

REASON PAPERS

A Journal of Interdisciplinary Normative Studies

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The Need for Realism in Business Ethics — Elaine Sternberg
The Virtue of Prudence as the Moral Basis of Commerce — Tibor R. Machan
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Review Essay

Review Essay: Brian Doherty's *Radicals for Capitalism: A Freewheeling
History of the Modern American Libertarian Movement*, Paul Starr's
Freedom's Power: The History and Promise of Liberalism, and Arthur A.
Ekirch, Jr.'s *The Decline of American Liberalism*

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- Paul Bloomfield, ed.'s *Morality and Self-Interest* — Jonathan Jacobs
Robert Levy and William Mellor's *The Dirty Dozen: How Twelve Supreme
Court Cases Radically Expanded Government and Eroded Freedom*
—Timothy Sandefur

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Editorial

Throughout its history, *Reason Papers* has periodically featured special issues with guest editors. The current edition is one such issue, a special symposium on business ethics guest edited by Nicholas Capaldi, himself a veteran of these pages. The practice of commerce and the economic system of markets are poorly understood both by the general public and by ethicists. Hopefully, this special issue, featuring several contributors who have written for RP in the past, will help increase understanding and foster constructive dialogue in these matters. We also have some unrelated, but none the less interesting, essays in the books section.

Aeon J. Skoble
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Rival Paradigms in Business Ethics

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1. Philosophical Roots

There are two competing narratives about modernity: the Lockean (liberty) narrative and the Rousseauan (equality) narrative. These two narratives permeate and largely define the entire spectrum of political and economic debate. It should therefore come as no surprise that disputes in business ethics reflect these narratives.

Comparison Charts

Ontology (What is the basic truth about ourselves?)

	Lockean Liberty	Rousseauan Equality
Persons	Individuals have free will	Society defines (is constitutive of) the individual
Ultimate Goal	Personal autonomy	Social good
Negative Concern	Tyranny	Victimization (exploitation, alienation)
Positive Concern	Liberty	Equality

Epistemology (How is the ultimate goal identified?)

Lockean Liberty	Rousseauan Equality
Individualistic	Communitarian
Moral pluralism: each individual creates his/her own substantive good	Individuals fulfill themselves within social institutions
Public practices are not ends in themselves, but instrumental to private good	Every institution and every practice must reflect the larger social good

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Axiology (Who or what is of ultimate value?)

	Lockean Liberty	Rousseauan Equality
Politics	Civil association; protect individual negative rights	Enterprise association; protect positive rights with democratic socialism
Law	Rule of law	Distributive justice (fairness)
Legislation	Maximize equality of opportunity	Maximize equality of result

Business Ethics (How ought people relate in the economic realm?)

	Lockean Liberty	Rousseauan Equality
Corporation¹	Nexus of contracting individuals ²	Social entity ³

¹ This dispute is reflected in the literature which focuses on the distinction among the so-called American model of capitalism as opposed to the Rhine (German or European) model of capitalism and the Japanese model of capitalism; see Michael Albert, *Capitalism against Capitalism* (New York: Wiley, 1992). The American model is seen as focused on liberty, whereas the European model is focused on social-democratic equality and the Japanese model provides benevolent authoritarian equality. See Jeremy Rifkin, *The European Dream: How Europe's Vision of the Future Is Quietly Eclipsing the American Dream* (Cambridge, UK, Polity Press, 2005), and Jonathan Macey, *Corporate Governance* (Princeton, NJ: Princeton University Press, 2008), pp. 28-45. For a shockingly out-of-date discussion of Japan, see Norman Bowie, *Business Ethics: A Kantian Perspective* (Oxford: Blackwell, 1999), where one finds talk about how the Japanese and Swedes are so much more productive than the Americans because of their workplace practices and (one assumes) governance practices. For a criticism of the Rhine and Japanese models, see Norman Barry, *Business Ethics* (West Lafayette, IN: Purdue University Press, 1999), pp. 78-84. For a criticism of the Japanese model, see Ian Maitland and Mitsuhiro Umezu, "An Evaluation of Japan's Stakeholder Capitalism," *Journal of Private Enterprise* 21, no. 2 (2006), pp. 131-64.

² See Milton Friedman, "The Social Responsibility Is to Increase Profits," *New York Times Magazine* (September 1970), p. 32; Elaine Sternberg, "The Defects of Stakeholder Theory," *Corporate Governance* 5 (1997), pp. 3-10; and David Henderson, *Misguided Virtue* (London: Institute for Economic Affairs, 2001).

³ See E. Merrick Dodd, Jr., "For Whom Are Corporate Managers Trustees?" *Harvard Law Review* 45 (1932), pp. 1145-60; R. Edward Freeman, *Strategic Management: A Stakeholder Approach*. (New York: Harper Collins, 1984); R. Edward Freeman, "The

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Role of Management	Production of profitable product or service; maximize shareholder value	Distribution trumps production; social good requires multifiduciary duty to stakeholders ⁴
Internal Organization	Hierarchy; contractual autonomy; employment at will	Industrial democracy ⁵

Politics of Stakeholder Theory: Some Future Directions,” *Business Ethics Quarterly* 4 (1994), pp. 409-21; Amitai Etzioni, *The Spirit of Community: The Reinvention of American Society* (New York: Touchstone, 1993); Max B. E. Clarkson, “A Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance,” *Academy of Management Review* 20 (1995), pp. 92-117; and Robert Kuttner, *Everything for Sale: The Virtues and Limits of Markets* (New York: Knopf, 1997).

⁴ In an early version of his position, Freeman advocated the existence of a “metaphysical director” who “has no direct constituency” and “would be responsible for convincing both stakeholders and management that a certain course of action was in the interests of the long-term health of the corporation, especially when that action implies the sacrifice of the interests of all”; see William M. Evan and R. Edward Freeman, “A Stakeholder Theory of the Modern Corporation: Kantian Capitalism,” in *Ethical Theory and Business*, ed. Tom Beauchamp and Norman Bowie, 3rd ed. (Upper Saddle River, NJ: Prentice-Hall, 1988), p. 104. This has a direct affinity with George Brenkert’s notion of a Philosopher-King in his *Political Freedom* (London: Routledge, 1991). Rakesh Khurana, in his *From Higher Aims to Hired Hands* (Princeton, NJ: Princeton University Press, 2007), p. 331, mourns what he sees as the eclipse of the notion that business schools trained managers as part of the university’s mission “to preserve, create, and transmit knowledge to advance the public good” in favor of agency theory. Khurana implicitly accepts the Rousseauan narrative (common good) and explicitly rejects the Lockean narrative (maximize shareholder profits). He rightly observes that this has important implications for who gets to teach management.

⁵ See Carole Pateman, *Participation and Democratic Theory* (Cambridge: Cambridge University Press, 1970); Denise Rousseau, et al., “Not so Different After All: A Cross-Discipline View of Trust,” *Academy of Management Review* 23 (1998), pp. 393-404; Denise Rousseau and Andrea Rivero, “Democracy: A Way of Organizing in a Knowledge Economy,” *Journal of Management Inquiry* 12, no. 2 (June 2003), pp. 115-34; and Joan Magretta and Nan Stone, *What Management Is: How It Works and Why It’s Everyone’s Business* (New York: Free Press, 2002). (The general theme of the Academy of Management meeting in Seattle in 2003 was “Democracy in a Knowledge Economy.”) James Hoopes gives a broad but critical historical overview of this dispute in the management literature of the twentieth century; see James Hoopes, *False Prophets* (Cambridge, MA: Perseus, 2003). The emphasis on profit and hierarchy are a stand-in for liberty, whereas the advocacy of democracy and the deemphasis on profit are a stand-in for equality.

