THE ENVIRONMENTAL ETHICS AND POLICY BOOK

Philosophy, Ecology, Economics

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ECONOMICS, ETHICS, AND ECOLOGY

V.A Letting the Market Decide

34. PREVIEW

> The way to make money is to buy when blood is running in the streets.
>
> *John D. Rockefeller*

> Darwin's theory of the struggle for existence . . . has . . . been cited as authorization of the encouragement of the spirit of competition. Some people also in such a way have tried to prove pseudo-scientifically the necessity of the destructive economic struggle of competition among individuals. But this is wrong.
>
> *Albert Einstein*

Many people probably share the sentiments of two writers who, in commenting on the despoliation of "our natural heritage" and the poisoning of the environment with the use of pesticides, stated that "although it is obvious that what we are doing is wrong, it is by no means obvious what would be right."[1] Indeed, the perplexities are deep. There is disagreement about whether certain practices are wrong, what proper policies would be, and, importantly, the grounds for deciding such matters. As noted in the "Introduction to Ethical Theory" and in Part III, one source of dispute concerns what sorts of things have moral standing. Even if that difficult question were resolved, there are other sources of perplexity. Although the following suggestion deserves critical reflection and continued reassessment, one way of categorizing competing approaches to deciding an important range of environmental disputes is to divide them crudely into (1) those which assume that the mechanism of the marketplace is the proper means of determining both the allocation of resources to different productive uses and the distribution of benefits and burdens across the relevant populations, and (2) those which assume that these matters should not be left much, or at all, to the contingencies of the marketplace (that is, certain matters should be decided politically and certain protections or constraints on the market must be politically enforced in order to avoid certain failures or abuses to which unconstrained markets lead).

We need to think about the effects of the market mechanism on the environment and assess the arguments for claiming that the environmental effects of the market mechanism are tolerable or desirable. Markets, of course, existed long before economists or ecologists did. A major source of defense of the desirability of the market mechanism comes, however, from economists. For this reason and because economists, more than any other group of social scientists, have explored environmental issues in considerable detail, it is important to identify and examine some fundamental strands in economic theory and also to see how economists tend to approach particular current problems, such as pollution, species extinction, or the question of whether we should save for the sake of future generations. "Economic reasoning"—indeed, the economic point of view—is extremely influential in policymaking and, for a number of reasons, inviting. Shortly we shall note a number of objections to orthodox economic theory; first, however, we should make it quite clear that economists deserve special praise for paying careful attention to consequences and to related tradeoffs. In short, the "economic approach" is sensitive to particular facts, it is specific, and it suggests a method for resolving questions of tradeoffs between competing and valued ends. The economic approach seems, then, "practical," "hard-nosed," and "realistic," and its use of precise, formal modes of quantification and calculation is alluring.

In recent years there has developed a more concentrated effort to identify the points of agreement and disagreement between economic theory, ethical theory, and the outlooks of ecologists. This effort (of which some essays in this book are examples) promises to be an important and revealing one for developing an adequate view of our environment and a reasonable approach to setting policy on environmental matters. Here we have room to touch on only a few central matters.

On the one hand, markets seem terribly useful. They provide us (or many of us) with all sorts of goods, including decent shelter, nutrition, medical care, and transportation—some "items" that few fail to value. In a decentralized fashion, without the (maligned) "government bureaucrats" deciding for the rest of us, the market allocates resources to myriad productive functions and provides a mode for distributing benefits (as well as the burdens of work, risk taking, and so on). That the market mechanism produces all sorts of wonderful results is not subverted by the disdain we may rightly feel for certain insipid, tasteless, or defective products that it also generates. Sometimes one person's junk is another's treasure; sometimes it is just another's junk as well.

