

1990

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Recommended Citation

Richard A. Posner, "Law and Economics Is Moral," 24 Valparaiso University Law Review 163 (1990).

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LAW AND ECONOMICS IS MORAL

RICHARD A. POSNER*

Thank you Dean Bodensteiner, Mr. Henke, Professor Malloy, ladies and gentlemen. It is a great pleasure to be here. My real name is Doctor Frankenstein. I am very proud of my monster and I hope to say some words in defense of him. Actually, the differences between Professor Malloy and me are, I think, largely semantic. And the semantic differences are rooted in an aesthetic one. Some people like to talk in moral terms—like to use a moral vocabulary. They like to denounce slavery, and the Nazis, and the Ku Klux Klan; it makes them feel good to denounce the causes, the organizations, the activities, and the ideologies of which there are, after all, no present-day defenders in respectable society. That to me is not a very interesting activity. I find it more interesting to explore the ambiguities in these terms. What exactly do you *mean* by slavery? Is it really the case that slavery is always and everywhere immoral?

I am going to say four things, and I hope they will serve adequately as my side of this debate. First, I am going to offer you my view of what Adam Smith stands for. Second, I will explain what I stand for or think I stand for. I will then show how wealth maximization—the Frankenstein monster—fits in to what I will be saying about Smith and about myself. I will close, if time permits, by taking some whacks at natural rights.

There are two intellectual dimensions to Adam Smith that have ensured his historical significance. The first is his opposition to mercantilism, and the second is his discovery and articulation of the invisible-hand mechanism. Mercantilism, which was the dominant economic ideology of the eighteenth century, is the view that a nation's proper objective is to maximize its gold reserves. This is done by trying to maximize exports, by conquests, and by other ways of getting foreigners to buy your goods, while minimizing your own imports so that you have a positive balance of trade and foreigners have to give you gold because you are selling them more

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goods than you are taking back. Mercantilism struck the leaders of eighteenth century European nations as the self-evident way of maximizing a nation's welfare. Adam Smith showed that, in fact, it had the opposite effect. It tended to impoverish a nation; a nation with a positive balance of trade was manufacturing goods for consumers in other countries and getting in return a largely worthless hunk of metal. There is still great mercantilist sentiment in the countries of the world. It is an important factor in American public policy. It is behind a lot of the hysteria about our negative balance of trade, and behind pressures for restricting imports. It is fueled, this mercantilist policy, by the self-interest of particular economic groups—for example, workers and employers in declining American industries. Adam Smith was intensely conscious of the element of self-interest in the mercantilist philosophy—not the self-interest of the citizenry as a whole, but the self-interest of particular manufacturers and workers. Mercantilism implies a *dirigiste* state—a powerful central government that regulates trade, has a large army and navy, and generally throws its weight around internationally. Adam Smith was hostile to all of these things and in consequence was hostile to large government. He was a small government man. So number one is Adam Smith's anti-mercantilism and corresponding hostility to governments, which he recognized as frequently the captives of special-interest groups. Second, and from a scientific standpoint more interesting, is Adam Smith's demonstration that economic activity can be coordinated without central governmental planning and regulation. This is the invisible hand—the equilibrium of independent producers and consumers that ensures, for example, for a vast city like New York, a daily supply of all the products that people purchase there without any government going around and placing orders and directing producers and transportation companies, grocers, etc., to make sure there is enough milk, enough coffee, enough scallions, and so forth, every day for New York consumers. In showing this Adam Smith was providing a complementary demonstration to his opposition to mercantilism, because he was showing not only that big government was a bad thing but that small government was entirely feasible and was consistent with a smooth-running economic system coordinated through the free market. There is a Newtonian cast to Adam Smith's invisible-hand portrait of the economy, a balance that resembles the balance among all those heavenly bodies which somehow are kept the right distance from each other by the equilibrium of opposing centripetal and centrifugal forces. Adam Smith, like most other eighteenth century intellectuals, was suffused with the type of thinking that had been responsible for Newtonian physics.