2. Lockean Liberty Narrative⁶

The Lockean liberty narrative is a form of explication. *Explication* presupposes that all social practices function with implicit norms and that to explicate a practice is to make explicit the inherent norms.⁷ In explication we try to clarify that which is routinely taken for granted, namely, our ordinary understanding of our practices, in the hope of extracting from our previous practice a set of norms that can be used reflectively to guide future practice. We do not change our ordinary understanding but rather come to know it in a new and better way. A relevant example is the reliance on *stare decisis* and the analysis of prior cases in the Anglo-American legal system. Explication is an intrinsically historical and conservative activity precisely because a practice is an ongoing historical event. To explicate is to explain what we have been doing, specifically what we have been trying to do. Explication, then, sees the present as a development out of the past; explication does not see the present as an imperfect vision of the future.⁸

The Lockean liberty narrative endorses (a) the Technological Project, (b) a free-market system, (c) limited government, (d) the rule of law, and (e) a culture of personal autonomy. It tries to identify the inherent norms of current business practice, and instructs students in how to participate in making the system work and how to be successful by following its norms.

The crucial theoretical argument for the centrality of a free market was made by Adam Smith.⁹ Smith emphasizes private property, competition, and the division of labor, all of which contribute to technological innovation. In Locke's version,

God, who has given the world to men in common, has also given them reason to make use of it to the best advantage of life, and

⁶ See Nathan Rosenberg and L. E. Birdzell, Jr., *How the West Grew Rich: The Economic Transformation of the Industrial World* (New York: Basic Books, 1985); and Deepak Lal, *Reviving the Invisible Hand: The Case for Classical Liberalism in the Twenty-First Century* (Princeton, NJ: Princeton University Press, 2006).

⁷ Ludwig Wittgenstein, *Philosophical Investigations* (Oxford: Blackwell, 1958).

⁸ This is why Marx is not engaged in explication. He is not content to describe the evolution of bourgeois capitalism out of feudalism, but claims to expose the hidden structure of capitalism and to predict the future. We should add that he is wrong.

⁹ See Adam Smith, *An Inquiry into The Nature and Causes of the Wealth of Nations* (Oxford: Oxford University Press, 1985 [1776]).

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convenience. . . . [I]t cannot be supposed He meant it should always remain common and uncultivated. He gave it to the use of the Industrious and Rational . . . not to the Fancy or Covetousness of the Quarrelsome and Contentious . . . for it is labor indeed that puts the difference of value on every thing . . . [O]f the products of the earth useful to the life of man nine tenths are the effects of labor.¹⁰

In order for a free market economy to function it requires a limited government. The government provides the legal context for maintaining law and order and for enforcing contracts. It requires as well that the government which performs this service understands that it should not interfere with the competitive and innovative process of the market. The government exists to protect the *rights of individuals*, who pursue their own individual interests, from interference either by others or by the government itself. It does not exist to further a collective good or to serve the bureaucracy or to serve a particular faction. This is the sense in which the government is limited or subordinate to the requirements of commerce. It exhibits the *rule of law*, characterized by Hayek as procedural norms within which individuals pursue their substantive self-interest, not a collective good.

In order for a government to remain limited and not become either authoritarian-totalitarian or subject to mob-rule or the tyranny of the majority (i.e., democracy), it is necessary that there be a larger supportive culture where the citizens are special kinds of people. They must be autonomous people.¹¹ *Autonomous individuals* are those who rule themselves, that is, they impose order on their lives through self-discipline in order to achieve goals that they have set for themselves. Autonomous people are inner-directed and therefore capable of participating in the Technological Project in a creative and constructive way. In fact, the ultimate purpose of the Technological Project is not simply to create more resources or wealth but to allow autonomous people to express their freedom. Wealth is a means to achievement and freedom, not an end in itself.

¹⁰ John Locke, *Second Treatise of Government*, ed. C. B. Macpherson (Indianapolis, IN: Hackett, 1980), ch. 3, paras. 26, 27, 34, and 40.

¹¹ See Michael Oakeshott, "The Masses in Representative Democracy," in Michael Oakeshott, *Rationalism in Politics and Other Essays*, ed. Timothy Fuller (Indianapolis, IN: Liberty Press, 1991). Also see Michael Oakeshott, "The Rule of Law," in Michael Oakeshott, *On History and Other Essays* (Totowa, NJ: Barnes & Noble, 1983).

3. Rousseauan Equality Narrative

The Rousseauan equality narrative is a form of exploration. The primary explanatory model of the physical sciences is exploration. In *exploration* we begin with our ordinary understanding of how things work and then go on to speculate on what might be behind those workings (e.g., molecules, viruses, etc.). In time, we come to change our ordinary understanding. The new understanding does not evolve from or elaborate on the old understanding; rather, it replaces it by appeal to *underlying structures*. The underlying structures are discovered by following out the implications of some hypothetical model about those structures. The social sciences in general and much of contemporary management adopt this perspective. Such social scientists seek to reveal a structural level of reality (e.g., socio-economic classes, subconscious, etc.) of which we are not immediately aware. By further analogy with the physical sciences, once the hidden structure is exposed, we should be in a position to construct a social technology that can resolve the practical problems of the social world in the same way that engineers apply the results of the physical sciences.

Our ordinary understanding is revisable in the light of the clarification of underlying structures. This is what John Rawls calls “reflective equilibrium,” in which our ordinary understanding is to be put into equilibrium with the constructs that reveal and explain the structural level.¹² Exploration then comes with a built-in critical capacity: it can both legitimate and delegitimize specific elements of our ordinary understanding.

There are several serious flaws in exploration within the social sciences. To begin with, the alleged hidden structures are never isolable and confirmable.¹³ There is nothing in the social world that corresponds to an atom or molecule, or even a virus. In the absence of confirmable structures, there are competing explorations none of which can empirically be confirmed. Denied formal criteria or extra-systematic criteria for evaluating their own hypotheses, theorists can only fall back upon aesthetic and/or informal criteria. Often, these criteria mask a hidden or not-so-hidden private political agenda.

The Rousseauan equality narrative (a) disapproves in whole or in part of the free market system, (b) identifies what *ought* to be the norms of business practice, and (c) instructs students on how to transform or modify

¹² See John Rawls, *A Theory of Justice* (Cambridge, MA: Harvard University Press, 1971), sec. 9.

¹³ See Friedrich A. Hayek, *The Counter-Revolution of Science: Studies on the Abuse of Reason* (Indianapolis, IN: Liberty Press, 1980).

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present business practice.¹⁴

In *Discourse on the Arts and Sciences*, Rousseau criticizes what we have called the Technological Project.¹⁵ Instead of satisfying genuine human needs, the arts and sciences are expressions of pride (promoting invidious self-comparison), and they have led to luxury as well as the loss of human liberty. In his *Discourse on the Origins of Inequality*, Rousseau offers a hypothetical, historical reconstruction in which the division of labor is blamed for economic inequality; the result is a (Lockean) social contract in which the rich and powerful coerce the less fortunate into institutionalizing inequality.¹⁶ Rousseau's own social contract is meant to displace this unhealthy hierarchy and inequality.

Rousseau's critique of modern society was adapted and broadened in the nineteenth century (e.g., by Robert Owen, Charles Fourier, Pierre-Joseph Proudhon, Louis Blanc, Saint-Simon, Marx, etc.), mainly by writers we now identify generically as socialist.¹⁷ These writers, unlike Rousseau, embrace technology, but criticize the poverty and inequality which they alleged were consequences of the Industrial Revolution. They advocate the abolition of private property, which they assert unfairly concentrates power and wealth among a few, exacerbates inequality, and does not provide equal opportunities for everyone. They seek "more equal" opportunity, a "fairer" and more

¹⁴ Rousseau and Rivero claim: "As a professional and scientific community, we also have a public role to play . . . [in] active monitoring of the practices and trends in contemporary organizations with respect to how they promote or impede democratic practice"; see Rousseau and Rivero, "Democracy: A Way of Organizing in a Knowledge Economy," p. 127.

