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0521860415 - The Voluntary Environmentalists: Green Clubs, ISO 14001, and Voluntary Regulations

Aseem Prakash and Matthew Potoski

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The Voluntary Environmentalists

Can businesses voluntarily adopt progressive environmental policies? Most environmental regulations are based on the assumption that the pursuit of profit leads firms to pollute the environment, and therefore governments must impose mandatory regulations. However, new instruments such as voluntary programs are increasingly important. Drawing on the economic theory of club goods, this book offers a theoretical account of voluntary environmental programs by identifying the institutional features that influence conditions under which programs can be effective. By linking program efficacy to club design, it focuses attention on collective-action challenges faced by green clubs. Several analytic techniques are used to investigate the adoption and efficacy of ISO 14001, the most widely recognized voluntary environmental program in the world. These analyses show that, while the value of ISO 14001's brand reputation varies across policy and economic contexts, on average ISO 14001 members pollute less and comply better with governmental regulations.

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To Alexander and Nives – Aseem

To Ben and Alicia – Matt

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Preface

This book examines how voluntary regulatory programs can mitigate collective-action problems. Drawing on club theory, we present a theoretical perspective to help scholars and policy-makers to think systematically about the challenges and opportunities of voluntary regulation. While the book focuses on voluntary environmental regulation, our approach is sufficiently general to be applicable to voluntary regulatory programs in other issue areas.

The assumption underlying most environmental regulation in the world today is that the pursuit of profit leads firms to pollute the environment. The standard prescription for mitigating pollution's harms has been for governments to enact regulations that *command* firms to meet specific pollution targets and *control* how firms do it, such as by prescribing specific pollution-control technologies for firms' production processes. While command and control regulations have had undeniable successes in reducing pollution, they have been criticized for being inefficient because they do not discriminate between costly and cheap pollution control. Budgetary pressures have curtailed governments' monitoring and enforcement programs and thereby undermined their efficacy. In light of such criticisms, several new policy instruments have been offered to complement command and control regulations. We firmly believe that the command and control system should continue to serve as the backbone of environmental governance. The challenge is to find new policy tools that can preserve its virtues and yet mitigate its negatives. One such tool, voluntary environmental programs, or "green clubs" as we term them, looks to improve firms' environmental performance by having firms voluntarily adopt an environmentally progressive code of conduct.

At first glance, voluntary programs may seem hopelessly naïve, if the assumption that profit maximization inevitably leads firms to externalize costs has any merit. While many voluntary programs are in operation around the world today, research provides no clear

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answer about the overall efficacy of these programs. Some studies suggest that one particular voluntary program improves participating firms' environmental behavior beyond what they would have done in the absence of the program, while studies of other programs have failed to find evidence of improved environmental performance among participants. We believe that the core theoretical challenge in voluntary program research is to identify what distinguishes the effective voluntary programs from the ineffective.

The book takes up the challenge of developing a theoretical account of voluntary environmental programs by identifying the core institutional features that distinguish effective programs from failures. Our theoretical framework draws on the economic theory of club goods (Buchanan, 1965; Cornes and Sandler, 1996). A club provides members with shared, group benefits from which non-members are excluded. Voluntary programs are like clubs in that they offer an excludable benefit that firms receive from their stakeholders because participation in the program signals that the firm is taking progressive environmental action. Because club membership creates benefits for firms by enhancing their standing with stakeholders, clubs can require member firms to incur the costs that stem from taking progressive environmental action. While command and control regulations seek to persuade firms to adopt such policies via the stick of mandatory enforcement, green clubs seek to do so via the carrot of enhancing firms' reputation through their membership in the club.

However, participating firms may have incentives to free-ride and enjoy the goodwill benefits of affiliating with the club's brand without paying the costs of adhering to its club requirements. That is, once they have joined the club, members may shirk their responsibilities and not perform according to the club's code of conduct. Effective clubs therefore need mechanisms to monitor and enforce their rules.

If voluntary programs function as clubs in the sense we described, two central questions emerge for studying these programs:

- Why do some firms join green clubs and not others? What enhances a club's brand reputation and how does this reputation induce firms to join the club?
- Does joining the club change participating firms' environmental and regulatory performances? After all, green clubs are useful tools to

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the extent they can induce firms to reduce their harm to the environment and show better compliance with public law.

We empirically examine our theoretical ideas about voluntary programs by analyzing ISO 14001, the most widely recognized voluntary environmental program in the world today. Our analyses show that the value of ISO 14001's brand reputation, and therefore its attractiveness to firms, varies across the policy and economic contexts in which firms operate. Our analyses also indicate that, at least in the US, joining ISO 14001 reduces the amount of time member firms spend out of compliance with government regulations and reduces the amount of toxic pollutants they release into the atmosphere. In other words, ISO 14001 induces firms to pollute less and better comply with governmental regulations.

The book makes three key contributions:

- It outlines an accessible yet robust theoretical framework for studying voluntary programs. We present a new theory, firmly grounded in the rational behavior of firms and their stakeholders, which can help account for the different research findings on the efficacy of voluntary environmental programs. This is an important contribution because the study of voluntary programs, while still in its infancy, is growing rapidly in many disciplines, including management, public policy, economics, political science, law, and sociology. Indeed, while we focus on environmental programs, our theory is sufficiently generalizable to apply to many other policy areas in which voluntary programs have been emerging.
- This book employs sophisticated quantitative tools to examine fundamental questions about voluntary programs. We supplement our quantitative analyses with short case studies of ISO 14001 adoption in the US and UK, and evidence from interviews with government regulatory officials and industrial managers.
- Most social science disciplines have become increasingly divided between scholars studying "domestic" issues and those studying "international" issues. This is one of the few texts that bridge the domestic–international divide by examining both the international and domestic (US) dimensions of ISO 14001's diffusion and efficacy.

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We began working on this project in August 2001. We initially worked on papers that helped us to think carefully about important issues in voluntary programs and focus our thoughts into a more coherent research program. In 2004, we embarked on a book project that would pull together our work, refine our theoretical approach to studying voluntary programs, and therefore present a theoretically compelling statement on voluntary program research.

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2. Covenant with Weak Swords: ISO 14001 and Firms' Environmental Performance. *Journal of Policy Analysis and Management*, 2005, 24(4); with permission from Wiley Interscience.
3. Regulatory Convergence in Non-Governmental Regimes? An Empirical Examination of Cross-National Adoption of ISO 14001. *Journal of Politics*, 2004, 66(3): 885–905; with permission from Blackwell Publishing.
4. The Regulation Dilemma: Cooperation and Conflict in Environmental Governance. *Public Administration Review*, 2004, 64(2): 137–148; with permission from Blackwell Publishing.
5. Policy Modes, Business, and the Natural Environment. *Business Strategy and the Environment*, 2004, 13(2): 107–128; with permission from Wiley Interscience.
6. EMS-Based Environmental Regimes as Club Goods: Examining Variations in Firm-level Adoption of ISO 14001 and EMAS in UK, US, and Germany. *Policy Sciences*, 2002, 35(1): 43–67; with permission from Springer.

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