



Kiron, David. "Overview Essay: Economics and the Good, III: Society," Part VII, Frontier Issues in Economic Thought, Volume 3: Human Well-Being and Economic Goals. Island Press: Washington, D.C. 1997. pp.239-248.

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### **“Economics and the Good, III: Society” by David Kiron**

Finding out what should be done is no less important than estimating what will happen. Hence, normative economics is no less important than positive economics. But the normative side of academic economics is nowadays heavily handicapped by its still being dominated by an outlook that is logically untenable...the utilitarian one.

- Serge-Christophe Kolm<sup>1</sup>

For over a century, mainstream economic theorists have deferred to the philosophy of utilitarianism. Today, however, utilitarianism finds little support among political philosophers. During the past three decades critics of utilitarianism have increasingly objected to its core idea that the goal of a moral society should be to maximize utility. A central focus for their objections is that utilitarianism is ill-equipped to address matters of justice. Although these problems have been well-known, it was not until 1971, when political philosopher John Rawls proposed a modern alternative to utilitarian moral theory, that these objections were considered by many to be decisive.

Rawls's work opened the way for other alternative conceptions of justice, which together challenged utilitarian hegemony within political philosophy. Collectively, these alternative theories of justice helped kindle an interdisciplinary debate on how to reconcile social goals such as equality, freedom, and rights with the economic goals of efficiency and wealth maximization.

This essay discusses the intersection of economic and social goals. It begins with a look at philosophical challenges to utilitarianism and moves to responses by selected economists. Next, the discussion focuses on the alleged trade-offs between efficiency and equity. It ends with a review of a significant recent debate within political philosophy -- whether the design of social institutions should start from a clear definition of what makes for good living or from a conception of individuals that secures the rights of all.

### **THE RAWLSIAN CHALLENGE TO UTILITARIANISM**

Until the 1971 publication of Rawls's *A Theory of Justice*, economists who had developed their skills during and after the ordinalist revolution (see Part 3) tended to neglect issues of distributive justice. For Rawls, a just society does not aim at a specific ideal of human good. Rather, its goal is to provide an institutional framework that embodies a set of basic freedoms and rights that allow individuals to pursue their diverse plans and objectives. To achieve this, he

proposed that the design of social institutions should be based on two principles of justice. The first principle, commonly referred to as “equal liberty,” states that each person is to have an equal right to the most extensive basic liberty compatible with a similar liberty for others. This principle is intended to guarantee that the rights of the few will never be sacrificed for the good of the many; as Rawls notes, this is a guarantee that is not secure within utilitarian doctrine.

Rawls’s second principle of justice, called “fair equality of opportunity,” states that social and economic inequalities are to be arranged so that they are both (a) reasonably expected to be to everyone’s advantage, and (b) attached to positions and offices open to all. This principle requires that distributions maximize the benefit of the least advantaged members of society -- the so-called maximin rule. This view, however, assumes what was denied by the ordinalists: the possibility of interpersonal comparisons.

Rawls defended his two principles of justice with a thought experiment that has garnered almost as much attention as the principles themselves. He claims that these are the principles that would be chosen in a hypothetical situation by rational, self-interested, free, and equal representative agents who, though ignorant of their own particular circumstances in society, are fully informed about the framework in which the society operates. Because their decisions will have ramifications over their entire lives, these representatives will be very risk averse, and will choose principles of justice that will ensure for them the highest possible quality of life even if they find themselves in the worst circumstances their society has to offer. This argument builds on a tradition of social contract thought, represented by John Locke and Immanuel Kant, and is therefore referred to as a contractualist theory.

Rawls presents his theory of “justice as fairness” as an alternative to utilitarianism, which he contends permits morally unacceptable trade-offs between liberty and welfare. His first principle of justice denies any moral justification for such trade-offs. He also argues that utilitarianism does not take seriously “the separateness of persons” when it treats the contribution of each person’s wellbeing as only a means to achieving the social optimum.

Another of Rawls’s objections to utilitarianism is that it implies that if an individual can give up all her preferences in order to have a different set that would create more utility, she ought to do so. Individuals are thus seen as “bare persons” without allegiance to their values and goals, except insofar as these promote their own utility. Consequently, utilitarianism slights an individual’s moral personality.