The demonstration that mercantilism is wealth minimizing, and the demonstration that an economic system can operate without central direction, are, I think, the basic contributions of Adam Smith to economic thought and public policy. He made a number of other economic points that

remain of enduring importance; there is also, as Professor Malloy suggested, a great deal more to Smith than economics. He was a distinguished moral philosopher, and he also wrote on jurisprudence. He was a Scotsman, with some typical Scottish qualities such as hostility to ostentation. All these veins of thought are in Smith's writings. In the diversity of his interests, as well as in the specific form of his economic thought, he again resembles Newton, who as many of you know had a profound interest in theology and also in astrology. We do not think that the meaning of Newtonian physics is inextricably entwined with Newton's theological and astrological views. We can similarly distinguish Adam Smith's contribution to economic science from his moral, philosophical, and ethical views. Whether they are right or wrong, they are not organic to the durable part of Adam Smith's thought, the part that has shaped not only modern economics in the scientific, the descriptive, sense, but also the modern free-market position that is hostile to mercantile policies—hostile to tariffs and the like.

To ask whether if Adam Smith were alive today would he support this or that view seems to me utterly fatuous. Adam Smith lived 200 years ago, the product of enormously different historical circumstances. If he were alive today he would have 200 more years of experience and he might have forgotten what he knew so clearly in 1776. The game of taking famous dead people and listing them on your side in current debates over public policy is, I have come to think, a chump's game, whether you do it with the founders, or, as some years ago a professor did to Justice, now Chief Justice, Rehnquist, with Herman Melville, author of (among other great works) *Billy Budd*. The implication of the attack was that if Herman Melville were alive today and writing about law, he would cast Chief Justice Rehnquist in a villainous role. We do not know how people who are the product of different cultures would think about our current problems. This by the way is one of the decisive objections to originalism in constitutional interpretation. We just do not know what people like Hamilton and Madison would think if they were alive today. To ask what Hamilton would have thought of "Dial-a-Porn" just is not a very fruitful exercise.

So let us put Adam Smith aside and talk about me. I will give you my credo. I consider myself to be a pragmatic economic libertarian. Let me explain those words, taking them in reverse order. By libertarian, I mean someone who believes in minimum government—as little government as possible. I mean someone who is suspicious of public intervention, who thinks that people should look to themselves rather than to their government for their happiness, their future, their success in life. I mean a practitioner of *laissez faire* in a general sense, not in a literal sense. I mean a small-government person. That to me is what a libertarian is, although, as Professor Malloy has explained, libertarians come in all stripes and some would not consider me one of them.

The reason I affixed the adjective “economic” is not that I am protective only of economic liberty—in fact, I do not see any sharp distinction between economic liberty on the one hand and personal or political liberties on the other hand—but that I use economic theory to try to figure out what the appropriate boundaries of the minimum state are. Basically my view is that the role of government is to intervene and correct, the best it can, serious market failures. I will give two examples. First, when people engage in a career as thieves they obviously do not consider the costs they impose on the victims of their crimes, costs to the rest of society, costs to the taxpayer, costs in self-protection—in alarm systems, locks, and all the rest. This kind of inconsiderate conduct that imposes costs on other people provides an apt occasion for governmental intervention. Indeed, the prevention of private aggression within the country, and the protection of the country from foreign aggressors, constitute the core governmental functions and define a truly minimum government, what is sometimes called the “nightwatchman” state. There are also more subtle forms of market failure that provide occasions for government intervention. One of these is the general area of education. Suppose there is a promising child—intelligent, energetic, and so forth—but the child has very poor parents. It would not be feasible for the parents or the child to finance the child’s education by promising to pay the financier out of the child’s future earnings. The enforcement of such a promise would lead us into a system of slavery (for what if the child defaulted?). Because of these difficulties, it is very hard for society to realize the economic potential of children without some public intervention for education. This does not necessarily imply public schools; education may be as well or better furnished through a system of subsidized private education. Government intervention appears to be indicated here for the additional reason that education confers benefits on more than the recipient. Educated people make it easier for others to transact with them.

