

# 1 | Economic Reasoning and the Ethics of Policy

**P**OLICY JUDGMENTS are easier to come by, the farther we are from our goals. If there are only two directions and we know which is forward, and there are limits to how fast we can go, no fine discrimination is needed. If aid to the poor is far too little, highway traffic far too fast, building codes far too lax, teachers' salaries far too low, or the rights of defendants far too little observed, we know what we need to know to get moving. We can worry about how much is enough when we get close, if we ever do. Meanwhile we can push on.

Knowing what to do is also easy if our capabilities are growing and our horizons receding, and yesterday's goals will be outgrown tomorrow. Like a family on a rising income, we needn't worry about overshooting: if we buy too big a house today, we'll afford it tomorrow.

I have often been glad that I wasn't in charge. It is easy enough to see plainly that there is too much inequality (or illiteracy, or ill health, or injustice) and to help to reduce it, knowing that despite all efforts too much will remain. But if it were up to me to decide *how much* inequality is not too much, or how much injustice, or how much disregard for the elderly or for future generations, I'd need more than a sense of direction.

Discomfort also arises when, intent on speeding toward an ever-

receding goal, the goal suddenly stops receding and we threaten to overshoot. There appears to be a widespread belief that overshoot is what we've done.

Worse, there is retrospective disenchantment with the mood that motivated the effort and set the goals in the first place, back in the 1960s. There is chagrin at having been too enthusiastic about what could be accomplished. There is disaffection toward those whose demands are insatiable and whose gratitude is inconspicuous. Whatever the reason, there is a reexamination of policy, especially policy that reflects social obligation. There is retrenchment in the air and on the ballot, and second thoughts about what we can afford for ourselves and what we owe others.

It isn't all sour grapes. Our projection of the possible has shrunk. Our economy is not behaving. Growing income no longer promises to make light of our burdens in another decade or two. We do not know what has been depressing our productivity and can't be sure that, whatever it is, we shall recover soon. Inflation has a mind of its own. The demographics of the labor force are against us, and at the same time the rules of the game allow endless numbers of people from faraway places, once over the line, to touch base and be safe.

So it is not surprising that commitments are being reassessed, "tradeoffs" discussed, costs weighed anew against benefits, and even constitutional initiatives promoted to enforce a policy of containment. Techniques of policy analysis that recently were despised as mean spirited and stingy by people who preferred to base policy on vision and generosity are being superseded by what used to be called meat-axes and straitjackets.

These are not "hard times" in the old sense. In this country life is still good and getting better for most people. But it is not measuring up to expectations. They might better be called "difficult times": it is the problems, not the times, that are hard. And among the hard issues are some ethical ones. They may not be the hardest or the most important, but they are important and they are hard.

I have been asked how economic reasoning can help, or how it misleads, in facing, solving, or avoiding the ethical components of policy. Does economic reasoning itself represent a particular ethic; or, if not the reasoning, the people who use it?

## The Ethics of Policy

What I mean by the ethics of policy is the relevant ethics when we try to think *disinterestedly* about rent control, minimum wages, Medicaid, food stamps, safety regulations, cigarette taxes, or the financing of Social Security.

Farmers have an interest in price supports, laundry operators in minimum-wage laws, doctors in the financing of Medicare, and electric utilities in clean-air regulation; and until my youngest child is safely overage I shall have a personal interest in the draft. When people take sides on a leash law we don't expect them to argue it the way they discuss the space shuttle. I want to define the ethics of policy as what we try to bring to bear on *those issues in which we do not have a personal stake*.

It is hard to find issues that are absolutely unsoiled with personal interest. On abortion and capital punishment our personal ethics usually dominate. Food stamps affect us, whether we qualify or not, because they cost money. Someone meticulously interested in his own welfare could find at least a minuscule personal interest in a UN program for alphabet reform.

Still, most of us on many issues want to think and to talk as though we are not interested parties. We want to discuss welfare and national defense and school construction and unemployment benefits and automobile-mileage standards as though we were not personally involved. There will be an unmistakable element of social obligation; nobody can discuss income-tax rates or welfare levels without a participatory awareness that the poor, the unfortunate, the disadvantaged, and the otherwise deserving have some legitimate claim on those among us who can afford to help. But although few issues are without financial impact somewhere, and most big issues involve big amounts of money, we can often confine our personal stake to an aggregate and nonspecific social obligation. Our position in the income scale affects our conditioning as well as our reasoning, but beyond that we can try to be neutral, removed, vicarious, impartial, judicious.

Incidentally, I say this only because I expect this book to be read by a special set of people. Most people probably devote most of their policy interest to the things that concern themselves and do it with a clear conscience. They do not get drawn into ethical abstractions. They may have strong ethical views on a limited

number of subjects that do not flow from their stake in the outcome, but on matters called “bread and butter” they accept the ethic that in politics it is fair to look out for your own interest, expecting others to look out for theirs. People who read or write books like this one, though, usually try to take distributive issues seriously but not personally. Students, for example, rebelling against higher tuition are reluctant to say it is to save their own money; they join the picket line in behalf of somebody poorer. And professors concerned to protect their *own* salaries are thought not to be playing the ethical game. But the tobacco farmer concerned solely with his own family’s welfare is excused from scholarly disinterest.

### **The Ethics of Pricing**

My students always like gasoline rationing. They believe in it on ethical principles. (They say they do, and they sound as if they do.) Evidently the principles lie deeper than rationing itself; the students must have some notion of what happens with rationing and without it, or with some specific alternative, and they must have a preference about the outcome. Students know that there are gainers and losers; their ethics appear to relate to who gains, who loses, and how much.