In Rawls’s theory, a moral personality consists of two moral powers -- a capacity for a sense of justice, and a rational power to organize and revise one’s plan of life in a social context. In order to develop and exercise these moral powers, every individual requires a number of primary social goods, which include basic liberties, rights, income and wealth, access to office, and the social bases of self-respect. Interpersonal comparisons of wellbeing are based on an index of these goods. Thus, Rawls neatly ties the basis of interpersonal comparisons to a person’s moral powers that embody the capacity for cooperation -- an element that is central to his vision of a fair society.

## **OTHER IDEAS OF JUSTICE**

Nozick followed Rawls in defending the inviolability of a private sphere of rights, but extended this sphere far beyond what is implied by Rawls's two principles of justice. Nozick defends the libertarian position that the state's role in achieving social aims should be minimal: it should act only as a nightwatchman, guarding the security of its citizenry and preserving individual rights. A free market becomes an important arena in which individuals can exercise their rights and exchange their possessions without unjust state interference.

Nozick's fundamental objection to utilitarianism also applies to Rawls's conception of justice. Both of these views, Nozick contends, require that judgments regarding the justice of a given distribution depend on comparisons with some ideal, such as equal utility. Nozick rejects such *end-state principles* as fictions, unsuitable for determining the justice of a given distribution. His alternative is a theory that consists entirely of procedural principles, which determine the justice of distributions according to whether property holdings have arisen through just acquisition and transfer.

In another approach, Sen argues that the informational base of welfare economics is too narrow, focusing only on information related to preferences. In his view, the appropriate informational base for normative economics should be, not welfare or good, but rather capabilities -- the ability of individuals to achieve valuable functionings, which for Sen, are the essential constituents of human wellbeing. According to his Aristotelian-inspired vision of a just society, benevolent governments must take a stand on a particular conception of what makes for a good life, and take steps to ensure that everyone has a reasonable chance to achieve it. One implication is that the capability sets of all persons should be made as equivalent as possible.

Taken together, these alternative conceptions of justice -- Rawls's, Nozick's and Sen's -- present different ways of defining the goals of institutions in a just or good society. Their respective views of justice imply different goals, but they all share the belief that justice requires equality in one sense or another.

Although economists have been reluctant to accept the possibility of interpersonal comparisons of subjective utility, many economists have worked at incorporating Rawls's maximin rule within a utilitarian framework that makes the heroic assumption that everyone has the same utility function. Such an effort exemplifies a common economists' response to recent major philosophical writings on distributive justice: they have worked at producing theories of justice that preserve the utilitarian roots of welfare economics.<sup>2</sup>

We have summarized several articles by economists grappling with challenges from philosophy. In the following section we will see Hal Varian's response to, and use of, Nozick's ideas of procedural justice. Later we will see John Roemer responding to Ronald Dworkin's work on equalizing resources; and Marc Fleurbaey taking up the ideas of Richard Arneson and Gerald Cohen on equalizing opportunities for human advantage. The summarized article by John Broome presents an attempt to reconstruct utilitarian theory to accommodate matters of justice without reference to preference satisfaction.

## **ECONOMISTS REPLY TO THE CHALLENGE: THE "ENVY-FREE" APPROACH**

Since Rawls's major work, a tradition within economics has developed that defines just distributions in terms of a single criterion. In a survey of this movement, one recent commentator states that

[t]he criterion of envy-freeness, according to which no agent should prefer any of his neighbors' allocation to his own, has become a central part of the economic theory of distributive justice. It essentially corresponds to the need to express an ideal of equality in societies where preferences and endowments are heterogeneous.<sup>3</sup>

The economic literature on envy-free justice witnessed its major developments in the mid-1970s, as academics contested whether the push for social and economic equality was driven by envy or by some loftier purpose. After a short hiatus in interest, this subject has flourished again in the 1990s.

Varian's early work, summarized here, was seminal in analyzing fair allocations in models of complex economic environments. Previously, it had been mathematically demonstrated that envy-free allocations were possible in models of exchange economies that excluded production factors; however, once production was brought into the model, there was no guarantee that a fair allocation<sup>4</sup> would exist. This problem arises because people with less talent might wish they had the larger resource bundles of goods that can be achieved by those with more talent. Varian's solution to the production problem was to argue that everyone would be satisfied with his or her own resource bundle (i.e., the distribution would be envy-free) if the definition of resource bundles included not only the goods and services contained in a given bundle but also the work effort required to attain those goods and services. An individual with lesser endowments would then prefer the resource bundle of the more talented only if he or she would be willing to make the efforts and sacrifices necessary to achieve it. Thus, it is impossible to model a competitive equilibrium in which no person prefers the resource bundle of another.