My third term, pragmatic, comes from my opening remark about not being enthusiastic about moral discourse. I do not derive my economic libertarian views from a foundational moral philosophy such as the philosophy of Kant, or Locke’s philosophy of natural rights, or utilitarianism, or anything of that sort. I regard moral philosophy as a weak field, a field in disarray, a field in which consensus is impossible to achieve in our society. I do not think it provides a promising foundation for a philosophy of government. You can if you want describe wealth maximization or libertarianism or laissez faire as moral philosophies. My point is only that I do not intend to try to derive my free-market views from something more fundamental, more rigorously philosophical. And the consequence of this lack of foundations is that I am not dogmatically attached to any of my free-market views. I do think the minimum state defined by the economic analysis of market failure is the state that works best to achieve the common goals of most people in the world. I think that in the disintegration of the commu-

nist states and the failures of socialism in a variety of noncommunist countries such as Argentina, Israel, France, and Greece, we find strong pragmatic support for the concept of limited government—as we do also in the failures of many of our own social programs, the experiments of a free society. But if you can show me that socialism really works well and achieves more of what most of us want than capitalism, then I shall be happy to give socialism a close look.

How does wealth maximization fit into the picture that I have presented of Smith and of myself? It is merely a way of operationalizing, of making concrete, the idea of economic libertarianism. It is an analytic tool. What it does primarily—and that is one of the things that disturbs Professor Malloy—is strip away distributive considerations. It strips away the complications introduced in public policy analysis when you think of dollars as being worth different amounts, in some ethical sense, depending on who has each dollar.

I will give you an example of how a distributive consideration—the attempt to weigh dollars according to who holds them—complicates public policy analysis, and how wealth maximization provides a cleaner approach. The example I will give is monopoly. If you have studied antitrust or cognate fields you know that the technique of monopoly is to restrict output, for by doing so the monopolist drives up market price. The monopolist thus creates an *artificial* scarcity of his goods. The result of raising price over a smaller output is to increase the profits of the monopolist, and of course to reduce the wealth of consumers because they now have to pay high prices. There is thus a transfer of wealth from consumers to the monopolist producer or the cartel of producers. If you ask what is the public policy significance of this transfer of wealth you quickly get into what I regard as essentially insoluble problems in the interpersonal comparison of worth or desert. Should consumers be wealthier than producers? Who are these consumers? Maybe they are the idle rich and the goods they are buying are luxury toys for the rich. The producers perhaps employ worthy poor people to manufacture these baubles. Maybe it is a good thing that wealth is being redistributed from these consumers to producers; or maybe not. Maybe the consumers are poorer, and maybe poorer people deserve some break relative to the rich. That is a complicated subject—how we decide how income should be equalized. It is the socialist prescription, which Professor Malloy is rightly troubled by. But the economist looking at the monopoly problem will tend to say, let us forget about the transfer of wealth from consumers to producers. Let us treat a dollar as worth the same in the hands of the consumer as in the hands of the producer. So the impoverishment of the consumer by the monopolist is offset by the enrichment of the monopolist. Let us forget about that. There is still a very serious objection to monopoly. When the monopolist creates his artificial scarcity of goods, some consumers continue to buy the monopolist's product at a higher price, but others

are deflected to substitute products. They reconsider the alternatives to the monopolist's product now that that product is more costly. Some of them will substitute one of the alternatives. The alternatives, however, look attractive only because the monopolist is charging a high price. If the alternative products are being sold by competitive producers, the cost to society of producing these goods may be higher than the cost of the monopolist's good. So one has an inefficient reallocation of resources; consumers' wants are satisfied at higher overall social cost. In addition, if you allow monopolization—if you dangle this pot of gold consisting of monopoly profits in front of sellers—they will invest resources in becoming monopolists. These resources (other than those devoted to obtaining monopoly by innovation or other means that benefit consumers) are like the resources that thieves invest in their burglar tools and way of life: they are sterile investments, made to effect redistributions of wealth. So, as I say, even if you abstract from all distributive considerations and you consider that sellers are as good as consumers and money in their hands is worth the same as money in the consumer's hands, you can still have an economic argument against monopoly, an argument for government intervention, and I think a more powerful argument precisely because it abstracts from highly controversial distributive considerations.