The main defense of the market mechanism appeals to the value of efficiency; it can be characterized as follows. In the best, perhaps idealized, case, two parties, for example, are mature, have settled preferences, are well informed, and with no undue pressure or misrepresentation agree to exchange goods or services. Perhaps one agrees to paint the other's house in exchange for an old car. One values the car more than the labor effort the other must make, and the other values having her house painted more than the car. After the exchange, both are better off. Other things being equal, the welfare of each is enhanced, and their respective utility levels are raised. Thus, the sum of (their) utilities is increased; alternatively, even if utilities cannot be summed (there is a dispute about this issue, and many economists since the 1930s "ordinalist" revolution deny the possibility), we may conclude that overall utility has increased if the judgment of all the affected parties is affirmative (and credible). The pretrade situation was one in which at least one of the two could be better off and no one worse off. It was, in the technical sense in which economists use the term, an *inefficient situation.* The posttrade situation is more efficient. Someone has become better off, and no one is worse off. Is efficiency valuable in itself? The answer from orthodox economic theory is no; rather, moving toward more efficient arrangements is viewed as desirable because to do so is to increase the total utility or welfare (to take a step toward "maximization of total net expected utility," to put matters more carefully). To understand the argument for adopting or perpetuating the use of the market mechanism, it is crucial to note these assumptions—ones that too often are in the background and that, hence, frequently escape scrutiny and moral appraisal.

To highlight some crucial assumptions and to emphasize which values or principles are being treated as basic, or alternatively, as derivative ones, it is useful to set out certain elements of economic reasoning more explicitly and systematically. Typically, what is implicit is the anthropocentric view that all and only humans morally count; thus, only benefits (utilities) or harms (disutilities) to humans have weight in evaluating actions or policies. For example, consider this representative remark: "To assert that there is a pollution problem or an environmental problem is to assert, at least implicitly, that one or more resources is not being used so as to maximize human satisfactions."[2] Thus, what is conceptually to count (for example) as pollution, directly or indirectly, must involve harm to humans; if penguins are poisoned by an industrial chemical but no humans (now or in the future?) are affected, that is not "pollution" (or, at least, morally significant pollution). Somewhat representative of this view are the remarks of economist William Baxter:

> My criteria are oriented to people, not penguins. Damage to penguins, or sugar pines, or geological marvels is, without more, simply irrelevant. One must . . . say: Penguins are important because people enjoy seeing them walk about rocks. . . . I reject the proposition that we ought to respect the "balance of nature" or to "preserve the environment" unless the reason for doing so, express or implied, is the benefit of man. Every man is entitled to his own definition of Walden Pond, but there is no definition that has any moral superiority over another, except by reference to the selfish needs of the human race.[3]

To make an important point briefly, if the anthropocentric assumption embodied in traditional economic theory is indefensible, then the theory as it stands is unacceptable—as would be a theory that regarded only benefits and harms to white people as having moral significance. A theory that is not anthropocentric will be a theoretically more complex one. But simplicity is not the sole determinant of rationality.

The modern economic approach also assumes and accepts (however inexplicitly) a distribution of legally protected property rights. Often there are further implicit assumptions. For example, human beings can be owners but cannot be owned. Any nonhuman can be owned. This view reflects the anthropocentric criterion of moral standing. Legal property in an object X is best understood as possession of a package of rights over what is owned, often a right to use X, to exclude others from doing so, to authorize others to use X, to be compensated for unauthorized uses, and, sometimes, to destroy X if one wishes. There is a moral question whether anyone should have a legal right to kill (or torture) animals. The "It's my property to do with as I please" mentality implies an affirmative answer. The main point here, however, is just that orthodox economists typically assume the moral legitimacy of *some* set of well-defined property rights. (On these matters see Section V.C, "From the Commons to Property.") Further, it is assumed that these rights will foster certain sorts of exchanges, for example, voluntary, nonfraudulent ones between competent persons. Thus, the core of the market mechanism, exchanges of goods or services (actually rights to such), is understood to occur against the background of morally acceptable norms and institutions; the latter constitute "the rules of the game" as it were.