Varian's article was also significant in demonstrating that a libertarian theory of justice, such as Nozick's, fails to adequately consider the justice of initial distributions. He attempts to remedy this lacuna in his own theory by assuming an initial distributions of consumption goods to all individuals that is equal in the sense that it will not give rise to envy (as defined herein).

### **A DEEPER LOOK AT EQUALITY**

The envy-free approach to distributive justice has led many to question whether it accurately captures the nature of egalitarianism. Clearly, envy plays a role in certain egalitarian claims. A child who does not receive his fair share of cake may be envious of the larger shares of his siblings. However, there are many types of egalitarian claims, not all of which are concerned with envy.

Michael Walzer's famous book, *Spheres of Justice*, partially summarized here, makes the case that most egalitarian claims arise not from envy, but from the harms that follow from inequalities. It is not that the poor desire equality because they desire the wealth of the rich (although they may); rather it is because the rich can grind the faces of the poor. Also, he disputes the very assumption with which the envy-free theorists begin their project -- that goods

simply appear in the hands of hypothetical agents in mathematically formalized models. Instead, justice requires an appreciation of the cultural meanings of goods and the historical conditions in which they develop. Consequently, the ideal of equality is better understood as a struggle for being free from the domination of those who have misappropriated the meanings of goods. In Walzer's articulate vision of an egalitarian society, more importance is placed on diminishing the effects of inequalities and less on eliminating the inequalities themselves.

The question -- equality of what? -- may be variously answered: e.g., equal welfare, freedoms, social primary goods, resources, or capabilities.<sup>5</sup> As we have seen, Rawls wants to minimize inequalities among individuals' holdings of primary goods, the resources that every rational agent needs to pursue his or her life aims. In situations where inequalities must obtain, he defends a difference principle, which requires that inequalities benefit the least advantaged. Sen argues for equalizing individuals' capability sets. Nozick seeks equal respect for property rights. Each of these thinkers uses "equality" in different ways, and for different purposes -- a point adeptly made by Robert Sugden in the summarized review of Amartya Sen's book *Inequality Reexamined*.

Along lines comparable to Rawls, philosopher Ronald Dworkin developed arguments opposing the idea, implicit in welfare economics and the envy free literature, that preferences, utility, and welfare are the appropriate terms in which to define egalitarian distributions. Although welfare economics often sidesteps issues of equality, its assumptions can be used to construct a distributive criterion aimed as equalizing differences among the utilities achieved by different individuals. However, Dworkin argues that the appropriate target of egalitarian concerns is resources, not welfare.

Prominent among Dworkin's criticisms of the equal welfare school (including, of course, the utilitarian) is the objection that this approach fails to hold people responsible for either offensive or expensive tastes. That is, if one of the objectives of a just society is to ensure that its citizens obtain equal welfare, then both misanthropes (who derive happiness from others' misery) and people who require the finest foods in order to be happy must receive more goods and services than others who have more average tastes.<sup>6</sup> Dworkin argues that these examples demonstrate that the concept of equal welfare fails to acknowledge the importance of personal responsibility in developing one's tastes and pursuing one's goals. Moreover, he takes these objections to imply that justice need not be responsive to individual tastes and preferences.

Dworkin's own view is that just social institutions should be willing to compensate individuals only for the effects of circumstances over which they have no control, such as being born with poor health or few talents, or suffering the effects of natural disaster. This implies that people should be compensated for inequalities among natural endowments over which they have no responsibility, but that people should be held responsible for their ambitions. Roemer (see summary) agrees with Dworkin that a theory of distributive justice should focus on responsibility, but argues that Dworkin's equal resource view cannot escape the need to address welfare, since a person's innate characteristics includes the ability to convert resources into utility. In fact, Roemer questions any approach that distinguishes handicaps from tastes, since preferences arise from many factors over which individuals have little control, such as genetic endowments and education.

The idea that welfare and responsibility are both relevant to issues of distributive justice is defended by proponents of the equal opportunity school, which seeks to equalize *individuals' opportunities for welfare*.<sup>7</sup> Proponents agree with Dworkin that an adequate conception of justice needs to distinguish talents from ambitions, but they also maintain that a concern with responsibility is compatible with a concern with preferences and welfare.