It is the same in the accident field. There are a number of colorful nineteenth century cases involving damage to crops caused by fires set by locomotive sparks. The question for law was, how to adjust this destructive interaction between railroads and farmers? One answer is to look at the cost that these railroad fires are inflicting, the costs in burned-up crops, and then see what it would cost if railroads were induced by the threat of tort liability to purchase spark-arresting equipment. If the spark-arresting equipment would cost less than the expected damage to crops, and also less than the cost to the farmers of growing fire-resistant crops or of not using their land at all, then we would say, well here is a case for government to intervene and maximize social wealth by imposing liability on the railroad. That is our tort system in a nutshell.

Now it is easy, as one casts one's mind across the entire range of public policy issues from a wealth-maximization standpoint, to find areas of uncertainty. Should a state pass a law requiring motorcyclists to wear helmets? As a first approximation, the wealth maximizer might say that if the motorcyclist falls on his head and breaks it, the harm is to the motorcyclist himself and he can balance that harm against the cost of buying a helmet. But in the second round of analysis one may wish to point out that many of the medical costs of American society are paid for today by government through the medical tax deduction, through Medicaid and Medicare, and hence, are not fully financed by the beneficiaries of medical care. So some of the costs of this injured motorcyclist will in fact be borne elsewhere. These are external costs analytically similar to that imposed by thieves. So

maybe there is a case for government intervention. But on the other hand, maybe to intervene continually in order to correct previous interventions is wrong. Maybe what we really need is a system of medical care that makes people pay for their own care. If you pay for your own injuries there is no reason as a matter of wealth maximization to forbid you to behave in a self-destructive fashion.

The point I wish to make is that once you abstract from controversial issues having to do with the distribution of wealth and the appropriate role of paternalism in government decision making—once you focus on the allocative effects of government policies—you have a powerful analytic tool with which to derive a system of optimal government, a system more limited than what we have, though more extensive than the classical *laissez faire* state urged by the nineteenth century English economists. But is the system that one comes up with immoral? In the passages from *The Economics of Justice* that Professor Malloy quoted and in much else that he could quote from my writings, I have wrestled with this issue and I have pointed out, not by way of reluctant concession but in a curious and concerned spirit, that the unflinching pursuit of wealth maximization will indeed lead to results that would be widely regarded as immoral or, at the least, highly controversial. One of these that is very much in the news is surrogate motherhood. In the first round of analysis, which is not likely to be the last round, the wealth maximizer sees in surrogate motherhood a contract between willing buyers—the father-to-be and his wife—and a willing seller, the woman who agrees to be the surrogate mother, to carry the fetus fathered by the husband to term and then give the child up to the father and his wife. Now clearly in the enforcement of such a contract there are substantial issues that a wealth maximizer would be concerned with. For example, should specific performance be used to enforce these contracts? But with regard to the basic issue, the propriety of the contract, it strikes the wealth maximizer as a perfectly sensible, because wealth-maximizing, arrangement. There are many couples in which the wife is infertile yet the couple want to have a child. And there are many women who, for a price, are willing to bear a child for another couple and give it up to them upon birth. Although there have been of course some famous controversies arising from surrogate motherhood—the most famous being the *Baby M* case in New Jersey—in fact most surrogate mother contracts are carried out uneventfully and everybody seems to be happy. So the wealth maximizer is apt to say—I would say—that surrogate motherhood is fine. But if you go a few steps beyond that—if you ask, for example, whether people should be able to sell babies—the analysis gets trickier. Suppose a woman conceives by accident and carries the baby to term and does not want to keep it. Should she be allowed to charge a price if people want to adopt it? I think this is a form of transaction that would be wealth maximizing and would repair a serious imbalance in the supply and demand for babies for