I can talk most of them out of it. It takes longer than fifty minutes, and I never try it if I have only a single class hour. They probably distrust my ethical principles and think I do not care about what they care about, or care as much. They very likely think my ethics are “process oriented” and the free market enchants me, while they are “consequences oriented” and don’t like the results.

Time permitting, I accomplish their conversion in two stages. I warn them in advance that I am going to show them that if they like rationing there is something they should like better. I join them in believing the free market needn’t be let alone, but I do propose what is sometimes called “rationing by the purse.” I suggest we let the price of gasoline rise until there is no shortage, and capture the price increase with a tax. Because that looks hard on the poor my students do not like it.

The first step in subverting their ethical preference is to propose that under any system of rationing that they might devise—and I take a little while to show them that it is not easy to design a

“fair” system of rations—people should be encouraged to buy and sell ration coupons. This proposal has little appeal. The rich will obviously burn more than their share of gas, the poor being coerced by their very poverty into releasing coupons for the money they so desperately need. But eventually students recognize that the poor, *because* they are poor, would like the privilege of turning their coupons into money. Where gas coupons can only provide them gas at a discount, transferable coupons can buy milk at a discount. If it is unfair that the poor cannot drive as much as the rich, it is the poverty that is unfair, not the gasoline system.

That principle established, we observe that coupons are worth cash, whether you buy them, sell them, or merely turn in your own at the local service station. If gas at the pump is \$1.25 and coupons sell for 75 cents, the net price of gasoline is \$2.00; anyone who gets ten gallons’ worth of coupons from the Department of Energy is getting a clumsy equivalent of \$7.50 cash. The station that sells ten gallons receives \$12.50 in money and \$7.50 in coupons that could have been traded for cash. What we have is a 75-cent tax payable at the pump in special money, and a cash disbursement to motorists paid in this special money. We could just as well do it all without the coupons.

There is more to it than that, but the “more” usually does not involve much ethics. It isn’t that we resolved an ethical issue. We merely lifted the veil of money and discovered that the ethical issue we thought was there was not. Or, perhaps better, the ethical issue that we associated with rationing was tangential to that procedure. Whatever the compensatory principle is that appeals to the students’ sense of fairness, there are many procedures that can achieve it, some better than others, rationing neither worst nor best; and once it is all converted to money, it is easier to see what some of the alternatives are and whether they are ethically superior. Superficially it may seem wrong to give gas coupons to people who don’t drive; but if the gasoline is taxed instead and the proceeds rebated to the public, we can judge the ethics of alternative distributions of the proceeds, not just those based on drivers’ licenses and car registrations.

Persuasion is a little harder with rent control, partly because students do not like landlords. We try to see whether there might be something better, even in principle; whether people seeking

apartments are losers under rent control; whether some nonevictable tenants in rent-controlled apartments would like to cash in their precious property right but are locked in because their claim is to a specific apartment. Usually by the time we have identified all the interested parties and the likely magnitudes of their interests, and have considered a few alternative ways to accomplish the things rent control is intended to accomplish, the liveliness of the issue is undiminished but the ethical loading has mostly evaporated.

I dislike “counting coup” over vanquished students in order to display, and to hope you are impressed with, some of the ways that economics can contribute to the clarification of ethical issues. But at least the claim for economics is modest: it often helps diagnose misplaced identification of an ethical issue. And it does this solely by helping to identify what is happening. It is not clarifying ethics; it is only clarifying economics.

Let me give a few more examples. Minimum-wage laws are thought to have ethical content. But if their main effect, or even their purpose, is to keep the young and the old and the otherwise least valuable employees from working at all, the ethical issues may not be what the proponents thought they were. Making utilities pay the full cost of smoke abatement seems eminently fair, unless the costs are borne by consumers of electricity and the clean air enjoyed by whoever lives downwind, in which case we may want to know who lives downwind and who buys the electricity, the utility company not having much interest in the matter. (Even if the electricity is procured mainly by business, we don’t know yet who is paying until we know who buys the products, or who will settle for lower wages when the other costs rise.) Even our feelings about people who evade the income tax by not declaring tips or typing fees or truck garden sales will depend on whether the system mainly lowers wages and prices in bars and restaurants and reduces the cost of lettuce or of getting theses typed.

### **The Clash between Equity and Incentives**

Policy issues are preponderantly concerned with helping, in compensatory fashion, the unfortunate and the disadvantaged. We have welfare for those who cannot work, unemployment benefits for people out of jobs, disability benefits for the disabled, hospital

care for the injured and the ill, disaster relief for the victims of floods, income tax relief for the victims of accidental loss, and rescue services for people who find themselves in danger. Social Security is based on the premise that people will arrive at post-working age with inadequate savings to live on.

An unsympathetic way to restate this is that a preponderance of government policies have the purpose of rewarding people who get into difficulty. People are paid handsomely for losing their jobs; if you smash your car the IRS will share the cost of a new one; and if your injury requires hospitalization you can stay in an air-conditioned room as long as the doctor certifies that you will recover better if you don't go home. By treating the absence of a "man in the house" as a special grievance for a woman with dependent children, families have even received a bonus for fathers' leaving home.

There is no getting away from it. Almost any compensatory program directed toward a condition over which people have any kind of control, even remote and probabilistic control, reduces the incentive to stay out of that condition and detracts from the urgency of getting out of it. It is a rare ameliorative program that has no visible way, by its influence on behavior, to affect the likelihood or the duration or the severity of the circumstances it is intended to ameliorate. And most commonly—not always but most commonly—the effect on behavior is undesired and in the wrong direction.

