ "US Renewables Industry Joins Big Oil to Fight Delays to Project Permits," *Financial Times*, April 23, 2023. <https://www.ft.com/content/adf4d72c-9c7b-46a5-960f-70a700072721>.

⁵ Eli Dourado, "Bringing NEPA Back to Basics," The Center for Growth and Opportunity, March 28, 2023, 1. <https://www.thecgo.org/wp-content/uploads/2023/03/Bringing-NEPA-Back-to-Basics-v1.pdf>. Eli Dourado's analysis is excellent, making the case that the inefficiency in the NEPA process impedes "national goals."

⁶ "Length of Environmental Impact Statements (2013 - 2018) – NEPA," Council on Environmental Quality, June 12, 2020. https://ceq.doe.gov/docs/nepa-practice/CEQ_EIS_Length_Report_2020-6-12.pdf.

⁷ Ibid.

⁸ Cf. Frederic Bastiat, "Seen and Unseen," 1850. As seen below, Peter Aranson casts doubt on Cass Sunstein's view that governments can measure and so balance the competing values of economic rights. The knowledge problem is not so easily overcome. The opportunity costs of a system without clear rules governing economic rights are impossible to measure, but large. The dog that didn't bark turns out to be the essential clue. Peter H. Aranson, "The Common Law as Central Economic Planning," *Constitutional Political Economy*, 1992.

Expensive. The process is exorbitantly expensive for private parties in terms of the time and resources needed to interact with government officials to demonstrate compliance with substantive standards. At the conclusion of the process, projects are often given a set of mitigation measures they are compelled to comply with, which can drastically warp a project from its original design and dramatically drive up costs.⁹

Opaque. Permittees often don't know where they stand in the permitting review and approval process. It is not just the regulatory *burden, per se*, that is a cost. Worse is the regulatory *uncertainty* surrounding when approval will be granted, if at all, and under what conditions.¹⁰

Arbitrary. Permittees have come to learn that the process is often subject to bureaucratic discretion. And agencies sometimes require mitigations that are not lawful.¹¹ This taints public confidence in the objectivity and fairness of the system, giving the appearance of bias or corruption that may or may not exist.

Corrupt. There is also actual corruption. As Nobel Laureate George Stigler proved, regulatory bodies are often captive to the largest interests they regulate.¹² This creates a barrier to competition and innovation.

Contradictory. There are often confusing or conflicting requirements between different agencies—not merely between competing federal agencies, but, as discussed in the healthcare section below, in tussles between federal and state powers as well.

The Clean Air Act is an example of the federalism nexus, insofar as the federal government sets standards and then requires states to implement them. This creates a

⁹ Council on Environmental Quality, "Forty Most Asked Questions Concerning CEQ's National Environmental Policy Act Regulations," Dept. of Energy, March 16, 1981. <https://www.energy.gov/nepa/articles/forty-most-asked-questions-concerning-ceqs-national-environmental-policy-act>.

¹⁰ Jaime Pluene and Edward Boling, "This Permit Reform Already Works. Why Aren't More Mine Permit Applicants Using It?," University of Utah College of Law Research Paper, Environmental Law Report 53, no 10463 (March 22, 2023), 6. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4390921. "This project is notable because certainty and transparency are often cited by project proponents as the biggest barriers to financing."

¹¹ Adam White and Jace Lington, "You Report to Me' with David Bernhardt," C. Boyden Gray Center Gray Matters Podcast, May 10, 2023.

<https://administrativestate.gmu.edu/podcast/you-report-to-me-with-david-bernhardt/>

¹² George J. Stigler, "The Theory of Economic Regulation." *The Bell Journal of Economics and Management Science* 2, no. 1 (1971): 3-21.

<https://doi.org/10.2307/3003160>.

state-by-state regulatory market for certain kinds of projects. One CEO commented to one of the authors about his clean energy project: “Just be grateful that the State of Texas now has primacy on preconstruction air quality permits.”

One disadvantage of all this overlapping authority is the way it hinders accurate measurement of benefits and costs. There is a tendency for some agencies, the EPA especially, to justify imposing some new regulatory costs (considered in isolation) by counting the same benefits twice, benefits that were counted previously to justify some prior regulation. This is precisely the sort of thing that EPA accuses private companies of doing.¹³

To be clear, permitting reform is not about watering down the standards of compliance. It is about understanding how the process (in this case different from state to state) negatively affects the implementation of that standard, and broader economic growth.

Current Attempts at Reform

FAST-41. Pursuant to Title 41 of the Fixing America’s Surface Transportation Act, President Obama created the Federal Permitting Council to coordinate and streamline the permitting process in a half dozen industries; this process is called FAST-41. The duties of the Permitting Council have since been permanently funded and are slowly being expanded.¹⁴ President Biden signed the Infrastructure and Investment and Jobs Act and the Bipartisan Infrastructure Law in part to expand the authorities and obligations of the Permitting Council.¹⁵

The FAST-41 process is voluntary, both for permit applicants and the federal agencies who grant them. If the applicant’s project is in a covered area, the Permitting Council will assign a lead agency to shepherd the project through the application process. Agencies must decide early on whether they are in or out, and if in, commit to a time frame to finish their review. They also must provide more early information to

¹³ “Double Counting,” Environmental Protection Agency, Feb. 5, 2023. <https://www.epa.gov/green-power-markets/double-counting>. Without acknowledging the possibility that EPA itself could double-count, EPA warns about the perils of businesses fraudulently claiming more than their share of benefits from renewable energy.

¹⁴ Pleune and Boling, “This Permit Reform Already Works. Why Aren’t More Mine Permit Applicants Using It?,” 3.

¹⁵ “The Biden-Harris Permitting Action Plan To Rebuild America’s Infrastructure, Accelerate The Clean Energy Transition, Revitalize Communities, And Create Jobs,” The White House. <https://www.whitehouse.gov/wp-content/uploads/2022/05/Biden-Harris-Permitting-Action-Plan.pdf>

applicants, and keep them informed as to the status of their application on a public dashboard.¹⁶ This appears to help because it tends to prevent later surprises in the application process, and creates social pressure on agencies to stick to the schedule they committed to.