adoption. We have in this country an enormous production of illegitimate births and, on the other hand, a terrible shortage of babies for adoption. This is clearly a disequilibrium, and it results in part from refusing to allow an explicit trade in babies. But this proposal is so disturbing to people, so shocking, that I have never advocated baby selling beyond an experiment that would consist of allowing adoption agencies to take a portion of the fee they charge to adoptive parents and pass it on to pregnant women as an inducement to the women to carry their fetus to term rather than have an abortion. With an experiment like that, we might test the depth of the moral concern in baby selling. But I do not deny that there *is* that moral concern, and I do not suggest that wealth maximization *should* override it. And similarly with the quotation Professor Malloy gave about racial exclusionary zoning. It would be possible in a system unflinchingly dedicated to wealth maximization to come up with results that would be deeply, perhaps universally, offensive. That obviously would and should give one pause.

What I have particularly emphasized in my writings and what Professor Malloy has not mentioned at all is that wealth maximization is an especially useful tool for guiding common law adjudication. I gave you the example of locomotive-spark cases. We can think more systematically about contract law, property law, tort law, and the branch of criminal law that comes down to us from the common law, in wealth maximization terms. Judges are reluctant to get enmeshed in distributive controversies, see prosperity and efficiency as relatively neutral social goals and ones within the judicial capacity to implement, and therefore, I think, consciously or unconsciously focus their efforts on trying to achieve efficient adjustments in these areas.

As Professor Malloy emphasized, the wealth maximization perspective is particularly disturbing to people who have a strong sense of natural rights. The whole economic vocabulary is so removed from considerations of natural rights that it seems the economist must be missing something fundamental. I do not question the depth of moral sentiment in areas where that sentiment may be opposed to efficient solutions to social problems. But I do deny that natural rights provide a coherent, cogent, sensible, alternative method of framing questions and of public policy. The natural rights view that Professor Malloy alludes to and that I think remains most influential in current natural rights thinking in American law is the view of natural rights that comes from John Locke. It starts from the notion that before there was society, when people were in a state of nature, they had a natural liberty to do what they wanted, and that society should be viewed as a compact in which people surrender just so much of their own liberty as is necessary to protect the equal liberty of the other people in society. For Locke, the social contract imagined in such a way leads to the minimum nightwatchman state, basically a police force. But in modern thinking, theorists often will expand the range of natural rights, as Professor Malloy at-

tempted to do, and come up with a larger conception of the state. On the other hand, Professor Richard Epstein, whom Malloy mentioned, uses the Lockean view to derive a sense of minimum government smaller than even I think appropriate.

I do not think natural rights talk really gets anywhere at all. It is extremely porous. Almost any public policy, however interventionist, socialistic—what have you—can be justified in natural rights lingo. For example, if we have a substantial program of redistributing wealth to the poor financed by progressive income taxes, we could call this basically a police measure designed to keep the poor quiet. This is like paying for police, and since the rich have most of the property they should pay most of the cost of any general police measure. Almost every socialist nostrum can be defended as the sort of police measure that, within a Lockean system of natural rights, is a proper function of government.

Natural rights theory also, although often embellished in democratic jargon, is fundamentally anti-democratic; it greatly curtails the role of democracy and representative government. The more rights people have, the less the scope for the people's representatives to deliberate on public policy issues. In some versions of natural rights theory, where the scope of government and the activities of government are highly predetermined, there really is no role for democratic debate except to pick the individuals to administer the machinery of the state. The machinery itself is determined by the natural rights theory. You have to have urban renewal or you cannot have urban renewal, or you have to have a large army, or you have to regulate television or cannot regulate television. If you decide exactly what you have to have, and what you cannot have, in government, there is very little left for elected officials to do.