¹⁵ See Jean-Jacques Rousseau, *Discourse on the Arts and Sciences* (London: J. M. Dent & Sons, 1919 [1750]).

¹⁶ This is the origin of all victimization hypotheses; see Jean-Jacques Rousseau, *Discourse on the Origin of Inequality*, trans. Donald Cress (Indianapolis, IN: Hackett, [1754]).

¹⁷ The disastrous and inhumane consequences and failures of orthodox Marxism (centralized and planned or command economies as well as one-party dictatorial political rule) would be rejected by those we here identify as socialist.

Ian Buruma and Avishai Margalit maintain that non-Westerners who criticize what we call the Lockean narrative invariably borrow from Western writers who reflect what we call the Rousseauan narrative: "[A]s usual the West was fought with ideas that originated in Europe," and "One of the traditional attractions of Islam was its egalitarian promise"; see Ian Buruma and Avishai M. Margalit, *Occidentalism* (New York: Penguin, 2004), pp. 145 and 117, respectively.

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egalitarian distribution of wealth, and the reorganization of society into smaller communities.

In *The Roots of Romanticism*, Isaiah Berlin identifies the romantic dimension of this narrative: “[Romanticism] introduces for the first time . . . a crucial note in the history of human thought, namely that ideals, ends, objectives are not to be discovered by intuition, by scientific means, by reading sacred texts, by listening to experts or to authoritative persons; that ideals are not to be discovered at all, they are to be invented.”¹⁸ He notes, further, that the fundamental basis of romanticism is “will,”

the fact that there is no structure to things, that you can mould things as you will—they come into being only as a result of your molding activity—and therefore opposition to any view which tried to represent reality as having some kind of form which could be studied, written down, learnt, communicated to others, and in other respects treated in a scientific manner.¹⁹

The allowance of market forces and the external, independent exercise of choice is a failure of imagination and creativity on the part of political, economic, and cultural leaders.²⁰ Again, as Berlin writes,

there is even such a thing as romantic economics . . . where the purpose of economics, the purpose of money and trade, is the spiritual self-perfection of man, and does not obey the so-called unbreakable laws of economics. . . . Romantic economics is the precise opposite of [laissez-faire economics]. All economic institutions must be bent toward some kind of ideal of living together in a spiritually progressive manner.²¹

¹⁸ Isaiah Berlin, *The Roots of Romanticism* (Princeton, NJ: Princeton University Press, 1999), p. 87.

¹⁹ *Ibid.*, p. 127.

²⁰ Romantic “molding,” I take it, differs from the autonomous exercise of human freedom because it applies to a social whole, it assumes that there cannot be unintended consequences (for which one would have to accept responsibility), and it assumes that there will be no unintended consequences because all will choose or acquiesce in the same choice.

²¹ Berlin, “The Roots of Romanticism,” p. 126.

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The most important and influential contemporary philosophical work in the Rousseauan equality-narrative tradition is John Rawls's *A Theory of Justice*.²² To begin with, Rawls provides an exploration,²³ not an explication. He presents a *theory about* justice. What this means is that instead of explicating what we commonly mean, Rawls takes our commonsense intuitions about justice as a springboard for exploring the hidden structure behind our ordinary preconceptions with the hope of modifying our preconceptions in the light of that exploration. Consequently, our commonsense intuitions will be "on trial" with the hidden structures revealed by exploration as the standard by which they will be judged. What Rawls describes as the method of reflective equilibrium is precisely what we have identified as exploration. It is as well an exploration in the form of a social contract (ahistorical and contextless); it has a counterpart to the state of nature

²² Victimization is present in Rawls in the form of the claim that we are all products of the genetic lottery and early environmental influences like the family. Moreover, none of us deserves our good fortune. Rawls's position was originally articulated in 1958; see John Rawls, "Justice as Fairness," *Philosophical Review* 67, no. 2 (April 1958), pp. 164-94. See also, John Rawls, *Political Liberalism* (New York: Columbia University Press, 1993). In the eighth edition of their text *Ethical Theory and Business*, the editors attach the following title to their selection from Rawls: "An Egalitarian Theory of Justice"; see Tom Beauchamp, Norman Bowie, and Denis Arnold, eds., *Ethical Theory and Business*, 8th ed. (Upper Saddle River, NJ: Pearson, Prentice-Hall, 2009), p. 674.

David Hume long ago demolished the notion of "fairness" by arguing that (1) there is no agreement on what the term means (this is an advantage if all one wants to do is to complain); (2) any division or redistribution of property based on "desert" will fail to attain a consensus (i.e., the same problem with defining "fairness"); (3) any redistribution based upon who will make the best use of the property is incalculable (anticipating Hayek); (4) in a world of equal assets, subsequent trade and economic activity will lead to inequality; and (5) any attempt to maintain the initial equality would require a comprehensive despotism (something which I shall argue below is welcomed by some intellectuals). See David Hume, *Enquiry Concerning the Principles of Morals*, ed. P. H. Nidditch (Oxford: Oxford University Press, 2005 [1777]), sec. III, part 2, esp. p. 194.

²³ There is no way of confirming an exploratory hypothesis or choosing among alternative explorations. Calling an exploration Kantian merely acknowledges the lack of both empirical foundations and confirmation. Explorations always maintain that they begin with our ordinary understanding and then go beyond it. We would suggest, contrary to Rawls, that the concept of justice as ordinarily understood is backward looking, whereas Rawls changes its meaning by equating it with future equality of outcome. Whatever the merits of the case for equality of outcome, it appears in this context to be an external value surreptitiously introduced as if it were both the logical and future historical outcome of the present meaning.

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in the form of a hypothetical state of affairs known as the “original position.”²⁴ As Rawls puts it, we must “leave questions of meaning and definition aside . . . to get on with the task of developing a substantive theory of justice.”²⁵ In the hypothetical original position individuals are said to choose principles of justice “behind a veil of ignorance.” This means that choices are to be made with no knowledge of “[one’s] place in society, his class position or social status; nor does he know his fortune in the distribution of natural assets and abilities, his intelligence and strength,” and not even one’s sex.²⁶

The egalitarianism in Rawls comes out in a number of ways. First, justice is tied to equality: “the principles that free and rational persons concerned to further their interest would accept in an initial position of *equality* as defining the fundamental terms of their association.”²⁷

Second, his insistence on pure procedural justice is designed to nullify the effects of specific contingencies that put men at odds and tempt them to exploit social and natural circumstances to their own advantage. Specifically, Rawls maintains that “everyone’s well being is dependent upon a scheme of cooperation without which no one could have a satisfactory life.”²⁸ This is a form of enterprise association.

Third, he insists not only that citizens have freedom, but that they have sufficient all-purpose means to make effective use of their freedoms. He specifically rejects “excessive” inequalities of wealth and power. That is why Rawls claims that Robert Nozick’s libertarian conception of justice in *Anarchy, State, and Utopia* is not a liberal conception of justice. According to Rawls, libertarianism does not assure all citizens sufficient means to make full and effective use of their basic liberties.²⁹

²⁴ “In morality as in everything else, the Rationalist aims to begin by getting rid of inherited nescience and then to fill the blank nothingness of an open mind with the items of certain knowledge which he abstracts from his personal experience, and which he believes to be approved by the common ‘reason’ of mankind”; see Oakeshott, *Rationalism in Politics*, p. 40.

²⁵ Rawls, *A Theory of Justice*, p. 579.

²⁶ *Ibid.*, p. 137.

²⁷ *Ibid.*, p. 10 (italics mine).

²⁸ *Ibid.*, p. 151; see also, pp. 522, 527, and 570-77.

²⁹ See Rawls, *Political Liberalism*, pp. 262-65.