While the FAST-41 process has shown promise in reducing the burdens of the federal permitting process in a relatively limited universe of eligible projects, there will likely be diminishing rates of return on these improvements. Pluene and Boling, who tout the benefits of FAST-41, also provide evidence that this reform is, ultimately, politically unworkable as a template for the whole government.

On the one hand, they argue that the body of evidence shows there is no need to reduce the quality (i.e., complexity) of environmental reviews, because “reducing the rigor of environmental analysis did not always produce faster decisions.”¹⁷ On the other hand, their analysis leads them to conclude that the way to speed up the federal permitting process is, therefore, to increase the number of federal employees devoted to the process. Yet they acknowledge the recent political climate makes that solution untenable because neither major party appears to favor a dramatic increase in the number of employees devoted to federal permitting.¹⁸

This reality begs the question of whether incremental improvements, however worthy, are really the solution to reforming an antiquated process. New technology opens a host of possibilities to modernize the process that we will discuss in subsequent papers. It may well be that, without reducing (and even while increasing) the effectiveness of environmental standards, there are more effective ways to regulate the implementation of projects with potential environmental impact.

Before we can understand how to modernize the permit process more fundamentally, we should try to understand the permit process in the broader context of regulation and governance as a whole.

Fiscal Responsibility Act (FRA) of 2023. The highly contentious debt ceiling negotiations demonstrated significant bipartisan appetite for permitting reform—although many reforms did not make the final legislation. The most significant changes appear to be both a narrowing and a possible broadening of the triggers for NEPA

¹⁶ Pleune and Boling, "This Permit Reform Already Works. Why Aren't More Mine Permit Applicants Using It?," 3-5.

¹⁷ Pleune and Boling, "This Permit Reform Already Works. Why Aren't More Mine Permit Applicants Using It?," 22.

¹⁸ Pleune and Boling, "This Permit Reform Already Works. Why Aren't More Mine Permit Applicants Using It?," 25.

review. While expanding categorical exclusions from NEPA review (including projects that receive “no or minimal federal funding”) the legislation also changes the wording of the definition of the “major federal action” trigger.

The trigger for NEPA review has been whether a proposed activity is a “major federal action,” which has been defined as “effects that may be major and which are potentially subject to Federal control and responsibility.” But under the FRA, the new definition is “an action that the agency carrying out such action determines is subject to substantial Federal control and responsibility”—which new definition does not even contain the term “major.” How the federal agencies implement this revised approach (likely via regulations or guidance) is yet to be determined.¹⁹

Yet to be determined indeed. This vague language has the potential to cause a lot more harm than good.

Statutory deadlines have now codified what was previously in the federal regulations for the completion of Environmental Impact Statements (2 years) and Environmental Assessments (1 year). But this does not represent a substantial change from what the regulations already required. It will be interesting to watch whether this actually has an effect on the permitting backlog.

The legislation also allows energy storage projects to participate in the FAST-41 process.

While it is heartening to see Congress taking up this issue, it is not clear these changes will have a significant impact—and they may only serve to blunt for a time Congress’s desire to make further reforms.²⁰ Before this comes up again, we can hope for a more robust understanding of permitting in the overall context of regulation and governance to drive the debate.

The Underlying Cause: Our Philosophy of Governance

¹⁹ Jeff Thaler, “How Much Permitting “Reform” Comes from the New Debt Ceiling Legislation?,” JDSUPRA, June 9, 2023. <https://www.jdsupra.com/legalnews/how-much-permitting-reform-comes-from-2187479/>
<https://doi.org/https://www.jdsupra.com/legalnews/how-much-permitting-reform-comes-from-2187479/>.

²⁰ Dmitrios J. Karakitsos and Todd Wooten, “Permitting Reform Outlook, Based on Provisions from Debt Ceiling Compromise,” Holland & Knight Alert, June 5, 2023. <https://www.hklaw.com/en/insights/publications/2023/06/permitting-reform-outlook-based-on-provisions-from-debt-ceiling>.

We are all French now.

America is prosperous because it is governed differently. A common assumption is that natural resources are the source of our wealth. But there are so many examples of countries with more natural resources than we have that remain poor. Institutions matter. The philosophy that animates those institutions matters most.

What could it be about America that made the United States grow, in only two centuries, from a post-colonial backwater into the only superpower on the globe? Our once preeminent rate of growth was due in large part to our philosophy of governance.

If you spend much time in Africa, you will learn: There are two Africas. One Anglophone, one Francophone. In Anglophone Africa, everything is permitted, unless it is explicitly forbidden. In Francophone Africa, everything is forbidden, unless it is explicitly permitted. This is the difference between the common law and the civil law, including the Napoleonic Code.²¹

These two governance systems strike a different balance between central authority and the individual right to take action. French authority and English liberty proceed from different views of the human person and the body politic; the distinction can be described as centralism v. decentralism.²²

²¹ Magatte Wade and Steven Horwitz, "Regulation and the Perpetuation of Poverty in the US and Senegal," The Center for Growth and Opportunity, Dec. 13, 2021, 34. <https://www.thecgo.org/wp-content/uploads/2021/09/Regulation-16-pdf-1.pdf>. This perspective is confirmed by the personal experience of Magatte Wade in her co-authored book chapter:

“...the Senegalese legal system is inherited from a state-centric civil law nation in Europe, modified by 40 years of socialism and its associated cronyism and rent-seeking. It is very far from an optimal legal system for business and generating economic growth.”

²² Noga Morag-Levine’s position is consistent with Coase and Aranson, in that, all agree that a defining feature of the difference between the common law and civil law traditions is the decentralized character of the common law. Morag-Levine proposes the “...tension between these [common law] principles and a countervailing continental regulatory tradition” as a possible explanation of the “cross-national differences in the enthusiasm with which the concept of tradable pollution rights was embraced.” That is, because continental civil law countries culturally look for across-the-board Kantian solutions, while common law countries are comfortable with the idea of different standards in different places. Noga Morag-Levine, “The Problem of Pollution Hotspots: Pollution Markets, Coase, and Common Law,” *Cornell Journal of Law and Public* 17, no. 1 (Fall 2007) 170.