Third, I do not think nature in fact is an important source of human wealth and welfare, and therefore it is difficult to criticize government when it takes something away that we had in nature. In nature we were glorified monkeys running around and throwing stones at each other. The wealth of society is a function of social interaction, making it hard to have a "natural" benchmark for the allocation of rights. Slaves in society are better off than free people in the state of nature.

And fourth, and most basically, I do not know why natural rights or nature *should* be the benchmark for answering public policy questions. Why nature? Locke had religious reasons for believing in natural rights. He was a devout Christian and much of his work is actually devoted to the exegesis of the Bible, from which he got many of his views. Adam Smith was not a religious person, and although there is natural rights talk in Adam Smith, it does not appear to have any theological source.

So natural rights as a concept seems to me to be porous, groundless,

perverse in many ways, and basically useless; natural rights talk in the concrete is sentimental, contradictory, and also pretty useless. Professor Malloy said, for example, that slavery is wrong *in all circumstances*. It is easy to say things like that. We do not have slavery in the United States. We do not have a big slavery lobby. If you denounce slavery in the United States, you are on pretty safe ground. I happened to read recently the graduation address of the president of Yale University. He said you young people going out into the world would have to deal with very difficult problems, show a lot of moral courage, and therefore he wanted to address a significant moral question. This turned out to be American Negro slavery, and he talked about what a terrible system it was. He gave many examples. Everything he said was right, but to use that as the touchstone of a lecture on moral courage seemed very dubious to me, since there was no one in the audience, no one in Yale University, indeed no one in the United States as far as I know, who wishes to restore slavery. But when one speaks of slavery as being wrong in all circumstances one betrays a historical naïveté and a semantic simplicity. One can easily point to historical circumstances in which slavery was not wrong, slavery was an improvement. If you go back to the earliest times of human warfare, you will find that the practice of the victors was to kill the captives whom they took in battle, and if they were lucky enough to conquer an enemy village or an enemy state they would kill the entire male population and take the women as concubines. Then someone had the bright idea of putting captives to work rather than killing them. When slavery took the place of genocide in warfare, that was a moral advance.

What is true is that slavery is abhorrent in modern society for a wide variety of reasons, and indeed in the society we have had for the last several hundred years, including the period when we had slavery in this country. But what is slavery? Slavery is the name for forms of involuntary servitude that we disapprove of. There is plenty of involuntary servitude; if we approve of it, we just do not call it slavery. We do not say, for example, that children are the slaves of their parents. We do not say that prisoners who are forced to work in prison are the slaves of the United States. (There are, in fact, almost a million people in American jails and prisons today and many of them are required to work.) We do not say, well in America we do not have as many slaves as we did in 1860, but we have several hundred thousand slaves. When people volunteer for Army duty, even in peacetime, they are not free to leave at will; they are subject to involuntary servitude. So it seems that while you can say, and you can feel good saying, that slavery is always and everywhere bad, and wrong, and evil, the truth is that many forms of involuntary servitude are approved in our society and all societies, and there have been times when far more extensive forms of involuntary servitude were moral advances.

There is a reason why people who like a moral vocabulary are prone to focus on cases, like slavery, as to which there is a moral consensus. The

reason is that when one gets to contested moral questions the power of moral discourse runs out. When one talks about abortion, or when one talks about welfare rights, or when one talks about the appropriate provision for the retarded, or when one talks about surrogate motherhood, or affirmative action, or any one of a dozen other highly controversial moral issues, moral discourse turns out not to provide any sort of solution to these problems. It merely provides a vocabulary in which people can express views that have deep emotional roots. While I do not deny the force of those views and I do not deny that government policy makers should take them into account, I do not think they are analytically fruitful. Wealth maximization is analytically fruitful and I think it has a large, although not an unrestricted, domain of application to law and to public policy in general. Thank you.