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Fourth, Rawls's positive distributive thesis is equality-based reciprocity. All social goods are to be distributed equally, unless an unequal distribution would be to everyone's advantage. The guiding idea is that since citizens are fundamentally equal, reasoning about justice should begin from a presumption that cooperatively produced goods should be equally divided. Justice then requires that any inequalities must benefit all citizens, and particularly must benefit those who will have the least. Equality sets the baseline; from there, any inequalities must improve everyone's situation, and especially the situation of the worst-off. These strong requirements of equality and reciprocal advantage are hallmarks of Rawls's theory of justice. "[S]ocial and economic inequalities" are to be to the greatest benefit of the "least advantaged," also called the "difference principle."³⁰ The difference principle is a response to socialist concerns about equality. It is a way of arguing that given the original position, we understand how self-interest is tied to the interest of others.

Finally, Rawls maintains both that liberty is a prior principle and that fair opportunity is prior to the notion that inequalities are or must be to the advantage of those less fortunate. With regard to the primacy of liberty, Rawls offers no argument or proof. Nor does he prove that adopting liberty advances the collective interest. Rawls does not specify which liberties are basic or how conflicts among liberties are to be resolved. A similar kind of criticism can be made of the difference principle, a principle which is not clearly deducible from the original position without some implicit assumptions about human nature, specifically the assumption that everyone's well-being depends upon everyone else's well-being. In addition, the discussion of the "maximin rule" does not differentiate between relative and absolute disadvantages (e.g., basic versus minimal needs). This leads to the suspicion that, for Rawls, the main concern is with how each views oneself relative to others. This suspicion is borne out by Rawls's contention that "the most important primary good is self-respect,"³¹ coupled with the view that self-respect depends upon how we see ourselves through the eyes of others.³² We are back to Rousseau.

³⁰ Rawls, *A Theory of Justice*, p. 75.

³¹ *Ibid.*, p. 440.

³² This is the polar opposite conception of self-respect from what one would find if the autonomous moral agent were taken seriously.

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The influence of Rawls (and therefore of Rousseau) on business ethics can be seen in the work of Thomas Donaldson.³³ By means of a hypothetical contract,³⁴ Donaldson postulates that corporations assume moral obligations to employees, consumers, and society as a whole. Corporations thereby assume social responsibilities beyond the creation of wealth and jobs. Going even further than Donaldson is Christopher McMahon, in his influential book *Authority and Democracy*. McMahon advocates co-determination, that is, “legally stipulating that boards of directors be composed in equal parts of representatives of employees and investors.”³⁵ Here we have a political agenda: If the majority of voters vote for candidates (executive and legislative branches) who favor these policies, then laws will be passed and regulatory agencies such as the Securities Exchange Commission (SEC) will enforce such laws, requiring board composition to be “democratic.”

Beyond the common moral critique, these authors disagree on exactly how to transform the present system and what the precise structure of the alternative will look like. What identifies someone as a proponent of this Rousseauan narrative is (a) the sense of being in an adversarial relation (of varying degrees) to whatever they take the present system to be,³⁶ (b) a moral

³³ See Thomas Donaldson, *Corporations and Morality* (Upper Saddle River, NJ: Prentice-Hall, 1982), ch. 3; Thomas Donaldson, *The Ethics of International Business* (New York: Oxford University Press, 1989), pp. 47-61; Thomas Donaldson, *The Ethics of International Business* (New York: Oxford University Press, 1989); Thomas Donaldson and Thomas W. Dunfee, “Towards a Unified Conception of Business Ethics: Integrative Social Contracts Theory,” *Academy of Management Review* 19 (1994), pp. 252-84; and Thomas Donaldson and Thomas W. Dunfee, *Ties that Bind: A Social Contracts Approach to Business Ethics* (Cambridge, MA: Harvard Business School Press, 1999).

³⁴ In the Lockean narrative, all contractual negotiation begins from the status quo, and no deal is an acceptable one unless all or some parties are helped and no party is hurt (i.e., it is Pareto-efficient). The Lockean narrative is focused on future growth, not redistribution.

³⁵ Christopher McMahon, *Authority and Democracy* (Princeton, NJ: Princeton University Press, 1994), p. 282.

³⁶ This is reflected in Edward Said, “Speaking Truth to Power,” in Edward Said, *Representations of the Intellectual* (New York: Vintage, 1996). In the field of business ethics, we are given an ethics “for,” not an ethics “of.” The narrative is always reformist; if there is nothing to reform, then there is nothing to say.

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critique in which it is necessary to identify the “bad guys”³⁷ and the “victims,” (c) the advocacy of restructuring, and (d) the failure to provide an explicit account of how the new structure will function. They are voices of grievance (and hope) without an explicit plan.

The hidden-structure hypothesis can never stray very far from the understanding of some practice or practices in which we are consensually engaged. In the end, the hidden-structure hypothesis is always an attempt to model one practice (the *disputed practice*) in terms of another (the *consensual practice*). The only question is whether the consensual practice (assuming it has been properly understood) is an appropriate and relevant model for the disputed practice. An example of this in the business ethics/corporate social responsibility (CSR) literature is taking big-corporate, organizational issues to be central and practice-of-commerce issues to be peripheral. Thus, managing people in organizations takes center stage and marketplace interactions between buyers and sellers are treated as peripheral phenomena of “business.” The point is that this focus isn’t (and indeed, can’t be) derived in a value-free way.

4. Democracy

Recent discussions in the management literature about democracy reflect the foregoing differences in outlook. The term “democracy” has taken on a wide variety of meanings depending upon what favored or disfavored political, social, economic, cultural, or any other feature the user has in mind.³⁸ For our purposes there are two different conceptions of democracy.

³⁷ The original “bad guys” were the large feudal landowners; this evolved into the multinational corporation. More specifically, with regard to the U.S., the original bad guys were “WASPS,” but later white males.

³⁸ Democracy may simply mean in the minds of its proponents that there should be an institutionalized widespread use of discussion and consultation among all segments of the organization (Habermasian democracy). This can range all the way from anonymous suggestion boxes (constructive or complaint and denunciation) to consultation with interested parties to periodic and publicized evaluations of all members of the staff either by co-workers, supervisors, or the supervised. Keep in mind, however, that the precise form of this consultation is itself not determined democratically but by those in hierarchical authority. Parents may consult their children but still run the family as a benevolent despotism. In today’s organizations, this is a widespread and accepted practice whose benefits are hardly ever challenged. It is also unclear why calling this democratic means anything. This is especially important in economies influenced by the Technological Project where autonomous individuals both need to know and wish to know in order to obtain maximum efficiency. In this important respect advocates of Taylorism were mistaken about the requirements of the Technological Project. From the point of view of practice this

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First, there is a Lockean version of democracy, which we shall call democracy₁. In what follows we shall use democracy₁ in the generic sense to mean majority rule; democracy₁ will mean majority rule as it functions within the context of a republic. The purpose of democracy₁ in the political realm is *negative*: checks and balances (competition). Democratic procedure is not a way of arriving at unanimity but a way of blocking any overall purpose from dominating. It actually models government so as to reflect certain aspects of a market economy rather than the other way around. Democracy, therefore, cannot be used to achieve efficiency and coordination. This is precisely the understanding of James Madison in *Federalist* #10, and it is borne out in the political practice of the U.S.³⁹

More importantly, the United States, as a primary example, is not a democracy. Jeffrey Kerr argues well that political democracy is not an appropriate or useful model for organizational democracy.⁴⁰ My thesis is much stronger: Political democracy neither characterizes the political system of the U.S. nor would it permit the proper functioning of a free-market economy.

There is thus, in an important sense, a total misunderstanding (or rejection) of the relationship that currently holds between the economic, political, legal, and social institutions in the U.S. In short, the democratization thesis in the management literature is not an attempt to explicate current practice but to replace it with something else.