<https://scholarship.law.cornell.edu/cgi/viewcontent.cgi?article=1123&context=cjlpp>

In the French view, it makes perfect sense for Paris to tell Lyon how many street lamps it will have and where to put them. Authority (and thus direction) proceeds directly from the king.

The English view is very different. Authority to take action proceeds from the individual's right to govern himself. But liberty is only one side of the coin; responsibility is the other. The king's job is to correct subjects who abuse their liberty, but otherwise leave the individual to his own devices.

The contrast between these governing philosophies is dramatic when you look at its effects on economic growth and innovation.

In the United States, we inherited and improved upon the English common law view of individual rights. For example, the U.S. Constitution's patent protections are a fundamental improvement upon our mother country, where the king was presumed to own all invention.²³ It is not an accident that, as we surpassed our English teachers in extending common law property rights more fully, our economy eventually surpassed theirs as well.²⁴ As the pendulum of governance in the United States has swung from decentralized liberty toward centralized authority, our rate of growth and progress has dramatically slowed.²⁵

The contrast between common law decentralism and civil law centralism is a useful cipher for understanding how economic progress occurs. The authority for action dramatically affects the incentives to take action. The more we have to wait for permission to act, the less likely we are to produce.

Recent technology demonstrates that decentralization leads to incredible growth. The astonishing growth of the Internet, which has yet to experience significant regulation, has helped us all understand the power of decentralized activity. Examples like Wikipedia, AirBnB, and Uber seem commonplace phenomena now, but would have astounded almost anyone just a few decades ago. The largest Taxi company²⁶ owns no

²³ We are indebted to a conversation with Carl Schramm for this observation.

²⁴ Paul G. Mahoney, "The Common Law and Economic Growth: Hayek Might Be Right," *The Journal of Legal Studies* 30, no. 2 (2001): 503-525. <https://doi.org/https://www.journals.uchicago.edu/doi/10.1086/322053>.

²⁵ The center of gravity of power in America has marched along inexorably from the states to Washington, D.C. since the ratification of the 17th Amendment in 1913 gelded state power in Congress.

²⁶ The Business Research Company, "Uber Rides Unchallenged in The Top Spot of The Global Taxi," Global Newswire, Nov. 25, 2020. <https://www.globenewswire.com/news->

vehicles; the top vacation rental company owns no homes; and the most popular²⁷ and largest online encyclopedia site is built by contributions from volunteers all over the world. But perhaps this would not have astounded students of Ronald Coase.²⁸ Online marketplaces succeed by lowering transaction costs.²⁹

Even before the Coase theorem,³⁰ Coase's most enduring contribution was his description of the firm in a market economy—as a way to avoid high transaction costs between the actors required to produce a good, replacing them with more efficient administrative costs.³¹ So he could plausibly claim to have predicted that, as the Internet dramatically lowered transaction costs, we would see new firms emerge that relied on independent contractors to achieve what before had only been possible in large firms.

If we want to harness the power of decentralized economic action—from which we all benefit—we should make sure that our governance system, including the permitting process, does not stifle our natural economic dynamism.

What is permitting?

The noun, permit, really comes from the verb of the same name. Requiring a specific license to do something is one form that permission can take. Silence is another. When weighing this as a policy choice, we should consider the benefits as well as the costs we

[release/2020/11/25/2133871/0/en/Uber-Rides-Unchallenged-In-The-Top-Spot-Of-The-Global-Taxi-And-Limousine-Market.html](https://www.similarweb.com/top-websites/reference-materials/dictionaries-and-encyclopedias/).

²⁷ "Top Websites Ranking," Similarweb, June 1, 2023.

<https://www.similarweb.com/top-websites/reference-materials/dictionaries-and-encyclopedias/>.

²⁸ Upon Coase's death, Cass Sunstein referred to him as "The Most Important Economist You've Never Heard Of." Perhaps he would agree that Coase is the father of the Cost Benefit revolution (or if Reagan is the father, then Coase the grandfather). Cass R. Sunstein, "The Most Important Economist You've Never Heard Of," *Bloomberg*, Sept. 5, 2013. <https://www.bloomberg.com/opinion/articles/2013-09-05/the-most-important-economist-you-ve-never-heard-of#xj4y7vzkg..>

²⁹ Orly Lobel, "Coase and the Platform Economy," University of San Diego Law School, Research Paper No. 17-318, December 15, 2017.

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3083764.

³⁰ The Coase Theorem states that "in the face of market inefficiencies resulting from externalities, private citizens (or firms) are able to negotiate a mutually beneficial, socially desirable solution so long as there are no costs associated with the negotiation process." "The Coase Theorem," *Britannica*.

<https://www.britannica.com/topic/environmental-economics/The-Coase-theorem>.

³¹ Ronald H. Coase, "The nature of the firm (1937)." *The nature of the firm* (1991): 18-33.

have been occupied with above.³²

The benefits of issuing a written permit include: Promulgating a standard of compliance (which aids enforcement) and reducing regulatory uncertainty (which provides a safe harbor for action). And, as stated above, the costs of permitting include the time, expense, and uncertainty of the process.

The public policy question of deciding whether to issue written permits for a particular activity should be whether the costs of written permission are justified by the benefits. And we can refine or reform the process precisely in order to increase those benefits while reducing the costs.

We should also keep in mind that permitting is susceptible to the larger challenges of governance, which must overcome two related problems: Dirigism and Cronyism.

Dirigism is the tendency to intervene or command; it is susceptible to the knowledge problem—what is known by a single agent is only a small fraction of the sum total of knowledge held by all members of society.³³ Cronyism is a distortion of incentives that gives outsized influence to some parties over others (usually powerful incumbents against would-be competitors). These problems are especially astute because they feed off each other. Powerful incumbents are well situated to persuade regulators that established interests should be protected, and regulators are all too willing to believe they are wise enough to know how to intervene in the public interest.