Many economists often insist that they engage in value-free inquiry, that they are impotent (as economists) to say whether the rules are good or right. Some deny that evaluative claims are rationally decidable or are any more than expressions of emotion. For example, McKenzie and Tullock claim that "the approach of the economist is amoral" and that "as economists we cannot say what is 'just' or 'fair.'"[4] Paul Heyne and Thomas Johnson maintain that "we do not have any (means) of resolving ethical disagreements, they are ultimately judgments of value . . . and cannot finally be proved or disproved."[5] These stances are questionable (and have been explored systematically and in detail in the philosophical literature for years), but many economists seem oblivious to this fact, and to the fact that their own implicit or explicit commitment to the value of the market mechanism or to efficiency or to maximizing utility (or aggregate human want satisfaction) suggests, to the contrary, that the discipline of economics (insofar as it purports not merely to explain or predict human behavior) rests, in part, on evaluative assumptions.[6] One who thought that only benefits or harms to penguins were significant would be making an important evaluative assumption. So also does one who says, "Aryans count; Jews do not." The question, rather, would seem to be which view is rationally superior; we simply cannot avoid evaluations.

The concept of efficiency, and its assumed high value (or possibly, overriding value), is so central in economic approaches to environmental matters that we should dissect it more thoroughly. To do so requires a bit of technical terminology; one would be helpless in trying to assess the economic approach without mastery of a few concepts.

In ordinary (nontechnical) talk, there is a tendency to use *efficient* as an honorific term; thus, if X is efficient, X is thought to be good (in a respect). Conversely, if X is inefficient, X is thought to be bad (in a respect). *Given* such usage, it seems perverse to question or oppose the efficient course, and unobjectionable or "nice" to urge efficient policies. All this can mislead us, however. The term *efficient* has a technical sense in economics; further, we should distinguish (1) what it *means* to say that some state of affairs is efficient, and (2) whether efficiency is a valuable goal that we ought to pursue. And importantly, is efficiency valuable in itself or only as a means? First, we have noted, in so many words, that a standard implicit assumption is, not surprisingly, that efficiency is understood as efficiency for humans. Modern factory farms that raise veal calves may be quite efficient for humans, but hardly so, let us assume, for the calves.[7] Let us return to (1). The standard criterion of efficiency that is employed is called the *Pareto criterion* (after the early twentieth-century economist-sociologist Vilfredo Pareto). If a situation in which parties possess various goods is such that at least one party could be better off (in that party's own estimation) *without* making anyone worse off, the situation is said to be inefficient (or not maximally efficient). A "*Pareto improvement*" could be made; that is, at least one party could be better off without worsening another's situation.[8] In our earlier tale, in which one individual got another's car and the other got her house painted, a Pareto improvement was made. Voluntary exchanges are thought to generate Pareto improvements—that is, to increase efficiency. If a situation is one in which it is not possible for anyone to become better off without worsening another's circumstance, it is said to be *Pareto optimal* (or maximally efficient).[9] As noted before, the core idea is that in a more efficient situation the total welfare of the relevant parties is greater than in the less efficient one even if one is not able to say by how much. Moving toward more efficient circumstances *seems* desirable since it moves things closer to maximum utility. If, in fact, the sketched mechanism is the best means of maximizing welfares or achieving ever-increasing improvements, that fact seems to be a strong reason to employ it. Thus, the market is often defended on grounds that it best maximizes utility (quite apart from, or in addition to, appeals to implementation of, or respecting, some sort of human right to choose). Although we may give three cheers for markets as we commonly encounter them, critical reflection may make us wonder whether they deserve three, or even two. Much depends on how much we should value utility maximization, or efficiency as a means of fostering it—whether voluntary exchanges invariably or usually increase efficiency, and to what extent exchanges really are voluntary when elements of misrepresentation are often present.[10]

It is easy to overlook some crucial points. We may have serious moral reservations about even maximally efficient situations. For example, suppose that X is a master and Y is X's slave. There may be no way to alter this arrangement so that one can be better off and no one worse off. That is, it may be Pareto optimal or maximally efficient. The criterion focuses on a given situation and prospective departures from it, not on how it came about. As noted, a distribution of goods between master and slave may be Pareto optimal or maximally efficient (in the Paretian sense), but morally indefensible. In short, it seems absurd to believe that whatever is efficient is right or permissible. If so, then we must conclude that although efficiency is desirable, it only is desirable *other things being equal.*