In Rousseauan exploration we must identify a different conception of democracy, which we shall call democracy₂. This conception of government harks back in part to the classical Greek ideal of the polis according to which a citizen is one who participates in public deliberation about public policy.⁴¹ It is the ancient, not the modern, conception of freedom. According to

version of democratization is both noncontroversial and relatively innocuous. There is also such a thing as shareholder democracy. Shareholders do, usually, vote, and a majority, usually, carries the day. But it is not “one shareholder, one vote”; it is “one share, one vote.”

³⁹ See Alexander Hamilton, John Jay, and James Madison, *The Federalist Papers* (New York: Signet, 2003 [1787]).

⁴⁰ See Jeffrey Kerr, “The Limits of Organizational Democracy,” *Academy of Management Executive* 18, no. 3 (2004), pp. 81-95.

⁴¹ “[D]emocracy is the power of the people and is manifest in ways . . . that promote participation in and influence over the decisions affecting their everyday lives”; see Rousseau and Rivero, “Democracy: A Way of Organizing in a Knowledge Economy,” p. 116.

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Benjamin Constant, what differentiates the liberty of the moderns from that of the ancients is that among the ancients, liberty consisted in

exercising collectively, but directly, several parts of the complete sovereignty; in deliberating, in the public square, over war and peace; in forming alliances with foreign governments; in voting laws, in pronouncing judgments; in examining accounts, the acts, the stewardship of magistrates; in calling them to appear in front of the assembled people, in accusing, condemning or absolving them. But if this is what the ancients called liberty, they admitted as compatible with this collective freedom the complete subjugation of the individual to the authority of the community. . . . No importance was given to individual independence, neither in relation to opinions, nor to labour [A]mong the ancients the individual, almost always sovereign in public affairs, was a slave in his private relations.⁴²

The political and philosophical left in general has, following Rousseau, sought to revitalize the ancient or classical conception of community within the modern context. The firm has become the new locus of democratic community understood in the classical sense:

⁴² Benjamin Constant, *Political Writings*, ed. Biancamaria Fontana (Cambridge: Cambridge University Press, 1988), p. 311. The latest movement on the part of unions to make all voting on whether to have a union public and to do away with the secret ballot is an ominous indication of what Constant was talking about.

According to John Stuart Mill, the ancient view was resuscitated in the early nineteenth century, and it viewed government as the formulator of the common good as determined democratically (which is a version of the general will). Under the influence of Thomas Macaulay, Mill had already criticized his own father, James Mill, and Jeremy Bentham as proponents of this position. What does this position assume? (1) All people are basically the same in their needs, and it is possible to achieve homeostasis both within the individual and within groups of individuals. (2) The human need to be in agreement (homeostasis) with others takes precedence over all other needs. (3) Dysfunctional behavior on the part of individuals or systemic bureaucratic dysfunction is the result of wrong information or asymmetric information. (4) Information symmetry solves every problem and open (i.e., “democratic”) discussion leads to symmetry. (5) Good management = open-ended therapy sessions, the result of which will be to get everyone on board if done properly. (6) If propositions (1) through (5) are true, then the larger social system has a collective common purpose with which corporate purpose links. (7) In the end, there will be only one firm or one world government with many delegated subunits (i.e., democratic socialism).

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In some ways, it may be easier to promote democratic practices in firms than in societies. Organization members tend to have consensus regarding task and mission. Firms have greater socialization capabilities via control over the selection, training, and attrition of their members. Particularly when they are small in size, firms and work groups can often more readily establish familiarity and trust. Last, members' interests and concerns may be easier to comprehend in the more focused environment of work. In contrast, societies are often large, complex and, with urbanization, can become depersonalized.⁴³

The foregoing account underscores the disconnection with democracy₁.

Amartya Sen argues that a critical aspect of democracy is that it gives people a voice in the rules that affect them.⁴⁴ And it reflects a salient characteristic of what constitutes democracy that may, in fact, provide better information for a company. Is this problematic? The answer depends on what is meant by "having a voice." Does this mean mere (benign) consultation or does it mean a (malignant) seat on the board or veto power?⁴⁵

Important to democracy₂ is its conceptual link to equality.⁴⁶ The origin of this link to equality lies in Rousseau's insistence in the *Social Contract* that the procedure of democracy itself must be ratified unanimously,

⁴³ Rousseau and Rivero, "Democracy: A Way of Organizing in a Knowledge Economy," p. 119.

⁴⁴ See Amartya K. Sen, "The Impossibility of a Paretian Liberal," *The Journal of Political Economy* 78 (1970), pp. 152-57.

⁴⁵ Evan and Freeman suggest a "board of Directors comprised of representatives of five stakeholder groups, including employees, customers, suppliers, stockholders, and members of the local community. . . . Whether or not each representative has an equal voting right is a matter that can be decided by experimentation"; see Evan and Freeman, "A Stakeholder Theory of the Modern Corporation: Kantian Capitalism," p. 104.

⁴⁶ Tom Christiano explicitly links democracy to equality by calling it "a method of group decision making characterized by a kind of equality among the participants at an essential stage of the collective decision making. . . . [T]he equality . . . may be more or less deep. It may be the mere formal equality of one-person one-vote in an election for representatives to an assembly where there is competition among candidates for the position. Or it may be more robust, including equality in the processes of deliberation and coalition building"; Tom Christiano, "Democracy," *Stanford Encyclopedia of Philosophy*, accessed online at: <http://plato.stanford.edu/entries/democracy/>.

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that is, everyone has an equal say in decision-making. Peter Singer and Jeremy Waldron both connect democracy to equality.⁴⁷

The advocates of democracy₂ are at odds with Lockean big-picture explication and the centrality of autonomy. What we have here are two competing world views. We have identified one as Lockean-libertarian, based on an explication of current practice,⁴⁸ and the other as Rousseauan-communitarian, based on an exploratory account of what institutional practice “should be,” itself based upon a different set of assumptions about fundamental truths.⁴⁹

With regard to the Rousseauan-Communitarian approach, R. Edward Freeman suggests expanding the community to those outside the firm, including such external stakeholders as “customers, suppliers, local community leaders, labor unions, and special interest groups.”⁵⁰ In Freeman’s universe, everyone is on the inside. Four observations are worth noting here. First, Freeman’s position is evidence of the extent to which democratization₂

⁴⁷ See Peter Singer, *Democracy and Disobedience* (Oxford: Oxford University Press, 1973); and Jeremy Waldron, *Law and Disagreement* (Oxford: Oxford University Press, 1999), ch. 5.

⁴⁸ See Milton Friedman, *Capitalism and Freedom* (Chicago, IL: University of Chicago Press, 1962); Friedrich A. Hayek, *Law, Legislation and Liberty, Volume 2, The Mirage of Social Justice* (Chicago, IL: University of Chicago Press, 1976); and Stephen M. Bainbridge, “Community and Statism: A Conservative Libertarian Critique of Progressive Corporate Law Scholarship,” *Cornell Law Review* 82 (1997), pp. 856-58.

⁴⁹ See Rawls, *A Theory of Justice*; Charles Taylor, *Sources of the Self* (Cambridge, MA: Harvard University Press, 1992); Evan and Freeman, “A Stakeholder Theory of the Modern Corporation: Kantian Capitalism”; Jurgen Habermas, “A Discourse-Theoretic Justification of Basic Rights” and “Citizenship and National Identity,” in Jurgen Habermas, *Between Facts and Norms* (Cambridge, MA: MIT Press, 1996); Richard Rorty, “The Priority of Democracy to Philosophy,” in *Reading Rorty*, ed. Alan Malachowski (Oxford: Blackwell, 1990), pp. 279-302; and Rousseau and Rivo, “Democracy: A Way of Organizing in a Knowledge Economy.” Freeman quotes Rorty on pragmatism with approval: “[P]ragmatists . . . hope instead that human beings will come to enjoy more money, more free time, and greater *social equality* [italics mine], and also that they will develop more empathy, more ability to put themselves in the shoes of others;” see R. Edward Freeman, “Managing for Stakeholders,” in *Ethical Theory and Business*, ed. Tom Beauchamp, Norman Bowie, and Denis Arnold, 8th ed. (Upper Saddle River, NJ: Prentice-Hall, 2009), pp. 66-67.