Unfortunately, discussions amongst the most recognized authorities on regulatory process often ignore permitting.³⁴ David Bernhardt is an exception:

³² Coase argues that *all* benefits and costs should be compared among the four methods of regulating any given activity: The market, the firm, the regulator, or no regulation at all. Coase, R.H., “The Problem of Social Cost,” *The Journal of Law and Economics*, (1960): 3. <https://www.law.uchicago.edu/sites/default/files/file/coase-problem.pdf>

³³ Friedrich A. Hayek. “The use of knowledge in society.” *American Economic Review* 35, no. 4 (1945): 519-530.

³⁴ Susan E. Dudley and Jerry Brito, “Regulation: A Primer,” The Mercatus Center at George Mason University, 2012. <https://www.mercatus.org/research/books/regulation-primer>; Ludwig von Mises, “Bureaucracy,” New Haven Yale University Press, 1944, https://cdn.mises.org/Bureaucracy_3.pdf; James Q. Wilson, “Bureaucracy: What Government Agencies Do and Why they Do It,” 1989; Michael Crozier, “The Bureaucratic Phenomenon,” Vol. 280, Transaction Publishers, 2000; Cass Sunstein, “The Cost-Benefit Revolution,” MIT Press, 2018.

Congress and agencies could greatly improve the regulatory process by further promoting the development of general permits³⁵ or permits by rule.

“Congress or a thoughtful agency administrator should require agencies to develop public requirements for conditions that must be met if certain activities can proceed. The permittee can go forward upon committing to meet those conditions, and would be held accountable for acting in violation of the requirements.³⁶

Permit by rule and general rules are novel attempts to capture the benefits of written permission while minimizing the costs. Part of the public policy benefit of these approaches, especially permit by rule, is that they can aid in enforcement when violations are made. This shift toward devoting fewer resources toward granting individual permission while making enforcement more effective can mean that it takes far fewer resources to achieve the same public benefit. This is a good example of shifting back toward a common law posture as opposed to a Napoleonic one.³⁷

³⁵ Many jurisdictions have what is called a “general permit” to mean something more similar to PBR. For example, the EPA’s “general permit” requirements also provide pre-set defined standards. The applicant would only put the government on notice of its intent to begin a project, but the government would not have to grant the permit affirmatively. The project could commence after a sixty day waiting period after the government is put on notice. 40 CFR § 49.156(e). Often, because they are so similar, this form of “general permit” is used synonymously with PBR, despite the nuanced difference that a PBR requires a government action of permission, while the “general permit” is automatically permitted after an allotted amount of time. However, for the purposes of this paper, we are using a different term, “general rule,” to demonstrate the most purely common law form, that is, no government permitting process in any form. Only standard setting and *ex post* enforcement.

³⁶ David Bernhardt, *You Report to Me* (New York: Encounter Books, 2023), 164.

³⁷ The shift back toward using courts rather than rule makers to regulate economic activity would not be lost on Alexis de Tocqueville, the most celebrated student of American democracy (and its contrast with France). Tocqueville thought the American extension of the English jury trial to include civil matters was an essential improvement on the English system. Much is made of recent surveys showing that citizenship in the United States is less and less valued by Americans. Tocqueville would surely say this is because we have undermined our reliance on institutions of self-government *for teaching that citizenship* as we have moved toward governance by technocrats. “The jury, and above all the civil jury, serves to give to the minds of all citizens a part of the habits of mind of the judge; and these habits are precisely those that best prepare the people to be free.” Alexis de Tocqueville, *Democracy in America*, Mansfield translation, p. 262 (I.ii.8).

Illustrative Examples

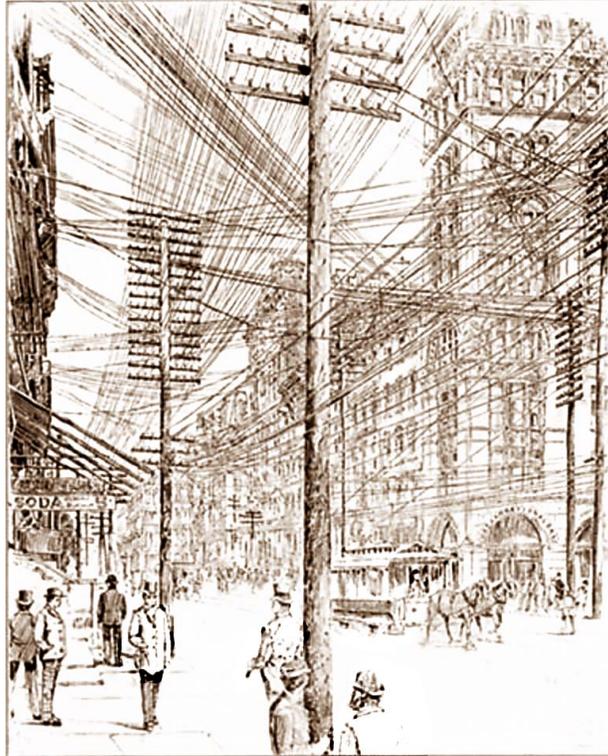
Selected elements from the history of regulation, specifically in three industries (Electricity, Healthcare, and Zoning) illustrate the implications of our philosophy of governance on regulation at the national, state, and local levels.

Electricity Regulation: From Local to Central (and back again?)

In 1879, Thomas Edison opened the first electric company in lower Manhattan. His prototype foreshadowed what would become standard for almost a century: A single company owning the power plants, transmission, and distribution (this ownership of multiple stages of a supply chain became known as “vertical integration”).³⁸ Electric power quickly went from a novelty luxury to an essential part of commercial, domestic, and industrial life.

Innovation in technology and in business models brought the industry up from intense hyper-local overlapping competition to consolidation and centralization. Initially, direct current transmission dictated that power plants operate very close (within a mile) of the ultimate use for the juice.

³⁸ Maryssa Barron, "U.S. Energy Markets 101: How Electricity Markets Work," LevelTen Energy, Oct. 10, 2019. <https://www.leveltenenergy.com/post/energy-markets-101>.