To keep the issue in perspective we can observe that private insurance, even the informal kind that allows us to ask for help when we run out of gas, can have the same adverse influence on behavior. People more willingly drive on slippery roads the more nearly complete their collision coverage; back doors are unlocked if the homeowner's policy is liberal in its provisions for burglary. I am more indulgent of my sore throat if my employer provides an ample quota of sick days.

There is no use denying it in defense of social programs. As is usually the case with important issues, principles conflict. On the one hand, we want to treat unemployment as a collective liability, sustaining the family at public expense when working members lose their livelihoods. And on the other, we want not to induce people to get conveniently disemployed or to feel no need when unemployed to seek work vigorously. What helps toward one ob-

jective hurts toward the other. Offering 90 percent of normal pay can make unemployment irresistible for some, and even a net profit for those who can moonlight or work around the home. Providing only 40 percent over a protracted period makes living harsher than we want it to be. There is nothing to do but compromise. But a compromise that makes unemployment a grave hardship for some makes it a pleasant respite for others, and we cannot even be comfortable with the compromise.

Decent welfare in a high-income state is bound to be at a higher level than in a low-income state. It induces migration. Even if we favor migration, the state that finds more and more migrants on its welfare rolls did not intend to reduce the poverty of other states by helping any and all who could get up and move. But to provide an unattractive level of benefits would condemn the intended beneficiaries to a level of living below what their home state wanted to provide them. Again two principles conflict.

There are exceptions to this tendency of inducing the wrong behavior. Federal deposit insurance was designed in the 1930s to provide restitution to people whose bank deposits were lost; by generating confidence, the insurance reduced precisely the behavior that caused the problem. And a benefit strictly related to age in years, though it may reduce efforts to save, at least can have no effect on the speed with which people grow older. But the tendency is pervasive. It accounts for a good part of the escalation of medical costs.

I do not know whether one of the principles, helping the disadvantaged, should be considered ethical and the other, not letting them get away with it, not ethical. Much of the discussion about welfare rights, about not proportioning medical care to the ability to pay, and about not producing a "work ethic" by threatening the unemployed with their families' starvation, is in an ethical mode. To a lesser extent, ethical considerations are evoked over the encouragement of malingering, rewarding those who beat the system, or inducing dependence on the state. Once it is recognized, however, that two principles conflict, that two desiderata point in opposite directions and neither is so overwhelming that the other can be ignored, that both objectives have merit, and even that there is no ideal compromise because there is a diversified population at risk, the ethical contents of the principles begin

to seem tangential to the inescapable problem of locating an acceptable compromise.

It is a universal problem. It won't go away. It can't be neglected. It isn't even unique to *public* policy. The word "compromise" has those two different meanings. Compromising *a* principle sounds wrong. Compromising *between* principles is all right.

### **Valuing the Priceless**

Among the poignant issues that policy has to face, explicitly or by default, are some that seem to pit finite cost against infinite value. What is it worth to save a life? How much to spend on fair trial to protect the innocent against false verdicts? What limits to put on the measures, some costly in money and some in anguish, to extend the lives of people who will die soon anyway or whose lives, in someone's judgment, are not worth preserving?

These issues are ubiquitous. They arise in designing a national health program. They are directly involved in decisions for traffic lights, airport safety, medical research, fire and Coast Guard protection, and the safety of government employees. They are implicitly involved in regulation for occupational safety or safe water supplies, in building codes and speed laws, even helmets for motorcyclists—because somebody has to pay the costs.

It is characteristic of policymakers, especially at the federal level, that they usually think of themselves as making decisions that affect others, not themselves. Hurricane and tornado warnings are for those living where hurricanes and tornados strike; mine safety is a responsibility of legislators and officials above-ground concerning the lives of people who work underground. Policies toward the senile, the comatose, the paralyzed, and the terminally ill are deliberated by people who are none of the above. Occasionally the legislator debating a 55-mile speed limit pauses to think whether the benefits in safety to his own family will be worth the added driving time, but if he or she is conscientious even that calculation may be surreptitious.

The situation is different when a small community considers a mobile cardiac unit or a new fire engine. The question then is not what we ought to spend to save someone else's life but what we can afford to make *our* lives safer. Spending or stinting on the lives of others invites moral contemplation; budgeting my expendi-

tures for my own benefit, alone or with neighbors for the school safety program, is less a moral judgment than a consumer choice, a weighing of some reduction in risk against the other things that money will buy.

There is a suggestion here. Maybe we can reduce the unmanageable moral content of that paternalistic decision at the national level by making it more genuinely vicarious. Instead of asking what society's obligation to *them* is, we should ask how *they* would want *us* to spend *their* money. In deciding how much to require people to spend on their own seat belts, smoke alarms, fire extinguishers, and lightning rods, it is easier to be vicarious and it is legitimate to get our bearings by reflecting on how much we might reasonably spend on our own safety. The question still may not be easy, but it is less morally intimidating.

Surely, if we were all similarly at risk and in like economic circumstances, this would be the way to look at it, whether for the town bandstand or the town ambulance. On a national scale it is less transparently so, but nevertheless so, that we should want our appropriations committees to think of themselves as spending our money in our behalf. We want them neither to skimp where it really counts nor to go overboard to prepare at great expense—our expense—for the remotest of dangers. We want them to be thinking not about what concern the government owes its citizens for their safety but how much of our own money we taxpayers want spent for our safety.

With that perspective it is remarkable how quickly the issue, now collectively self-regarding instead of other-regarding, drops the ethical content that was only a construct of the initial formulation. We can still find ethical issues, but not the one that seemed so central.