In the exchange of an old car for the painting of a house, there was a gain from trade—both parties were better off, and aggregate welfare increased. In applying the Pareto criterion, economists typically assume that the proper way of determining whether the parties to the transaction are better off is to solicit the judgments of the parties themselves (usually post-trade). Several comments are relevant here, and all of them may reduce one's enthusiasm for thinking that the market is invariably the proper vehicle (or an effective one) to enhance social (human) welfare. First, in idealized models, the traders may possess "complete information." In fact, actual traders are ignorant to a degree (sometimes victimized by self-interested, or profit-maximizing, individuals or corporations). We may believe, prior to trading, that acquiring a widget (a product often discussed in economics texts, but hard to find) and forgoing some money may improve our lot. On getting the widget, the car, the meal, or the compact disc, we often regard ourselves as worse off. In fact, voluntary exchanges do not always (often?) yield a Pareto improvement over the preexchange situation, because one party *is* worse off postexchange. This point tends to be overlooked or discounted by some ostensibly empirical scientists.

To avoid, so it would seem, this awkward result of observing what actually happens with some actual transactions, some economists seem to stipulatively define 'voluntary exchange' as one an individual would engage in if and only if beneficial to that individual. Thus, with this conceptual sleight of hand, it becomes analytically true (roughly, true by definition) that "all voluntary exchanges benefit the parties who engage in them." But then this use of 'voluntary exchange' does not mean what most of us mean by the expression.

A brief comment may provide food for thought. We desire things *under-a-description* (at least often). Thus, Oedipus wanted to marry Jocasta. He got "what he wanted." Was he better off? He did not want to marry his mother, but since Jocasta was his mother, he also got what, in one sense, he did *not* want. The economists' model of human psychology and choice seems too simple in not attending sufficiently to complexities that result from the existence of multiple true descriptions of what one wants, self-deception, ambivalence, weakness of will, subconscious motivation, and so on.

Another feature of the market mechanism concerns *who* participates in market transactions, either small or large. It is worth observing that only those who are *willing and able* to pay have access to markets—that is, can participate in market transactions. It may not be far wrong to estimate that of the world's (almost) 6 billion members of *Homo sapiens*, at least a billion or so are unable to cast, or are radically hindered from casting, an effective vote in the economic marketplace, such as the extremely poor, the very young, the severely retarded, the seriously (mentally) disturbed. Nonhumans are not the only ones who have no say about the distribution of benefits and burdens generated by market transactions; a large number of existing humans are also voiceless in this way—not to mention future generations.

For the reasons mentioned, it is doubtful that voluntary, "informed" exchanges invariably benefit existing human participants in those exchanges. Even if they did, much of the world's population effectively is excluded from participation in market transactions. In spite of the incautious praise heaped on capitalism by some ideologues, the proper assessment of markets (and especially commercial practices and environmental effects) must involve consideration of the alternatives to a given market system. Large questions of political philosophy and economics arise that cannot be explored here. However, there are two basic alternatives to a comparatively unconstrained market system. If a given system seems intolerable in some respect, it may be possible to add a new constraint to it in order to remedy the problem. This is the alternative of setting appropriate constraints on the market. Thus, if we judge that blood (or bodily parts, or babies) ought not to be bought and sold (to the highest bidder?), we can legally prohibit the practice—and let the distribution be determined by nonmarket procedures. Similarly, if we judge that a corporation's self-interest in a good reputation is not an adequate safeguard to prevent it from selling defective products or polluting the environment, we can require governmental testing and set stringent liability rules that function as disincentives to corporate distribution of dangerous products or polluting. Defenders of the market are fond of pointing out that it is not the baker's altruism but his self-interest that makes bread available for purchase. This is no doubt true, but this same motive also can lead to industrial spying, theft of trade secrets, corporate bribery, and "coverups" of dangerous products.