Technological change allowing efficiency gains from economies of scale drove the growth of vertical integration.³⁹ Samuel Insoll in Chicago pushed for the adoption of alternating current and managed to buy up many small competitors, turning their power plants into his substations. He argued that the electricity industry should be regarded as a natural monopoly. Naturally enough, as a shrewd businessman who had also innovated the use of dynamic pricing at peak demand, he wanted to be the monopolist.

In the early 1900s, states began to govern emerging utility monopolies.⁴⁰ In 1907, Wisconsin created a state commission with powers to restrict entry into the electricity market by requiring a “certificate of public convenience and necessity.” This law became a model for other states to follow.⁴¹ By 1914, forty-three states regulated electricity.⁴² Federal regulation came into play when grids crossed state lines.⁴³ For the majority of the twentieth century, the electric power sector was dominated by vertically integrated

³⁹ "Vertically Integrated Utility," Harvard Electricity Policy Group. <https://hepg.hks.harvard.edu/faq/vertically-integrated-utility>.

⁴⁰ "Regulation - Public Vs. Private Power," PBS. <https://www.pbs.org/wgbh/pages/frontline/shows/blackout/regulation/timeline.html>.

⁴¹ R. Richard Geddes, "A historical perspective on electric utility regulation," *Regulation* 15 (1992): 75.

⁴² "Emergence of Electrical Utilities in America," Smithsonian. <https://americanhistory.si.edu/powering/past/h1main.htm>.

⁴³ "The History and Evolution of the U.S. Electricity Industry," University of Texas at Austin. https://energy.utexas.edu/sites/default/files/UTAustin_FCe_History_2016.pdf.

companies that were state-regulated by public utility commissions.⁴⁴ Electric providers enjoyed exclusive geographic franchises in exchange for submission to government regulation. However, standards emerged from the free association of practitioners rather than from legislation or bureaucracy.

The North American Electric Reliability Corporation (NERC), a nonprofit, emerged through voluntary coordination across all regions (initially just in the US, then expanding to include parts of Canada and Mexico) to share information and create standards for best practices and interoperability. Only decades later did Congress recognize its desire to regulate these standards, creating the designation of an electricity reliability organization (ERO).⁴⁵

In the 1990s, deregulation began with a series of federal actions, and then laws passed by America's largest states, forcing competition. We now have vertically integrated monopolies regulated by state public utility commissions, as well as somewhat less regulated markets where electric energy prices are set by the market, with some federal oversight of wholesale market operations. The results of this unfolding process appear to be a mixed bag, with critics of deregulation pointing to higher rates in the states that imposed deregulation.⁴⁶ There may be such thing as “deregulatory capture” where the process of reform is weaponized by entrenched industry interests to support their position in the market.⁴⁷

Texas exceptionalism in particular comes under fire with bad press from the system fragility exposed by the deep freeze of February 2021, costing Texans some 130 billion dollars in damages, which might have been mitigated by better risk management including winterization and converted energy storage.⁴⁸ Self-sufficiency is a relatable

⁴⁴ "Electricity Industry Structure and Regulation," Pennsylvania State University. <https://www.e-education.psu.edu/eme801/node/529>.

⁴⁵ The following is a good official inside story of the organization. David Nevius, "The History of the North American Electric Reliability Corporation," North American Electric Reliability Corporation, 2020. <https://www.nerc.com/AboutNERC/Resource%20Documents/NERCHistoryBook.pdf>

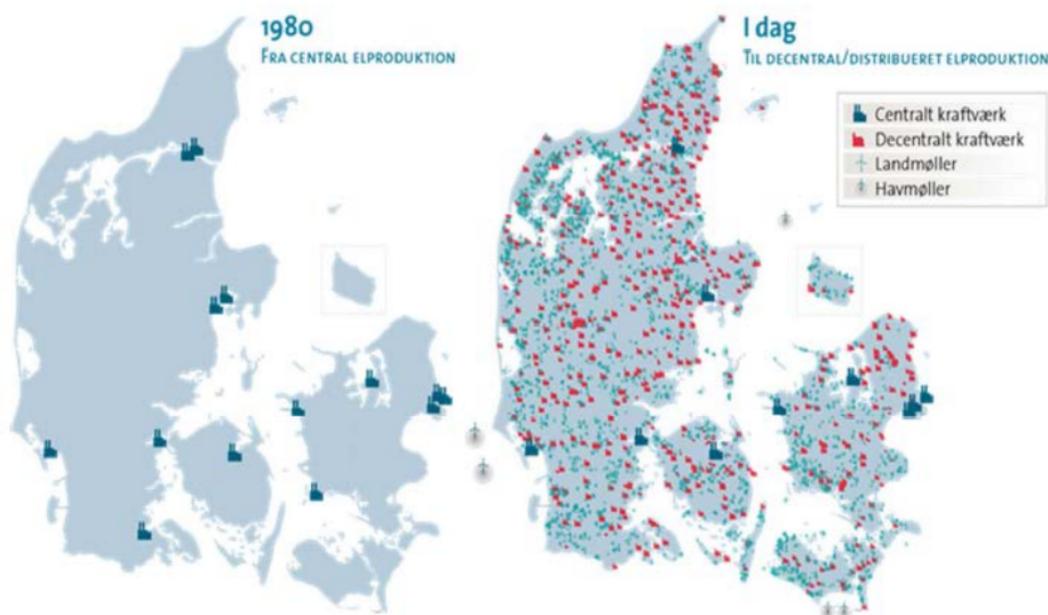
⁴⁶ Tyson Slocum, "The failure of electricity deregulation: history, status and needed reforms," FTC.gov, 2007. https://www.ftc.gov/sites/default/files/documents/public_events/Energy%20Markets%20in%20the%2021st%20Century:%20Competition%20Policy%20in%20Perspective/slocum_dereg.pdf.

⁴⁷ Jan Whittington, "The Making of California's Energy Crisis." *Berkeley Planning Journal*, 16, no. 1(2002).

⁴⁸ Becky L. Jacobs, "Professor Commentary: Failing to Learn from the Texas Power Crisis, (or, the Paradox of an Unreliable Electric Reliability Council and a " Public Utility Commission" in a Largely Unregulated Market)." *Transactions: The Tennessee Journal*

and laudable political sentiment, which needs translation into actual preparation by assigning appropriate accountability. Decentralized power requires decentralized responsibility.