We could call this the contractual approach to social obligation. In the absence of an understanding, I may owe you, in your extremity, unbounded attention and concern, comfort and livelihood, room and board, and the best medical attention in perpetuity, and feel guilty when I stop to wonder whether you are worth the burden you are putting on me. When it is my turn of course I'll expect the same from you (or from whoever has the corresponding responsibility toward me that I had toward you), feeling a little guilty perhaps but not enough to relinquish my claim. But if we could sit down together at an early age in good health and

legislate our relation to each other, specifying the entitlements we wished to obtain between us, recognizing equal likelihood of being beneficiaries or benefactors, we could elect to eschew exorbitant claims. And it would not strike us as an ethical issue.

The contractual approach can help with some of those other tantalizing dilemmas, like which planeload of passengers to save, the big plane with lots of passengers or the one with mostly empty seats, if both are at risk and one at most can be saved. What I should do in the control tower if that Godlike decision were mine is an ethical dilemma that for some thoughtful people has no easy answer. But if I am an airline passenger answering a questionnaire for the FAA on what rule I want the control tower to follow in emergencies, the issue is neither ethical nor a dilemma.

I cheated a little in supposing that we were all similarly situated with respect to some risk and alike in our ability to afford protective measures. We usually are not. But the value of this conceptual approach, of considering what the safety is worth to the people who are safer, may still be salvaged. If you are more at risk than I—let's say you are at risk and I am not at all—and the rule is that we share the cost of reducing the risk and we are purely self-regarding, I shall find the measures worth nothing, while you find the measures twice as attractive as if you had to pay it all yourself. If you fly a plane and I do not, the new runway lights at the local airport will cost us each \$1,000, and may be worth it to you but not to me. If they are worth more than \$2,000 to you, they ought to be bought, at least if you'll pay for them. (Whether I ought to pay half is a separable issue.) But suppose you wouldn't pay more than \$1,500 for the slight contribution the runway lights make to your safety. I propose that they shouldn't be bought.

Even though we divide on the issue of whether, paying \$1,000 apiece, we ought to buy the lights, the economist in me formulates the problem this way: If, because your personal safety is involved, you are entitled to my contributing \$1,000 toward the purchase of runway lights, and I acknowledge your claim and put up my money for your exclusive benefit, do you really want to buy the runway lights or would you rather take my \$1,000 and keep it? I don't care. I may be annoyed at having to put up the money when you don't want the lights after all, but I might be more annoyed that you are spending my \$1,000 on something that you

didn't consider worth the cost. In fact, we could both be better off if instead of purchasing the lights I just gave you \$750 and we forgot the lights.

For some among us that may not settle the issue. But I propose that it is nevertheless a useful perspective, a relevant consideration, and although other considerations are relevant too they may not be ethical ones, or if they are they are not the ethical question of whether our little two-person society put too low a value on *your* life in deciding not to buy the runway lights. (*You* may have put too low a value on your life, but I don't know why I should feel guilty about that. You may also need better lighting in your driveway.)

A harder question is what to do if you are poor and I am rich, and you use a cheap little airport and I use a better equipped one, and better runway lights are now available, and they are to be provided, if provided at all, out of a common fund for airport safety. If the lights will make as much difference to safety at your airport as at mine, and someone raises the question whether we should afford the same expensive lifesaving apparatus at your cheap airport as at my more lavish one, we really come up against the question: is your life worth as much as mine? (Leave aside the possibility that there are more of you to benefit from your lights, or fewer of you, compared with the traffic at my airport.)

Let's face the question. If you are poor and I am rich is your life worth less than mine? "Worth" refers here to how much might properly be spent to protect it from some specified risk. (Notice that "worth" is an arithmetical construct: If we are willing to spend \$2,000 per capita, but not more than \$2,000, to protect everybody from something that is fatal for one person in five hundred, we shall spend an average of \$1,000,000 per life saved. In that respect and only in that respect have we "valued" each life at \$1,000,000.) And when we ask what your life is worth, or what my life is worth, and whether your life is worth less than my life, it helps greatly in straightening out what we have in mind if we ask, worth to whom? And, who's to pay it?

If you are poorer than I, it is likely that *your* life is worth less to *you* in *your* money than *my* life is worth to *me* in *mine*. You cannot afford to pay as much for anything, including personal safety, as I can, precisely because you are poorer.

We expect the poor to invest less in home or auto safety than

the well-to-do, because these goods are purchased at the expense of more urgent necessities. We expect a poor town to spend less on fire protection than a well-to-do town, because the poor town can afford less taxes and needs schools and streets as well as fire engines. But does this mean that a government air-safety program might properly decline to provide you those new runway lights, while my airport gets them at government expense?

The economist in me wants to say “yes.” The policy adviser in me will go only as far as “maybe” or “it depends.” It depends on who is ultimately putting up the money, and it depends on what the alternative is if you don’t get the lights.

The affirmative argument contains something worth knowing. It runs as follows, in stages.

First, if the users of each runway had to pay for all the facilities at that runway, including safety facilities, we might find that the lower-income users of your airport did not consider the marginal addition to safety contributed by the new lights to be worth the money, while the well-to-do people at my airport considered the lights a good bargain. We may have feelings just like yours about life and death; but the expenditures we forego to pay for our lights are less important to us than if we were as poor as you. So one should not be surprised to find that our airport gets the lights and yours does not.

If now (stage two) a federal safety authority were to consider requiring those new lights, the lights still to be paid for by each airport’s users, to require you to buy the lights they would have to believe that you had made a mistake. Assuming that you knew the cost of the lights, they would have to assume either that you did not know how much the lights would reduce the risks of landing and takeoff, or that you didn’t know how to weigh your own safety against your own money. But notice that they would have to believe that you had made a mistake from your *own* point of view; and if they can ascertain that you did understand how much reduction in risk the lights would provide, they must now think that you undervalue your own life or overvalue the other things you have to buy out of your income. Maybe you do; but you may not see why federal air-safety authorities should have a better idea than you do of what your money is worth to you. You might reasonably protest the requirement that you equip your airport at your own expense with those expensive runway lights.