Fleurbaey, in a summarized article, objects to the equal opportunity principle on the grounds that it is simply impracticable to equalize the opportunity sets of all individuals over the course of their lives, given that individuals change their preferences, suffer bad luck, make poor judgments, and may or may not have free will. His alternative egalitarian theory avoids the need to distinguish talents from ambitions -- a problem that has plagued both the equal opportunity school and Dworkin's equal resource theory. Instead, Fleurbaey argues that social institutions should equalize those outcomes for which they are responsible, a view that turns on the more feasible distinction between private and social realms. This is one of the few theories of justice sponsored by an economist that avoids the language of preferences and utilitarian ideals.

A final approach is to reformulate utilitarianism in terms that avoid the language of preferences. In the summary of selections from *Weighing Goods*, Broome argues for a teleological theory of the good which emphasizes the structure rather than the content of good. He defines the structure of good in terms of a "betterness relation" (see summary) that allows him to avoid analyzing the concept of utility, in terms of preferences or anything else. A normative economics built on Broome's utilitarianism need not define Pareto optimality on the basis of preferences, and avoids problems relating to Sen's *Impossibility of a Paretian Liberal* argument (discussed in Part 3).

In the past, utilitarians gave lukewarm support for redistributive transfers. They could justify transfers from the wealthy to the poor on the grounds that the poor will benefit more than the wealthy from the same incremental benefit; however, as the nineteenth century economist, Frances Edgeworth pointed out, this is true only if the wealthy and the poor have similar benefit functions. In his view, as a utilitarian and an aristocrat, they did not: the wealthy could do more with more. Broome has offered a more convincing approach to utilitarian equality; in his view, equality is desirable in itself, as part of the general or social good. For instance, where one falls in the income distribution matters from the perspective of general good. It follows that inequality can be a harm to a person, whether or not the rich can do more with more.

### **WHAT IS THE RELATIONSHIP BETWEEN EQUITY AND EFFICIENCY?**

As long ago as the eighteenth century, economists considered the social goal of equality (broadly understood) to be directly opposed to the economic goal of efficient resource allocation. The question of how to balance efficiency goals with the distributive goal of equality is often interpreted as a question of sacrifice: should wellbeing levels be traded for justice? And whose wellbeing? Would an individual living in a just society be better off (if other things could remain the same) than the same person living in an unjust society? If so, it is not clear whether this is because justice is a component of, or in a more fundamental way a condition of, her wellbeing or her quality of life.

A common belief implied or stated in the teaching and practice of economics is that, if equity and efficiency are both regarded as desirable things, we face a zero-sum game in which it is necessary to settle for less of one in order to get more of the other. A justification for this view is the assumption that redistributive transfers (aimed at equalizing material resources) eliminate the differential rewards necessary to motivate people to be productive. However, many recent thinkers have come to question not only this motivation argument, but also the idea that these goals are opposed to one another.

A basic philosophical issue arises when we consider the possibility of making a trade-off between equality and efficiency.<sup>8</sup> Such a trade-off makes sense if we believe these to be values or goals of similar standing: i.e., if both are regarded as final goals, or else if both are seen as intermediate. However, recent writing in philosophy and among philosophically-inclined economists has emphasized that, while equality may be regarded as a means to other ends, it is often also held as an end in itself. By contrast, while economic theory is often taught and promulgated as though efficiency were a final goal, few commentators overtly defend such a position. If equity is a final goal and efficiency is only a means to other, final ends, it should be possible to find ways to avoid a trade-off between them.

Kenneth Arrow has been a strong advocate of the view that modern equilibrium theory implicitly supports the compatibility of equity and efficiency. In a summary included here, Arrow contends that the motivation argument relies on the mistaken assumption that a person is always entitled to the value of his marginal product. In fact, an individual's marginal product depends on substitute or complementary factors beyond his or her control. Justice does not require assigning the full value of their product to individuals who are not responsible for the value of these factors.

Another practical observation is that, in many sectors of the economy and in many types of firms, productivity levels do not rise with increasing benefits; that is, higher pay does not necessarily lead to higher productivity levels. Therefore, appropriate redistribution strategies need not reduce productivity levels. Arrow also defends the idea that transfers from the wealthy toward investment in social and human capital formation among the poor will raise society's productivity levels in the long run, if not in the short run. Far from being a trade-off, efficiency and equality are interdependent and mutually reinforcing.