Looking ahead to the transition to clean energy, the future of the electric grid may lie in its past. Decentralization may go hand in hand with economically sustainable power. For example, Denmark leads the world in distributed energy generation with wind power and combined heat and power (CHP).⁴⁹ This map shows the stark contrast between the number of power stations in 1980 and the number of windmills today:⁵⁰



“The Danish power system. Dominated by central power stations in the 1980s and today changed into a decentralised power system with large amount of wind power.”⁵¹

The U.S. would benefit from a decentralized and localized energy grid, if it were permitted. The technology exists. Microgrids by neighborhood could provide their own power supply, but are generally illegal in the highly regulated U.S. electricity industry.⁵²

of Business Law 23, no. 3 (2022): 8.

<https://ir.law.utk.edu/cgi/viewcontent.cgi?article=1613&context=transactions>.

⁴⁹ Erik van der Vleuten and Rob Raven, "Lock-in and change: Distributed generation in Denmark in a long-term perspective," *Energy Policy* 34, no. 18 (2006): 3739-3748.

<https://www.sciencedirect.com/science/article/abs/pii/S030142150500220X>.

⁵⁰ "Integration of Wind Energy in Power Systems," Danish Energy Agency, May 2017, 9. https://ens.dk/sites/ens.dk/files/Globalcooperation/integration_of_wind_energy_in_power_systems.pdf.

⁵¹ *Ibid.*

⁵² Bill Nussey, "Microgrid powered neighborhoods are a real thing – how can we get more of them?," *FreeingEnergy*, Aug. 2, 2018.

Healthcare at the State Level: CON and COPA

The United States spends significantly more on healthcare compared to other nations, but without better healthcare outcomes. In 2021, U.S. healthcare spending reached \$4.3 trillion (on average about \$12,900 per person). The average cost of healthcare per person in other wealthy countries is only about half as much.⁵³ Despite this high spending, life expectancy in the U.S. lags behind that of its peer countries.⁵⁴ The U.S. has among the highest number of hospitalizations from preventable causes and the highest rate of avoidable deaths compared to peer nations.⁵⁵ Healthcare is also arguably the most heavily government-regulated industry.⁵⁶ Providers and organizations must follow many regulations developed and enforced at the federal, state, and local levels.⁵⁷

For the purposes of illustrating a problem of federalism working itself out, we select a complementary or perhaps competing pair of policies within the healthcare industry: CON and COPA.

What are CON laws?

Certificate-of-need (CON) laws are state regulation of major capital expenditures and projects for healthcare (e.g., hospitals). These laws require healthcare providers to get permission from the state before they offer new services, expand their facilities, or purchase new equipment. And who do state regulators tend to consult about the hospital business? Naturally, the executives of incumbent hospitals. But how can those executives be disinterested when answering whether there is a need for them to have more competition? Industry leaders may pretend to know the answer to what is “needed” but can at best give a guess from their own limited perspective. The end result

<https://www.freeingenergy.com/microgrid-powered-neighborhoods-are-a-real-thing-how-can-we-get-more-of-them/>.

⁵³ "Why Are Americans Paying More for Healthcare?," Peter G. Peterson Foundation, Jan. 30, 2023. <https://www.pgpf.org/blog/2023/01/why-are-americans-paying-more-for-healthcare>.

⁵⁴ "Charted: The countries with the most expensive healthcare," World Economic Forum, Feb. 9, 2023. <https://www.weforum.org/agenda/2023/02/charted-countries-most-expensive-healthcare-spending>.

⁵⁵ Roosa Tikkanen and Melinda K. Abrams, "U.S. Health Care from a Global Perspective, 2019: Higher Spending, Worse Outcomes?," The Commonwealth Fund. <https://www.commonwealthfund.org/publications/issue-briefs/2020/jan/us-health-care-global-perspective-2019>.

⁵⁶ Ephrat Livni, "Regulation Nation: What Industries Are Most Carefully Overseen?," FindLaw. <https://www.findlaw.com/legalblogs/small-business/regulation-nation-what-industries-are-most-carefully-overseen/>

⁵⁷ Robert I. Field, "Why Is Health Care Regulation So Complex?," National Library of Medicine, Oct. 2008. <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC2730786/>.

has been the opposite of their supposed policy intent: CON reduces access, increases prices, and lowers quality.⁵⁸

Origin of CON

New York State first passed a CON law restricting new hospital construction in 1964, and then the American Hospital Association lobbied other states to adopt CON regimes.⁵⁹ In 1974, Congress mandated all states to establish a CON program.⁶⁰ By 1980, every state except Louisiana had a CON law on the books.⁶¹

CON raises prices and reduces the quality of healthcare:

- CON limits the supply of healthcare services, leading to higher prices for patients.
- CON bars entry for new providers, making it difficult for them to enter the market and compete with established providers.⁶²
- CON inhibits innovation by preventing providers from investing in new technologies or expanding their services.^{63,64}

‘Stickiness’ of CON

Congress repealed its CON mandate in 1986.⁶⁵ Some states did so as well—and without suffering a big cost increase in healthcare. Even though there is a bi-partisan consensus of experts that CON is counterproductive,⁶⁶ many states still maintain active CON

⁵⁸ Matthew D. Mitchell, "Certificate-of-Need Laws: How They Affect Healthcare Access, Quality, and Cost," Mercatus Center, May 21, 2021. <https://www.mercatus.org/economic-insights/features/certificate-need-laws-how-they-affect-healthcare-access-quality-and-cost>.

⁵⁹Maureen K. Ohlhausen, "Certificate of Need Laws: A Prescription for Higher Costs," *Antitrust*, 30, No. 1 (Fall 2015): 51. https://www.ftc.gov/system/files/documents/public_statements/896453/1512fall15-ohlhausenc.pdf

⁶⁰ *National Health Planning and Resources Development Act*, Public Law 88, U.S. Statutes at Large 2225 (1975), 2225-2276.