We have noted some important criticisms of letting the market mechanism determine allocation and distribution questions. The alleged efficiency of the market process seems a means to maximizing utility. Utility maximization is hardly an uncontroversial goal. There are powerful philosophical arguments in favor of the view that maximizing utility allows or *requires* unjust distributions of benefits and burdens. As we have noted, to assume the value of maximizing only human utility is to beg the question against antianthropocentric counterarguments. Further, even if those difficulties were not serious, there are reasons (as noted) to doubt that all (most?) voluntary participants in market exchanges are better off as a result. If they are not, there may be no net increase in efficiency or total utility. We have observed also that much of the world's population is disenfranchised from casting an effective monetary vote in the market decision process.

In this brief survey of moral and other worries about the market, we have omitted a concern that economists rightly and increasingly have stressed in recent decades: that many parties who are not participants to voluntary, informed exchanges are made worse off as a result of the exchanges. These are what are called *negative externalities*. The focus here is on the generation of unconsented-to harms to some individuals, "costs" generated for which compensation is not paid. Thus, much pollution of the air or water is a prime example of negative externalities. Because only some of the costs to all parties are borne by the "private parties," the "social costs" exceed the "private costs." It is commonly held that if external costs only could be "internalized" (borne by those who seek to benefit from activities that generate them), there would be no problem (no moral complaint?). Thus, it is claimed that we *ought* to prevent or minimize externalities (some economists might be uncomfortable with this blatantly normative mode of speaking). How can we do that? To oversimplify, three basic alternatives present themselves: (1) persuade people or corporations or nations not to generate externalities, that is, appeal to voluntary self-restraint; (2) coerce by attaching criminal penalties to violations of publicly set standards; or (3a) coerce by attaching "taxes" or charges to each additional unit of pollution emitted beyond a certain amount—or (3b) coerce by requiring possession of legal rights to pollute and possibly allowing trading in such rights. Many economists have a sufficiently low estimate of human nature so as to dismiss (1) rather quickly. A less than rosy estimate is surely correct even if one regards the picture of people embodied in *Homo economicus* (roughly the assumption of psychological egoism and the earlier mentioned simplifications regarding motives) as a nontrivial misrepresentation of human nature.

The current debate between defenders of (2) and (3) is important, intriguing, and embodies noteworthy psychological and moral assumptions. Once more, the focus on unconsented-to harm *to others* is viewed anthropocentrically. Only harms to humans count. The English hunter W. D. M. Bell is reported to have killed 1,011 elephants in his lifetime.[11] This slaughter, if involving no unconsented-to harm to humans, fails to count as an externality needing any internalizing—according to the orthodox economic view. The term *social costs* means costs to human society. An obvious question is whether a cost–benefit accounting can be thought thorough when "costs to nonhumans" are either tacitly treated as nonsensical or recognized but treated as irrelevant. These matters are taken up in the next section.

It should not go unnoticed that many economists would object to labeling negative externalities as "instances of market failure." Instead, they would maintain that unconsented-to harms ("negative externalities," "overexploitation of resources," "pollution," and so on) result from the failure to have a market. As some have argued, the solution is to allow property rights in "resources." The "tragedy of the commons" is that "goods" that are unowned (except "owned by all") get misused in one fashion or another. Since "chunks" of air or water rarely can be partitioned off so that particular individuals have a right to them, such persons may have little (self-interest) incentive to preserve, respect, or ration consumption of such things. According to the view being considered, it is better to allow the market to operate more broadly (by creating a more extensive distribution of property rights) than to restrict the market's scope of operation. Having been somewhat negative about much in economic theory in these introductory remarks, we leave it to the reader to critically appraise this proposal—as well as the criticisms we have set forth.

The earlier quote from William Baxter, expresses, in no uncertain terms, an anthropocentric approach to environmental tradeoffs. One might question whether "maximize human satisfaction" underlies his economic viewpoint. A more qualified and cautious effort at setting out fundamental, theoretic assumptions of modern economic doctrine (such as Pareto considerations) and applying them to environmental questions (for example, what to do about pollution) is found in A. Myrick Freeman's essay (35), "The Ethical Basis of the Economic View of the Environment." It is not easy reading, but it is a rich summary and deserves careful study. That approach is often one that conflicts with alternative views; this kind of disagreement occurs in the dispute over sustainability, a matter discussed in some detail in Section V.E.