Martha Nussbaum also argues (in an article summarized here) that issues of justice and wellbeing go hand in hand. She defends a capabilities-based conception of human good in which the political planner must satisfy Aristotle's primary condition for a just polity -- that no one lacks for sustenance. This requirement of political justice, also found among institutional theories of the welfare state (see Part 8), implies a wide safety net for the disadvantaged and places extra emphasis on the importance of education, for it is here that the powers of mind are cultivated. Beyond these basics, it is crucial to Nussbaum's view, (though not to Sen's) that the political system ought to promote everyone's capability to live an experientially rich human life.

### **SOME REMAINING DEBATES**

It was assumed, by many of the great economists from Adam Smith and his precursors up through the early part of the twentieth century, that an understanding of economic systems, and a

measure of their success, must be rooted in moral and political philosophy. As markets play an ever larger part in everyday life, this assumption seems more, not less, relevant today; but utilitarianism and positivism -- the two major philosophical influences on economics -- are withering or have already withered on their original philosophical vines. This essay and the summaries it introduces represent the leading modern alternatives. Among these we have stressed Rawls's theory of "justice as fairness" and Sen and Nussbaum's "capability ethic," as of particular relevance for the field of economics.

Economists might have come closer, by now, to understanding the relationship between the goals of efficiency and justice if philosophers could offer a widely accepted answer to the Socratic question: what makes for a good life? Modern answers may be divided along the lines of a debate that is sometimes represented by the technical-sounding question: does the right have priority over the good?

On one side of this debate are those such as Nussbaum and Sen who, with Aristotle, believe that, from the point of view of political institutions, it is necessary to define what it means to have a good life before one attempts to figure out which political arrangements best serve this goal. On the other side are those such as Rawls and Scanlon, who believe that it is necessary for a political planner to accept that citizens may have life goals that conflict with one another; this puts the priority on establishing social institutions that preserve the rights and liberties of individuals even while they pursue their different aims.

Much of the recent debate about the respective virtues of the capability ethic and social contract theory concern just this issue: can the good life be defined independently of the concepts of rights and liberties? For normative economic theory, this debate is important for the following reason. The contractualist approach has advantages when applied to the design of political, social and economic institutions within constitutional democracies, but it has limits in other parts of the global arena. On the other hand, the capability approach has advantages when applied to issues of international economic justice.

The challenge for philosophy and economics is to work together to promote, simultaneously, the goals of freedom, justice, security, and prosperity. The question is still open whether there is a unified social philosophy that will usefully replace utilitarianism in guiding economic theory and policy for all parts of the world; or whether for a variety of circumstances economics requires a variety of philosophical underpinnings.

## Notes

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1. Serge-Christophe Kolm, *European Economic Review* 38(1994): 721-730. Quote is from p. 721.
2. The major exception to this trend is the reaction of economists to Michael Walzer's theory of justice, discussed below and represented in a summary. Communitarian economists have been especially responsive to Walzer's work.
3. Christian Arnsperber, "Envy-Freeness and Distributive Justice," *Journal of Economic Surveys* 8(1994): 155-186. The quotation is from p. 155. This article is also a good resource for anyone interested in an overview of the major issues in this field.
4. This literature defines a "fair allocation" as one that is both equitable (envy-free) and Pareto efficient.
5. The philosophical literature on equality, and on the appropriate target of egalitarian concerns, is vast and wide-ranging. For an illuminating discussion of problems that crop up in comparing and contrasting these theories see,



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Norman Daniels, "Equality of What: Welfare, Resources, or Capabilities?" *Philosophy and Phenomenological Research* 1(1990), Fall Supplement.

6. Another objection is made by Sen, who points out that the equal welfare approach would allocate more resources to a pleasure wizard than to a cripple, because one is a very efficient converter of resources into welfare, while the other is not.

7. Richard Arneson, "Equality and equal opportunity for welfare," *Philosophical Studies* 56(1989): 77-93. Gerald Cohen, "On the currency of egalitarian justice," *Ethics* 99(1989): 906-944. There are subtle differences between their respective views. Cohen believes that the equal opportunity principle applies to a slightly broader concept than welfare, namely, human advantage. Strictly speaking, neither view seeks to equalize opportunity sets; rather the aim is to make them equivalent.

8. Arthur Okun popularized this notion in his book *Equality and Efficiency: The Big Tradeoff* (Washington: Brookings Institute, 1975). For two similar opposing views, see Julian Le Grand, *Equity and Choice: An Essay in Economics and Applied Philosophy* (New York: Harper Collins, 1991). Also, Zamagni, "Efficiency, Justice, Freedom: A Perspective from Modern Economic Theory," *Giornale degli economisti e annali di economica*, 52(1993).