⁶¹ "Improving Health Care: A Dose of Competition," Department of Justice, July 2004, ch. 8, 2. <https://www.ftc.gov/sites/default/files/documents/reports/improving-health-care-dose-competition-report-federal-trade-commission-and-department-justice/040723healthcarerpt.pdf>

⁶² "Certificate-of-need laws: Why they exist and who they hurt," State Policy Network, April 1, 2021. <https://spn.org/articles/certificate-of-need-laws/>.

⁶³ "Certificate of Need Regulations: Mixed Evidence for Cost Containment," Easy explainer, No. 3, July 2015. <https://www.healthcarevaluehub.org/advocate-resources/publications/certificate-need-regulations-mixed-evidence-cost-containment>.

⁶⁴ Ohlhausen, "Certificate of Need Laws."

⁶⁵ Pub. L. 93-641, 88 Stat. 2225 (1975).

⁶⁶ Ohlhausen, "Certificate of Need Laws."

regimes.⁶⁷ This appears to be an instance of the ratchet effect, where new government programs are born but do not die instead outliving their original intent and purpose,⁶⁸ in part because of regulatory capture. Regulators are said to be “captured” by the industry they regulate when they serve its interests over that of their mandate by law.⁶⁹ CON serves up concentrated benefits to a specific interest group, with unseen costs distributed across the whole population of sick people and their families, who pay higher prices, travel further, and suffer a lower standard of care.

COPA

Certificate of Public Advantage (COPA), in contrast, is an attempt made by individual states to create a shield of protection against federal antitrust oversight by the FTC for healthcare mergers (e.g., combining hospitals) deemed by the state to be in the best interests of their citizens.⁷⁰ While CON discourages new entrants, COPA removes barriers to consolidation. The fact that these seemingly contradictory policies are both favored by incumbent hospitals is a telling indicator of regulatory capture.

In this paper we take no position on the merits of antitrust regulation or the appropriate level and process for its enforcement. It suffices to note the difficulty when state governments come to different conclusions than the national agencies about what is for the best. Proponents of federal antitrust law argue that the local state can be too easily subject to regulatory capture. In any case, one regulator suing another certainly creates regulatory uncertainty that can only have a chilling effect on both new competition and economies of scale.

The Healthcare Lesson

Although CON and COPA are only two small parts of the vast patchwork of regulations around healthcare, they do serve us here as illustrations of difficulties in permitting. The harmful effects of a federal mandate can remain ‘sticky,’ lasting at the state level long

⁶⁷ Jordan A. Zoeller, Matthew J. Muller, and Nicholas J. Janiga, "Understanding the Value of a Certificate of Need," *Business Valuation*, Jan. 29, 2020.

<https://healthcareappraisers.com/understanding-the-value-of-a-certificate-of-need/>.

⁶⁸ For a good recent discussion of this theory, see the following: Christopher J. Coyne, Abigail R. Hall, and Matthew Owens, "The Ratchet Effect," *GMU Working Paper in Economics*, June 13, 2022. <https://ssrn.com/abstract=4135816>.

⁶⁹ Michael J. Boyle, "Regulatory Capture Definition with Examples," *Investopedia.com*, March 1, 2021. <https://www.investopedia.com/terms/r/regulatory-capture.asp>.

⁷⁰ Randall R. Bovbjerg and Robert A. Berenson, "Certificates of Public Advantage," *Urban Institute*, Feb. 2015. <https://www.urban.org/sites/default/files/publication/42226/2000111-Certificates-of-Public-Advantage.pdf>.

after the repeal of the mandate. Simply decentralizing down from Congress and leaving it to the states to decide is no guarantee of a fair and efficient outcome.

Somewhat like driving with your foot on both the brake and gas pedal, some states even have both CON and COPA,⁷¹ trying to reduce free entry on the one hand but empower the existing actors to merge to save costs on the other hand. From a protectionist perspective of regulatory capture by the established players, this is utterly unsurprising: These policies seem to be opposites but are both exactly aligned with the interests of the large incumbents against those of their potential competitors and, ultimately, consumers.

Zoning

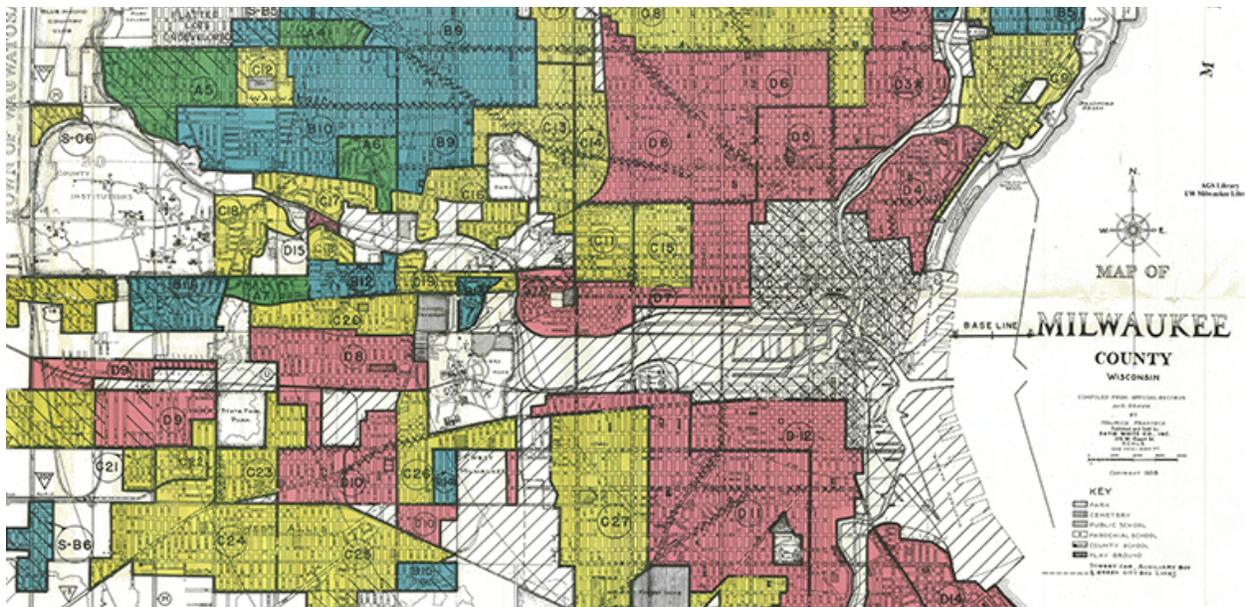
Americans have been particularly susceptible to the assumption that the only alternatives in land use regulation are zoning or chaos. As the United States went from zero to nearly all cities adopting zoning in less than a century, Americans have come to assume this is the only way things can be. We remain ignorant that the rest of the world doesn't do this, and that there is one major city here—Houston—that doesn't do it either. And yet these unzoned places are not in chaos.