Part of the critique of "the economic viewpoint" (*actually* traditional, neoclassical economic doctrine) is set out in Mark Sagoff's essay (36), "At the Shrine of Our Lady of Fàtima, or Why Political Questions Are Not All Economic." Sagoff calls attention to where market decision making (or "the cult of Pareto optimality") has led us. He is not enamored of the resulting gas stations, tract developments, strip mines, pizza stands, beach condos, and snowmobiles in the mountains. Importantly, he questions the tendency of economists to view citizens' expressions of *ideals* (such as "we ought to preserve dolphins") as just another consumer *preference or desire*—as just another consumer vote in the economic marketplace—to be taken seriously only if backed by the willingness and ability to pay.

NOTES

1. Robert and Nancy Dorfman, eds. *Economics and the Environment* (New York: Norton & Company, 1972), p. XIX.
2. William Baxter, *People or Penguins: The Case for Optimal Pollution* (New York: Columbia University Press, 1974), p. 17.
3. William Baxter, *People or Penguins*, p. 5.
4. Richard B. McKenzie and Gordon Tullock, *The New World of Economics* (Homewood, IL: Irwin, 1978), p. 7.
5. Paul Heyne and Thomas Johnson, *Toward Economic Understanding* (Chicago: Science Research Associates, 1976), p. 767.

6. It is worth noting that moral and political philosophers and those who work in environmental ethics in particular, have some things to learn from economists in game theory, decision theory, and examination of slippery issues surrounding the notions of efficiency and utility that are of importance to virtually any environmental policy question. For example, the important idea of choosing behind a veil of ignorance, one that has been put to such creative use by John Rawls in his *A Theory of Justice*, could have been found in the work of economist John Harsanyi in the early 1950s; we do not know whether Rawls was, in fact, influenced by Harsanyi on this point.
7. See Peter Singer, *Animal Liberation* (New York: Avon Books, 1975).
8. To emphasize a point "another" is usually understood *not* to include future persons and not to consider nonhuman living creatures. Thus evaluative assumptions get made here. The desirability of efficiency so understood is hardly self-evident, but this point often goes undiscussed and undefended.
9. There may be *many* Pareto-optimal situations, and some may be, on the face of things, unjust and have been arrived at in an unjust manner.
10. Recently, for example, General Electric has offered an electric light bulb advertised as replacing a 100-watt bulb and saving money; the deal sounds attractive until one examines the fine print and learns that the "replacement" is simply a 90-watt bulb that yields less light.
11. Bell's act is reported in Cleveland Amory, *Man Kind?* (New York: Dell, 1974), p. 30.

35. The Ethical Basis of the Economic View of the Environment

A. Myrick Freeman III

I. Introduction

At least in some circles, economists' recommendations for a policy concerning pollution and other environmental problems are regarded with a good deal of skepticism and perhaps even distrust.[1] For example, when we suggest that economic factors such as cost should be taken into account in setting ambient air quality standards, we are told that it is wrong to put a price on human life or beauty. And when we argue that placing a tax or charge on the emissions of pollutants would be more effective than the pres-ent regulatory approach, we are told that this would simply create "licenses to pollute" and pollution is wrong.

I am not sure how much of this type of reaction stems from a misunderstanding or lack of familiarity with the arguments for the economists' policy recommendations, and how much is due to a rejection of the premises, analysis, and value judgments on which these recommendations are based. And I will not attempt to answer this question here. Rather, I will limit myself to making clear the rationale for some of our recommendations concerning policy and the value judgments on which they are based.

To the economist, the environment is a scarce resource which contributes to human welfare. The economic problem of the environment is a small part of the overall economic problem: how to manage our activities so as to meet our material needs and wants in the face of scarcity. The economists' recommendations concerning the environment flow out of our analysis of the overall economic problem. It will be useful to begin with a brief review of the principal conclusions of economic reasoning concerning the allocation of scarce resources to essentially unlimited needs and wants. After reviewing some basic economic principles and the criteria that economists have used in the evaluation of alternative economic outcomes, I will explain the economic view of the environment and some of the major policy recommendations which follow from that view. I will conclude by identifying some of the major questions and possible sources of disagreement about the validity

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