⁵⁰ Freeman, “Managing for Stakeholders,” p. 53.

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within the firm is closely tied ultimately to democratic socialism.⁵¹ Second, there is nothing in a market economy that prevents groups of individuals from forming a firm, organizing it along communitarian lines, and competing as such. These sorts of communities have existed since the nineteenth century (e.g., Owen Fourier, etc.).⁵² Contrary to Freeman, looked at from that broader time slice, such communities have not been very successful. Third, forgotten in much of this is the investor/shareholder. Would investors choose to invest in firms structured along the lines of democracy₂? If such firms were successful economically, investors would certainly buy in. But given the second observation, it is clear on the whole⁵³ that they don't and why they do not. Finally, are not customers in a position to signal their preferences by choosing to buy or not to buy? As Ludwig von Mises puts it:

With every penny spent the consumers determine the direction of all production processes and the details of the organization of all business activities. This state of affairs has been described by calling the market a democracy in which every penny gives a right to cast a ballot. It would be more correct to say that a democratic constitution is a scheme to assign to the citizens in the conduct of government the same supremacy the market economy gives them in their capacity as consumers. However, the comparison is imperfect. In the political democracy only the votes cast for the majority candidate or the

⁵¹ This was part of Friedman's original critique of the CSR movement; see Friedman, "The Social Responsibility Is to Increase Profits."

⁵² Limited partnerships and small software start-ups in which all of the employees are shareholders hardly reflect the kind of thing that advocates of democratization₂ have in mind, not least because what the latter have in mind is the socialization of profits (i.e., including the employees in "profit sharing") and the privatization of losses (to be suffered by investor-owners, not employees). The small software start-up exposes its employee owners to risk. Henry Hansmann recites the standard observation that Anglo-American corporate law provides a set of off-the-rack rules of governance that the organizers of firms are free to deviate from in constructing the firm's by-laws; see Henry Hansmann, *The Ownership of Enterprise* (Cambridge, MA: Belknap Press of Harvard University Press, 1993). Hansmann also observes that the thrust of American public policy since World War II has been toward encouraging the formation of firms in almost every structure *except* the investor-owned one. Thus, there have been tax breaks and subsidies for the formation of employee-owned firms, producer and consumer cooperatives, etc. Not only are they "free" to pursue these other forms of organization, they have actually been encouraged through incentives to do so.

⁵³ Socially responsible investing accounts for a very small percentage of investing. It also consistently fails to outperform the rest of the market.

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majority plan are effective in shaping the course of affairs. The votes polled by the minority do not directly influence policies. But in the market no vote is cast in vain. Every penny spent has the power to work upon the production processes.⁵⁴

The communitarian perspective is not based upon scientific empirical evidence. Nor is it based upon the actual practice of management in the current knowledge economy. Rather, it is an account that hopes to see management conform to an “independently” determined model. It is largely an account of what is to be pursued without consideration of how it is to be pursued. If management education were based upon it, then management education would become indoctrination in how to articulate and implement the model. But the “independently” determined model is really an abstraction from an entirely different kind of practice. It is a secularized version of what management would be in a religious monastery (i.e., an enterprise association encompassing the whole of society). This is wholly inappropriate and irrelevant to modern commercial societies. Analogizing businesses to not-for-profits with “public good” missions is equally misguided.

We would contend, further, that experience shows that the foregoing assumptions about humanity just are not true. On the contrary, what distinguishes us from animals is that we are free to choose how we interpret experience. This is what post-modernity has emphasized. To be human is to be free in employing our imagination and intelligence, and it is these faculties that we use to define ourselves as individuals and give meaning to our experience of the world we inhabit. Individuals freely choose meaningful ways of understanding themselves and the world around them. Even our cultural inheritance involves an act of selective appropriation and choice, including the possibility of rejection. Hence, while we may all be born into a social and cultural context, it is simply not true to say that we are products of that context.

5. The Nature of the Firm

In order to understand the firm we must introduce a distinction between civil associations and enterprise associations.⁵⁵ In an *enterprise association* individuals are related by the pursuit of a collective substantive goal (e.g., the defense of the state from external aggression, the achievement of religious salvation in the next life, the production of harps, etc.). The role

⁵⁴ Ludwig von Mises, *Human Action* (Irvington, NY: Foundation for Economic Education, 1996), p. 271.

⁵⁵ See Michael Oakshott, *On Human Conduct* (Oxford: Clarendon Press, 1996), pp. 108-14.

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of management (or government in an enterprise association) is to manage the relationship of the individuals to the collective goal.

In a *civil association* the individuals do not share a collective substantive goal. On the contrary, what the individuals acknowledge are a personal good and a common good, where the latter is understood to encompass rules prescribing the conditions to be observed in making choices about how to pursue one's chosen purposes. The role of government is to be the guardian of the common procedural conditions. The connection between personal autonomy and the civil association should be obvious. Individuals in a civil association may thus share a common good in the formal conditions to be observed, but it is not a substantive collective good in which their interests are subsumed. Within an enterprise association, the law (or rules) that are instrumental in advancing the collective goal are articulated by the government (or management). The politicized, managerial, and/or totalitarian implications of law within an enterprise association are manifest. Within a civil association, the law (or set of rules) is formal, not instrumental, and the rule of law prescribes the conditions within which individuals pursue self-chosen purposes.

Firms are to be understood as *enterprise associations* within a larger civil association. A firm is an enterprise association, that is, individuals are voluntarily involved in the pursuit of a common substantive purpose, specifically a productive undertaking. In a free-market economy, the goal of the firm is usually to produce a profitable product or service. The goal cannot be equality, fulfillment, etc., because these are not substantive purposes. Moreover, as an enterprise association, a firm cannot have two or more discrepant purposes; if there are multiple purposes, then they must be prioritized or systematically related.⁵⁶

The enterprise association that constitutes a firm is an historical artifact, the creation of contracting individuals. The firm is, therefore, a nexus of contracts.⁵⁷ Given the need for and the nature of limited liability, the core of this nexus is management. This is essentially Stephen Bainbridge's view.⁵⁸

⁵⁶ See Michael E. Porter and Michael R. Kramer, "Strategy and Society: The Link Between Competitive Advantage and Corporate Social Responsibility," *Harvard Business Review*, December 2006, pp. 78-92.

⁵⁷ See Ronald H. Coase, "The Nature of the Firm," in *The Economic Nature of the Firm*, ed. Louis Putterman and Randall Kroszner (Cambridge: Cambridge University Press, 1997).

⁵⁸ See Bainbridge, "Community and Statism."

In his director-primacy view of the firm, top management is the firm's core and that core has fiduciary duties to equity owners because that is the best way to constrain their self-seeking behavior and to focus them upon the success of the enterprise.

6. Understanding Management

There must be a decision procedure for deciding how to pursue the common purpose, that is, there must be management. Neither the structure of management nor specific managerial decisions are entailed (i.e., deducible) from the common purpose. They are contingent, and therefore subject to evaluation and re-evaluation. Nevertheless, whatever the structure of management, its decisions, once made, are *compulsory*, for the same reason that no divergence is permitted from the common purpose. Management is, therefore, *hierarchical* even when the managers themselves are chosen by others. The issue is not how and when management consults the staff; the issue is who makes the final call when the consultation is over.