Now (stage three) let the authorities dispose of funds with which to provide safety equipment, including those new lights. They offer them to your airport at public expense. You may refuse them; but they will be free and, although they are worth less to you than what they cost, they are better than the old lights. Is the best outcome that you be provided those lights at public expense?

I try to teach my students when asked a question like that to ask in return, *what is the alternative?*<sup>2</sup> If the alternative is tax reduction—your taxes—you are really paying for these lights, paying taxes while receiving the lights “free.” You might elect lower taxes, a smaller public air-safety budget, and the old lights.

But maybe, being poor, you pay much less in taxes than we do who fly in and out of the other airport. If you decline the lights you will save *us* most of the cost. Your share of the cost, in the taxes you would save, may be less than what the lights are worth to you. Now should you take the lights with a clear conscience?

There is a final alternative. If the air-safety authorities give you the price of the lights and do not oblige you to spend it on lights—or if they give you the lights and you can sell them to somebody and keep the cash—you will probably choose the money. And I don’t care. I’d rather have the money, the lower taxes, but if you are entitled to the money and would rather have money than lights, I’ll get no satisfaction out of making you buy the lights. Maybe you will compromise, and settle for a little less in money than the lights would have cost, and save me a little in taxes.

I think that is a powerful argument in favor of the proposition that a government might properly spend less per capita to save the lives of poor people than to save the lives of people who are well-to-do. But notice that it is not an unconditional argument. It is only an argument that there is a better way to use the money—a better way from the perspective of the poor.

It is not a decisive argument. In some contexts it may be no help in resolving the issue. If the money is available only for those lights and you cannot have the money to spend as you prefer, if it is available only for air safety and not for reduced airport noise or better schools, if we who pay the taxes will respond to your appeal for comparable airport safety but will not give you other services or the equivalent in a reduction of your taxes—then your alterna-

tive to more runway safety is only less runway safety. The above line of reasoning will not help you get something better than runway lights.

But these qualifications, important as they are and decisive as they often will be, are more like political constraints on programming for safety than the ethical issue that initially seemed to arise in the question, should the lives of the poor as a matter of policy get less protection than the lives of the rich? Still, when a plane crashes at that airport with the obsolete lights we may find it hard to explain to our children why that little airport on the other side of the tracks was of less apparent concern to the safety authorities than our own airport. The authorities may have trouble explaining it to their children, too. There still are ethical issues, if not quite the one we first perceived.

### **The “Something Better” Approach**

What the reader will have noticed both with gas rationing and with airport safety is a technique that economics commonly employs in addressing whether a particular condition or policy or program has virtue. That technique is to explore whether, in respect of alternative outcomes or consequences, some alternative policy or condition or program technique is “better.” And “better” has a particular definition: superior, as an outcome, for everyone involved or, somewhat less ambitiously, for all the identifiable interests. Of gasoline rationing we explore whether there is something better, something that meets whatever objectives rationing was supposed to fulfill and does a little more besides, or meets some of them more amply, or achieves the same results at lower costs to someone concerned. To find something better does not necessarily mean that rationing is not among the better policies, only that it is still inferior to some identifiable alternative. Sometimes, but not always, it is possible to measure or estimate a lower or upper bound to the magnitude of the superiority. And sometimes if an alternative is better for not quite everybody and disadvantageous to some, we can find a way to estimate the extent of disadvantage, or put an upper bound on it.

The example of runway lights illustrates precisely what this reasoning accomplishes and some of its limitations. It is concerned only with outcomes, not with appearances, not with processes. Most important, the reasoning does not demonstrate that the su-

perior policy or program technique is actually achievable. In particular, it may depend on institutions that do not exist or politics that are unacceptable or administrative determinations that are infeasible. I doubt whether many readers will be any more convinced than I am of the wisdom of publicly providing inferior airport safety at the airport utilized by lower-income passengers and crews, even though in principle a deal could be struck according to which they obtained instead something (money, for example) worth more to them in their own judgment than the uneconomically modest improvement in runway safety.

To explore the example further, I conjecture that if airport safety were a municipal rather than a federal responsibility we would not expect the same investment in lifesaving facilities at municipal airports used mainly by low-income people as we would expect at airports frequented by business executives and wealthier tourists. We might not feel obliged to tax the passengers at the wealthier airports and transfer the proceeds to the less favored cities. We might even expect people in search of economy fares to fly in and out of the less well-protected airports, taking advantage of lower fares reflecting lower airport fees reflecting lower-cost ground equipment. And if it were then proposed that the federal budget should subsidize ground equipment at the poorer municipal airports, there would appear competing claimants to argue that more good could be done or more lives could be saved by programs for nutrition, pest control, toxic waste disposal, or police and medical care downtown instead of runway lights out at the airport.

Let me close this part of the discussion by reiterating with emphasis two points. First, this line of reasoning attempts, when honestly done, to reshuffle the consequences by rearranging proposed programs and comparing alternatives, leaving intact the original weighting system by which the outcomes for different people, or different interests, were to be evaluated. It explores alternative consequences, assessing those consequences from the points of view of all the affected parties, to see whether, whatever the proposal is or the situation being evaluated, there is "something better." It is therefore of limited, but genuine, usefulness. And the second point is that there is no mystery, nothing that cannot be penetrated by a responsible policymaker, one who is willing to make some effort to discover whether indeed there is something better.