M. Nolan Gray has ably sketched the history of zoning in the United States as beginning with a “Bootleggers and Baptists” coalition of wealthy property owners with racists who wanted, on the one hand, to protect their property values from competition, and on the other, to keep undesirable populations away. The resulting zoning policy, developed first in 1916 in New York City and then in Berkeley, was foisted on the rest of the country by aggressive promotion by the federal government, which conditioned housing subsidies on the implementation of zoning.⁷²

The salient point for our analysis of regulation and permitting is that, while zoning laws have deleterious effects (driving up the price of housing to unaffordable levels for those of modest incomes) they do not, in the end, really change how cities organize themselves spontaneously.

⁷¹ Amy Y. Gu, "Updated: States with Certificate of Public Advantage (COPA) Laws," The Source, Aug. 10, 2021. <https://sourceonhealthcare.org/updated-states-with-certificate-of-public-advantage-copa-laws/>.

⁷² M. Nolan Gray. *Arbitrary Lines: How Zoning Broke the American City, and How to Fix It*. (Washington, D.C.: Island Press, 2022).



Urban planner Alain Bertaud’s compelling argument is that cities organize themselves by natural market forces. Densities are set by companies bidding up the price of land in central cities in order to gain preferential access to the largest possible labor market.⁷³ This is why cities (whether they have zoning or not) have similar patterns of development, with densities highest in the central city and getting lower in rings outward, with exceptions for subdistricts organized around employment (in Houston, these smaller “downtowns” include the Texas Medical Center and Uptown, which anchors the Energy Corridor).

Another important lesson that zoning teaches us is that local government control (certainly more decentralized than federal control) is not enough by itself to guarantee a healthy enough level of the economic freedom that would be effective at addressing problems like affordable housing. Local bureaucrats are just as susceptible as national ones to be persuaded that they should tell the rest of us what to do—as long as they are doing what powerful cronies want them to do.

The final lesson we will consider gives its due to the only major U.S. city that is a holdout from zoning—Houston. Repeated ballot initiatives supported by wealthy residents to adopt zoning have been rejected by voters of modest means.⁷⁴ And yet Houston is an especially vibrant city with extraordinary economic opportunity (and is the most cosmopolitan city in the United States, with more large immigrant communities than any other).

⁷³ Alain Bertaud, *Order without Design: How Markets Shape Cities*, (Cambridge, MA: MIT Press, 2018).

⁷⁴ Gray, *Altered Lines*, chapter 9.



“The same block of Midtown in 2010 and 2020. Thanks to Houston’s lack of zoning, densities can rapidly increase in response to surging demand for urban living. (Google Maps)”⁷⁵

Houston has a private alternative to zoning, called restrictive covenants or Deed Restrictions. There is one fundamental difference between zoning and Deed Restrictions:

Zoning is an effort of some property owners to tell other property owners what they may or may not do with their property. But Deed Restrictions⁷⁶ are covenants (written agreements) that a property owner accepts voluntarily *in order to buy* property in the first place. In other words, prospective property owners band together to govern themselves, agreeing to limits on the use of their land in exchange for knowing others will follow the same rules. Whereas in zoning, incumbent property owners seek to impose restrictions upon others through government.

The moral difference between these two governance gambits for land use regulation explains why the latter avoids the deleterious effects of the former. Effective governance, and effective property rights, are those that give a voice and vote to those stakeholders who should have a voice and vote. But not the ability to impose their will on others.

Conclusion

While there is a broad consensus that the federal permitting process is broken, there is little acknowledgment that the broken process raises questions about the governing philosophy that should animate the administrative state. That is the goal of this paper.

We have argued that the once-preeminent economic dynamism of the United States was due in large part to our improvement upon the English common law system: We once governed with a posture of liberty that allowed citizens to act without waiting on the

⁷⁵ Gray, *Altered Press*, 153.

⁷⁶ "About Deed Restrictions," City of Houston.

https://www.houstontx.gov/planning/Neighborhood/deed_restr.html.

government, and then corrected them after the fact if they failed to meet their obligations. This empowered decentralized action and dramatic economic growth, from which we and the whole world have benefitted.

In the last century, we have come unmoored from our common law roots, and taken a Napoleonic turn toward a civil law posture of requiring permission in advance of taking action. This administrative posture slows economic growth, and often does not do a better job of enforcing compliance with environmental or other standards.

The goal of permitting reform should be to improve compliance with standards without stifling the economic dynamism that makes us all better off.

That requires improving governance. The touchstone of good governance is making sure that the voice and vote—the property rights—of all those with legitimate interests are protected. In the case of permitting, it is important to minimize the costs of issuing permits while maximizing their benefits.

This suggests a return to the traditional common law posture of American governance (even while making use of new technologies). We should promulgate clear rules and allow industry standards to emerge naturally through enforcement in courts and private cooperation, rather than by empowering a bureaucracy that will always be prone to dirigism and cronyism. We should enforce those rules when necessary. But not *before* it is necessary.

The current state of things is not set in stone. There is an unfortunate human tendency to assume that the *status quo* was somehow inevitable.

Good governance comes in different sizes and shapes. We need not look for a single cookie-cutter solution either in the broader effort to modernize governance, or the narrower effort to reform the permitting process.

In future papers, we will examine the reality that procedural reforms can improve standards and lead to better social outcomes, outline alternative methods of regulation, and consider especially, as particularly ripe for common law enforcement, permits by rule and general permits.