Managerial decisions involve a response to external factors and to internal factors. The overarching external factors are the Technological Project (which in principle cannot be planned and is unpredictable⁵⁹) and the actions of others in a market. No firm will remain profitable and therefore in existence, unless it accepts the constraints and discipline of both the Technological Project and the free-market economy.⁶⁰

The major internal factor is the presence of other agents (e.g., employees or associates). One of the consequences of the Technological Project is the development of what is now called a knowledge economy; the most important contribution of employees is not their physical labor but their technical skill and knowledge as well as their imaginative capacity. The most desirable employees are therefore autonomous ones; however, this means that they have their own personal goals and, if they are inner-directed and creative, are autonomous beings whose cooperation and productivity cannot be coerced. Therefore, dictatorial management models are inherently defective. Our general conclusion is that in a knowledge economy we necessarily have a management structure characterized by hierarchy with delegation. Totalitarian societies committed to the Technological Project (e.g., the former Soviet Union and an earlier Communist China) eventually found it necessary to cater to such individuals. A knowledge economy implies hierarchical but non-dictatorial management.

⁵⁹ Which is Hayek's thesis about why planning will not work.

⁶⁰ See Oliver E. Williamson, *The Economic Institutions of Capitalism, Firms, Markets, and Relational Contracting* (New York: Free Press 1985).

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Does the need for a non-dictatorial management imply democratization₂? The answer is no. What we have is a situation in which firms (organizations) cannot replace markets.⁶¹ The reality is a dynamic market of trial and error with the continuous re-grouping of firms and individuals within those firms. Good management can only exist within a firm that has a clear conception of its present collective goal. At the same time, that clear conception is subject to modification because of the dynamics of the market process, something over which no manager can have control or unerringly predict. Good management of employees consists in choosing people who either have the “right” preferences vis-à-vis the overall common purpose of the firm (which involves judgment) or who can be persuaded through incentives to shape their own preferences to be consistent with that common purpose or at least not antithetical to it (which requires bargaining skills). Neither the managerial judgment nor the skills can be imparted simply through information. Moreover, a successful team under one set of market conditions is not guaranteed success under another set of conditions.

The personal autonomy of the individuals involved is preserved through voluntary contracts. In a knowledge economy, a skilled individual can and does negotiate a relationship with management that is far more satisfactory to that individual than something deliberated according to democracy₂. Such negotiation is easier precisely in those cases where management has a clear conception of its goal or agenda. One may question whether the kind of fulfillment sought by communitarians in an enterprise association is either possible or desirable.⁶² What a knowledge economy permits and calls for is an ever-increasing need for autonomous professionals who relate to each other contractually. It is the Technological Project that promotes the knowledge economy and autonomy.

7. Implications

a. Investors are more important than all other stakeholders

There can be no progress in the Technological Project if there is no market flexibility. The market works because people are willing to invest in a

⁶¹ See Ronald H. Coase, “The Problem of Social Cost,” *Journal of Law and Economics* 3 (1960), pp. 1-44; and Coase, “The Nature of the Firm.”

⁶² Oakeshott says, “Almost all modern writing about moral conduct begins with the hypothesis of an individual human being choosing and pursuing his own directions of activity. . . . [T]his autonomous individual remained as the starting point of ethical reflection. . . . [W]e may promote the ‘happiness’ of others, but we cannot promote their ‘god’ without destroying their ‘freedom’ which is the condition of moral goodness”; see Oakeshott, “The Masses in Representative Democracy,” pp. 367-68.

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limited-liability system; they are willing to invest because of the prospect of profit, and not because they value profit as an end but because of the projects that profit in turn permits them to pursue. Whatever additional motives guide investment, profit remains supreme qua their relationship, as investors, in a specific firm. There is no way to avoid this, short of a planned economy, and then the Technological Project suffers. We might like a greater say on our jobs, but we want cures for cancer and AIDS more.

This is a systemic feature of the relationship between the Technological Project and a market economy. In the nineteenth century some hoped for a world in which the major resources were widely owned and not held by a few individuals or families. This would permit greater opportunity for individuals to define their own economic projects. Ironically, we do in large part have such a world today. Few individuals are in a position to own a major enterprise. Ownership is much more widely diffused.⁶³ Major corporations are “owned” by thousands of individuals, including employees. This widespread ownership, by the way, is much more prevalent in American-style capitalism than it is either in the E.U. (Rhine model) or in Japan. However, the nature of the Technological Project and its present scale requirements lead to the existence of management operating as an enterprise association.

It will be objected that since shareholders vote by the number of shares they hold, not all investors have an equal voice. True enough, but is there an alternative? Would investors allow “equality” of voice? Again, followed to its logical conclusion, the only real alternative is a centrally planned economy with public ownership. Marx was right about that. However, we have tried that alternative, and it fails to maximize the benefits of the Technological Project and leads to other undesirable consequences.

b. Customers are more important than employees

Markets are responsive to consumer demand. You cannot sell a product or a service profitably without catering to the needs of consumers. As Mises pointed out long ago, a greater form of democracy prevails in a free market precisely because producers cannot dictate to consumers.⁶⁴ Myths about subliminal marketing aside, neither management nor employees can dictate to consumers; both must respond to consumer demand.

⁶³ Technically speaking, investors are not owners of the enterprise but of shares. This merely reinforces my point that systemic requirements of the Technological Project must be taken seriously before any discussion of the structure of management or suggested changes to it.

⁶⁴ See Mises, *Human Action*, n. 54 above.

c. Autonomy is more important than democracy

If the capacity to be free is a fundamental feature of humanity and if once autonomy is achieved,⁶⁵ I would venture to affirm, it is an irreversible state, then all institutions, economic and political, must reflect this autonomy. Politically speaking, democracy is not itself a positive expression of autonomy but a negative means of maintaining it. Autonomy is preserved for investors, customers, and contracting employees. The freedom to hire and fire at will preserves the vitality of firms, but it also permits potential employees to change jobs and even careers.⁶⁶ It also creates more durable and reliable relationships with employees on a case-by-case (contractual) rather than an all-or-nothing (union model) basis. A knowledge economy within the Technological Project makes this possible to a greater and greater extent. As a contracting employee to whom some responsibility has been delegated through negotiation, I have greater autonomy than I would have if every conceivable stakeholder had to pass judgment on what I have negotiated.

d. The foregoing system maximizes individual choice

It does not guarantee unlimited choice and preference to all, but it does maximize choice as compared to rival systems.

e. Globalization: If we want to encourage political democracy, then we must encourage a free market economy⁶⁷

A non-democratized₂ free market system maximizes the potential for the rule of law and political (i.e., representative) democracy₁ in a global economy. There are no democratic regimes in the fullest sense that are not underpinned by a free-market economy. Some will claim that there are market economies that do not lead to political democracy. This is not the case. The foregoing claim identifies a market economy only with the existence of private property. A market economy implies private property,

⁶⁵ Accepting one's freedom and the responsibility that goes with it is a cause, to some, of great anxiety. It can appear as a serious burden.

⁶⁶ Defenders of the Rousseauian equality narrative oppose employment at will (see Patricia Werhane and Tara Radin, "Employment at Will and Due Process," in *Ethical Theory and Business*, 8th ed., pp. 266-74), whereas defenders of the Lockean liberty narrative are in favor of employment at will (see Richard Epstein, "In Defense of the Contract at Will," *University of Chicago Law Review* 34 [1984], and Alexei Marcoux, "The At-Will Doctrine in Employment and Employee Rights," Society for Business Ethics Session, American Philosophical Association Central Division Meeting, Chicago, IL, April 23, 2004).

⁶⁷ See Thomas Carothers, "The Democracy Nostrum," *World Policy Journal* 11 (1994), pp. 47-53; and Valerie Bunce, "Democratization and Economic Reform," *Annual Review of Political Science* 4 (2001), pp. 43-65.