Unfortunately, economists use the term “efficiency” to describe this process, and often distinguish between considerations of “equity” and “efficiency.” The word “efficiency” sounds more like engineering than human satisfaction; and if I tell you that it is not “efficient” to put the best runway lights at the poorer airport, you are likely to think you know exactly what I mean and not like it, perhaps also not liking me. If I tell you that “not efficient” merely means that I can think of something better—something potentially better from the points of view of all parties concerned—you can at least be excused for wondering why I use “efficient” in such an unaccustomed way. The only explanation I can think of is that economists talk mainly to each other.

### **Escaping the Dilemma of Equity and Efficiency**

Among the most divisive issues that policy deals with is the distribution of income and wealth. Taxation and tariffs, welfare and food stamps, rent control, farm price supports, the regulation of natural gas, minimum-wage laws, public housing, Social Security and its financing, electric rate regulation, and laws about labor relations and collective bargaining are mainly about the distribution of income. At least, controversies over those policies are controversies about the gains and costs to the farmers and the urban consumers and the unemployed and the landlords and the chronically ill and the healthy and the well-to-do. Freedom is an issue, but often what is fought over is freedom to pursue profit or livelihood. Rights are an issue, but they are often rights to welfare, rights to work, rights to lifepreserving medical attention, and the right to persist in a threatened occupation like fishing or farming, or the right to compete for jobs and markets.

Capital punishment, abortion, and preventive detention are issues that divide us and are not primarily concerned with the distribution of income. But even these are loaded with distributional significance. It was abortions at public expense that resurrected the controversy over the right to procure an abortion; capital punishment and the rights of defendants involve procedures that may be suspect precisely because they discriminate by income.

Ethics aside, we expect controversy along lines of economic interest. The auto industry wants protection against foreign automobiles, the steel industry against foreign steel, and the meat industry against foreign beef, and we expect both business and

labor to couch their self-serving arguments in the most captivating moral terms they can think of; their political adversaries to do likewise. But for those among us who want to affect a disinterested stance and to judge right and wrong by reference to the public interest, with special concern for the ethical implications of particular policies or the overall distribution of income, what help can we get from economics?

On the relative virtues of different distributions of income, or on how much money a poor person has to get to justify an intervention that denies a dollar to somebody who is not poor, the answer is “not much.” True to the somewhat ethically evasive character that I have been imputing to economics, economic reasoning is better at helping to choose among ways to accomplish a distributional objective than at helping to choose objectives. It can help in minimizing the cost to the rich of doing something for the poor. And in case that doesn’t interest you, economic reasoning can help to point out that it ought to! There is more for the poor, at any given cost to the rich, if you do it in the least wasteful way. And often the way economics does this is simply by looking at two things at the same time.

Economics is often like a broker or mediator in a bargaining process, good at promoting “integrative bargaining.” Integrative bargaining is searching for superior trades, finding ways to bring to the bargaining table those things that matter more to the beneficiary of a concession than to the party making the concession. If your coffee break costs me as much as an expanded medical program that you would rather have, trading coffee for medicine may make us both better off. But it requires bringing both topics to the table together.

Let me illustrate with another tantalizing proposition that I put to my students, who reject it, and to whom I then make it palatable by dealing with it in two dimensions rather than one. The income tax allows you to subtract, in going from gross income to taxable income, \$1,000 per child. It allows it whether the child is an infant or a teenager, whether you have six or only one, and—what I want to focus on—whether your income is \$20,000 or \$120,000 per year. The question is, if at \$20,000 per year \$1,000 is allowed for each child, at \$120,000 should the deduction still be \$1,000? Let me propose, as I do to my students, that the figure ought to be larger than \$1,000 per child at the higher income.

One way to make the case is that high-income families spend much more on children and the “cost” of raising their children is much more. There are counter-arguments. One is that the children of the rich are already so privileged that they don’t need tax privileges, too, compared with poor children; it should not be official policy that rich children enjoy several thousand dollars of family income while poor children get along on \$1,000. Another is that although the rich children do “cost” more than the poor and there is no need to begrudge them their superior life and environment, there is also no reason why taxpayers should collectively support well-to-do families with many children; there are other worthy causes that deserve tax relief more. It can also be argued that some wealthy couples like nice automobiles and expensive homes, some like pets, and some like children; and whether or not we approve of those who choose to spend their money on children, we should not have to share the cost with them, especially if we ourselves are not wealthy like them.

That is not an easy argument for my side to win. But to set the stage I point out an anomaly. The tax schedule that the Congress legislates is in two parts. First there is a schedule of taxes for a married couple without children; then there is a formula to adjust for family size. It is this family-size formula that allows the invariant \$1,000 per child. To increase that allowance for the well-to-do would lower the taxes for well-to-do families with children, and reduce the total taxes paid by the well-to-do. But the Congress could just as well have legislated a tax schedule not for the childless couple but for the “typical” family, say a family with two children or three. Then the basic schedule needs an adjustment, because families without children can afford to pay more income tax. A “childless premium” might be attached; that could be done either by canceling some other deductions and exemptions, say \$1,000 worth for the family that had one child and \$2,000 for the family with no children, or by adding “virtual income” to the basic income in arriving at taxable income. Question: In raising the taxable income of the childless couple, compared with the base-rate family with two or three children, do we *add* the same amount of taxable income to the family with only \$20,000 as we add to the family with \$120,000?

Evidently the family earning \$20,000 can pay somewhat more taxes if it has no children than if it has two or three, but not a lot

more; the childless couple with \$60,000 or \$120,000 appears able to pay a good deal more. Just sending a child to college can cost \$10,000 per year. If the object is to get all the taxes we can from the well-to-do families, once we have screwed the taxes as tightly as we can on families with three children, there ought to be a lot more still to be squeezed out of that childless couple living on \$60,000 or \$120,000 a year. It looks as though the adjustment for childlessness should be much larger for the family that has three or six times \$20,000.

But that is simply the mathematical contradiction of the principle we worked out a moment ago! We originally found it difficult to argue that the taxable-income difference should be larger for the rich family than for the poor; now we find that the taxable-income difference ought to be larger for the rich family than for the poor. Since the same income tax can be formulated either as a base schedule for the childless couple with an adjustment for children, or as a base schedule for the family with children plus an adjustment for childlessness, it should not make any difference which way we do it. But by simply reformulating the same income tax we seem to have arrived at the opposite conclusion.

The students work it out by themselves if I give them a little time, but my pedagogical interest is not in the tax treatment of children in different families but in the proposition that two dimensions give you more freedom than one. So I resolve the issue for them.

We have a two-dimensional tax schedule. One dimension is income, the other is family size. We can manipulate them independently. True, with any given income schedule a larger deduction for children at high income levels reduces the taxes paid by the rich. If *your* ways and means subcommittee first sets the basic schedule for childless families and *my* subcommittee gets only to determine the size of the deduction for children, there is no way that I can enlarge the child differential at high incomes without forgiving some wealthy families some taxes. But if my subcommittee goes first, and we determine larger differentials for high-income families with children, you can set as progressive a schedule as you please, making sure that the rich pay the same amount of taxes you would have wanted them to pay if my subcommittee had treated children quite differently. Together we can have as wide a child-differential as we please at high income levels with-

out providing any average tax advantage to the rich, by designing the schedule so that the childless rich pay more than they would have if the child differential were small.

In two dimensions we can have it both ways. We adjust the child differentials to conform to our notions at each income level of what difference children ought to make to the taxes paid at that income. And we design the basic income-tax schedule so that, compared with the poor, the well-to-do pay whatever we want them to pay. The income dimension and the family-size dimension allow us to meet both objectives.

The test of my success is not whether I have changed the minds of the students and they can go propose over lunch that the children of the rich should receive larger income tax deductions, and proceed to persuade their incredulous luncheon partners. The test is whether on the next issue that arises, maybe energy pricing, they understand the principle well enough to see how it applies there.

And how is that? Well, *that* is that rising energy prices during a time when energy costs are going up and shortages are becoming common do two things. They induce an “efficient” (sic!) response to the rising cost of energy. And they impose an income loss on consumers, a loss that may be quite disproportionate in its distribution, perhaps especially affecting the poor or at least the poor who live in cold climates or depend on transportation.

By an “efficient” response I mean (a) that people will use less fuel because it costs more in the other things that money will buy; (b) that those who have stronger needs for fuel will pay for more and burn it while those who have less urgent needs will save their money for other things; and (c) that the supply of fuels will be enhanced from sources that were not economical at lower prices, or through new technologies that are economical now that fuel savings are worth more. (Whether this is the same or a different use of the term “efficient” is a little intricate and needn’t be resolved here.)

If the decision is whether to let the price of fuel go up or instead to impose price control, to subsidize imports, or to reduce demand by denying specific uses, we have a dilemma, a tradeoff. We can hurt the poor (and many others in all kinds of special categories that are especially dependent on fuel) by making them spend more for the fuel they need with less left over for other necessities,

or we can spare them that hardship while pricing fuel in a way that encourages waste and discourages conservation and new supplies. Here we are again weighing “equity” against “efficiency.” An inescapable dilemma? Nothing to do but compromise, with strongly divided interests in compromising between the energy-efficient end of the scale and the hardship-minimizing end?

To the rescue we bring the two-dimensional approach. We have two problems. We can call them the energy problem and the poverty problem. They may turn out to be an efficiency problem and an equity problem, but our object is to avoid that. Like a Supreme Court that shies from constitutional questions if it can settle a case on other merits, we try to resolve the competing claims of poverty and energy without choosing sides between equity and efficiency. The way we do this is to recognize that, although we have two objectives or criteria or competing claims, we also have two sets of instruments for coping. We have an energy problem and a poverty problem; we have an energy program and a poverty program. With two programs to work with, and two objectives to meet, we may be able to evade the ethical dilemma.

All we need technically is a way to identify the poor (and the otherwise deserving) who would suffer severely with higher fuel prices, estimate what they would lose in the higher prices, and give them an income subsidy. Not easy, but not terribly difficult. No program is perfect in targeting help to *all* of those and *only* those who are intended to receive it. But compared with holding down the price of natural gas—while fending off all the customers who want cheap gas but cannot be accommodated, and discouraging exploration for new supply, letting rich and poor alike enjoy the cheap gas as long as they are among those lucky enough to be old customers, with the rich getting proportionately more benefit because, being rich, they can buy more of everything including gas—a combination of higher gas prices and a separate compensatory program targeted on the not-rich, or on the poor, or on the very poor, can easily be a superior policy.

It will be opposed of course by those who benefit from cheap fuel who could not put forward a legitimate claim under a poverty program.

It will also be opposed by the poor or their representatives if they have learned through experience that the principle of split-

ting the problem into two parts is sometimes an excuse for relieving the one part from responsibility for what happens to the poor while neglecting the second part that was supposed to take care of them. (Having separate congressional committees deal with energy pricing and with programs that compensate the poor makes it appear that if the energy committee doesn't protect the poor there is no assurance that another committee will.)

But again we may have transformed an ethical problem into a political problem.

We may also have run up against another ethical problem. This one did not reveal itself in the original formulation. If we have money to compensate the poor, why compensate only the poor who are worse off on account of the rising prices of fuel? Specifically, suppose we put a 50-cent tax on gasoline and dedicate a fraction of the proceeds to offsetting the cost increases to families whose income is below the bottom quartile. As a way to buy off the poor's opposition to the tax, concentrating assistance on those and only those whose poverty will be aggravated by the tax can be shrewd politics. But once we have the tax and a source of revenue to help the poor in proportions determined by their dependence on fuel, somebody will propose that there are people in the bottom 10 percent who were *already* poorer, before the tax, than a lot of low-income people after the tax. The family with \$8,000 that has burned eight gallons of gasoline per week stands to lose \$200 a year from the 50-cent tax and fall to \$7,800, while the elderly couple that has no car and lives on \$6,000 qualifies for no gasoline bonus. The poor family that paints its modest home and finds the cost of paint up \$200 might prefer that the gas tax revenue help all the disadvantaged, not just those who burn gasoline.

This looks like an ethical issue, and not the one we started with. It reflects our political system. Our system recognizes that there are some poor and otherwise disadvantaged and deserving people who should receive help. But instead of dealing with their needs in a unified way, deciding how much we want to help, we tend to help the poor a little in each of many different and uncoordinated things we do. We help with food stamps and medical care and subsidized housing, and we invoke hardship in programs to keep farm prices up and rents down. This piecemeal approach does not necessarily do a bad job, but it does create repeatedly that ethical

dilemma that arose out of our compensatory programs for gasoline and heating fuel.

If a family loses its rent-controlled apartment, because rent controls are eliminated or because the apartment is eliminated, and if taxes are raised on all rental apartments and some of the proceeds set aside to help the disadvantaged, do we help only those disadvantaged by loss of rent-controlled apartments? Or do we help whoever is most in need of help?

### **The Market Ethic**

Nothing distinguishes economists from other people as much as a belief in the market system, or what some call the free market. A perennial difficulty in dealing with economics and policy is the inability of people who are not economists, and some who are, to ascertain how much of an economist's confidence in the way markets work is faith and how much is analysis and observation. How much is due to the economist's observing the way markets work and judging actual *outcomes*, and how much is a belief that the *process* is right and just? (Or right, if occasionally unjust; or right, and justice is indeterminate.)

The problem is compounded because some economists do identify markets with freedom of choice, or construe markets as processes that yield returns that are commensurate with an individual's deserts. A conclusion that arises in the analysis of a perfectly working competitive market is that people who work for hire are paid amounts equivalent to their marginal contributions to the total product, to the difference it makes if one's contribution is withdrawn while the rest of the system continues. An ethical question is whether one's marginal product constitutes an appropriate rate of remuneration. Critics of the theory, however, typically direct their energies toward the empirical issue, arguing that actual markets work differently. Nevertheless, there are economists who have given considerable thought to the matter who find that a system that distributes the fruits of economic activity in accordance with marginal contributions, be they contributions in effort or ideas or property, is ethically attractive, and others who have given considerable thought to it and find that such a system has great practical merit but little ethical claim. Most of these others believe there is a need for policies to readjust the results.

There is even an important socialist school of market economics, pioneered by Abba Lerner and Oscar Lange in the 1930s, that asserts that pricing in a socialist economy should mimic the pricing of a perfectly competitive free market, that such an economy would be least wasteful of resources, and that extramarket income transfers should compensate for any results that one does not like.

And there is a large body of professional opinion among economists, perhaps more among older than among younger ones, to the effect that markets left to themselves may turn in a pretty poor performance, but not nearly as poor when left alone as when tinkered with, especially when the tinkering is simplistically done or done cleverly to disguise the size and distribution of the costs or losses associated with some “innocuous” favoritism.

Whether or not an economist shares the ethic or the ideology that values the working of the market system for its own sake (or that identifies it not only *with* personal freedom but *as* personal freedom), most professional economists accept certain principles that others, if not the economists themselves, would recognize to have ethical content.

An example is incentives. Economists see economic incentives operating everywhere; they find nothing offensive or coercive about the responses of people to economic opportunities and sanctions; they have no interest in overcoming or opposing incentives for the sake of victory over an enemy; and they have a predilection toward tilting incentives and augmenting and dampening and restructuring incentives and even inventing incentives, to induce people to behave in ways that are collectively more rewarding or less frustrating. You can usually tell an economist from a noneconomist by asking whether at the peak season for tourism and camping there should be substantial entrance fees at the campgrounds of national parks.

A related touchstone of market economics is the idea that most people are better at spending their own money than somebody else is at spending it for them. Sometimes this is directly elevated into an ethical principle: the consumer's right to make his own mistakes. But usually it is simply that giving a poor family a shopping cart filled from the shelves of a supermarket is not as good as giving them the money and the cart and letting them do their own shopping. The idea is that *they* will get more for *your* money if *they* get to spend it. A given amount of your money will

do more good for the family from the family's point of view if it is spent the way they want it spent.

Economists have a long checklist of exceptions to this principle, exceptions from the point of view of that family's welfare and from other points of view, but generally the economist thinks the burden of proof belongs on those who want to give food stamps or subway tokens or eyeglasses to the poor and the elderly, not money. Proof may not be hard to come by; but the burden, for most economists, should be on those who don't trust the efficacy of money. It often sounds like an ethical principle. Maybe it is.

There have recently been proposals to compensate poor families in cash for the exact amount by which their heating bills, at deregulated prices, exceed what the same amount of fuel would have cost at regulated prices. The question was raised why they shouldn't merely receive, unconditionally, an amount of money estimated in advance by that formula. The retort was that, being poor, they couldn't be trusted to spend the money on heating fuel. They might spend it on something else!

This is the point at which most economists can only shake their heads slowly.