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but the converse doesn't hold. There are many places in the world where private property exists within a quasi-feudal and mercantilist structure and without the rule of law (e.g., China).⁶⁸ It is not private property *per se*, but private property in a true free market protected by the rule of law that maximizes the benefits of the Technological Project. By a free market, I mean a system in which private property is freely alienable and freely acquirable, and there is no central allocation of resources. The rule of law is operative only in societies that are civil associations and that therefore recognize the primacy of personal autonomy. Achieving the rule of law and personal autonomy may be the most serious obstacles to participating in the benefits of the Technological Project, free-market economies, and limited government. The introduction of democracy into a culture that is not characterized by autonomy leads to the use of the political process to redistribute wealth, by which the many poor despoil the rich. This was Aristotle's warning, the concern of Alexis de Tocqueville and John Stuart Mill,⁶⁹ and it has more recently been reiterated by Arthur Okun.⁷⁰

f. The serious obstacles to the benefits of the Technological Project are cultural, not economic or political

Vast numbers of people both at home and abroad have failed to realize their autonomy, and this incapacitates them for full participation in the creation and enjoyment of the benefits from the Technological Project. Non-autonomous people⁷¹ are accustomed to having others direct their lives, to

⁶⁸ See Hernando de Soto, *The Other Path* (New York: Basic Books, 1989); and Hernando de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (New York: Basic Books, 2000).

⁶⁹ See Alexis de Tocqueville, *Democracy in America* (Baltimore, MD: Penguin, 2003 [1835]); and John Stuart Mill, *On Liberty and Other Writings*, ed. Stefan Collini (New York: Cambridge University Press, 1998 [1851]).

⁷⁰ See Arthur Okun, *Equality and Efficiency: The Big Trade-Off* (Washington, DC: Brookings Institute, 1982).

⁷¹ See Oakeshott's analysis of the "anti-individual" in his "The Masses in Representative Democracy." The rise of the autonomous individual "bred envy, jealousy, and resentment" in others. "And in these emotions a new disposition was generated . . . [F]rom the frustrated 'individual manque' there sprang the militant 'anti-individual', disposed to assimilate the world to his own character by destroying the individual and destroying his moral prestige"; *ibid.*, p. 372. Oakeshott notes as well that the morality of the anti-individual is "not of 'liberty' and 'self-determination', but of 'equality' and 'solidarity . . . the love of the 'community' . . . All must be equal and anonymous units in a 'community'," *ibid.*, pp. 374-75. He says further, "The rights called for on his [anti-individual] behalf [include] . . . [s]ecurity against having to make choices for himself and against having to meet the vicissitudes

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living under a feudal system of influence-seeking rather than a legal system that protects their rights, and to seeing political democracy as a means of increasing economic advantage at someone else's expense through redistributive policies rather than as a means of protecting and promoting economic growth.⁷²

of life from his own resources . . . [and] the right to live in a social protectorate which relieved him from the burden of 'self-determination,'" *ibid.*, pp. 377-78.

⁷² One of the reasons for the success of the "Asian Tigers" (Singapore, Taiwan, Korea, etc.) and the present high growth in China is that the quasi-authoritarian element in many Asian cultures serves as a barrier to democratic redistributive tendencies.

The Need for Realism in Business Ethics¹

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1. Introduction

Although conventional approaches to business ethics have been successful in spawning an industry, and in encouraging pernicious public policy, they suffer from fundamental confusions. Lacking realism about business or ethics, the prevalent trend in business ethics undermines both genuinely ethical conduct and individual freedom.

The prevalent trend in business ethics, referred to here as 'the conventional approach', consists of an unfortunately broad range of academic and popular doctrines. What they have in common, is the claim that businesses, and people in their business capacities, must pursue some objective other than owner value in order to be moral. Whether expressed in the language of corporate social responsibility ('CSR') or stakeholding, the 'triple bottom line' or 'corporate citizenship', conventional approaches typically identify extraneous responsibilities that businesses allegedly owe to others; fulfilling such 'social responsibilities' is what constitutes conventional business ethics. Starting with faulty assumptions, and applying defective theories, CSR as conventionally understood could well stand for 'Coercive Specious Reasoning' or 'Counterproductive Stakeholder Regimentation'.

2. Fundamental Confusions

a. Failure to differentiate 'business' and 'corporation'

The lack of understanding that is characteristic of the conventional approaches starts with the ostensible object of their attention. Conventional business ethics and corporate social responsibility both typically assume that 'business' and 'company' are the same. They are, however, categorially different. 'Company'—'corporation'—designates a particular organisational structure, which can have any objective agreed by its shareholders: it need not be, and frequently is not, business. 'Business', in contrast, designates a particular objective: maximising owner value over the long term by selling goods or services². That definitive

¹ This version of 'The Need for Realism in Business Ethics' replaces the one originally published as pp.33-48 of *Reason Papers* Vol.31 (Fall 2009); that previous version was distorted in the course of publication and should not be used.

² Sometimes abbreviated to 'maximising long-term owner value' or just 'owner value'. For a detailed derivation, justification and explanation of this characterisation of business, see

business objective is most commonly pursued *not* through corporations, but via sole proprietorships and partnerships. When, therefore, advocates of business ethics address themselves to companies, and use the language of *corporate* social responsibility, they neglect the majority of businesses that are not corporate in form. Conversely, when CSR advocates assume that companies must be businesses, they routinely misrepresent the requirements of both corporate governance and of corporate responsibility.

b. Failure to recognise the role of purpose

Conventional approaches to business ethics and CSR suffer from considerably more egregious confusions concerning the relation of business and ethics. They typically fail to recognise two very basic truths: that only a *business* can be an ethical business, and that what counts as an ethical business depends crucially on the purpose of business.

Artefacts and activities are most sensibly evaluated by reference to their definitive ends. The criteria of a good handkerchief are different than those of a good razor, because the purposes of handkerchiefs and razors are different. The purposes of businesses, families, churches and governments are equally dissimilar: each has a distinctive objective that both differentiates it from every other activity or organisation, and that determines the appropriate standards for assessing its conduct. The application of inappropriate, extraneous standards—of care from families, for example, or of equality from citizenship—is typically what leads conventional approaches to business ethics mistakenly to consider business as such not to be (sufficiently) ethical.

According to the conventional approach, business is ethical, or 'socially responsible', only if it pursues some 'socially responsible' objective: common candidates include 'corporate citizenship', 'stakeholder interests', and the 'triple bottom line'. But though such views are very widely held, they are, nonetheless, literally absurd. Business is a specific activity, with a definitive end, that of maximising long-term owner value. Well-ordered non-business corporations ('not-for-profits') similarly have specific objectives that define their reasons for being — housing the homeless, for example, or finding a cure for cancer. To the extent that businesses or corporations pursue something other than their definitive purposes, they fail to be organisations of the designated sort. But such deviation is just what conventional business ethics and CSR demand. It's no wonder, then, that conventional business ethics is so often dismissed as an oxymoron. It's because, as understood conventionally, it is genuinely oxymoronic: it makes refraining from business the condition of being responsible or ethical by business.

Proponents of the conventional approaches may now protest: they don't

Elaine Sternberg, *Just Business: Business Ethics in Action* (second edition; Oxford University Press, 2000; first edition, Little, Brown & Co (U.K.) Ltd, 1994), especially Chapter 2.

usually advocate abandoning the business purpose. They merely want to restrain it, by combining it with other, supposedly more worthy ends. When goals conflict, however, one must take precedence. For CSR advocates, it is typically 'social responsibility' that dominates, and the corporate or business purpose that gets sacrificed.

3. The Stakeholder Doctrine Repudiated

The business objective, and thus the possibility of ethical business, is always excluded by one of the commonest bases of conventional business ethics and CSR: the profoundly defective Stakeholder Doctrine. The term 'stakeholder' is popularly associated with three different views. Two are commonplace and have no particular moral significance; the third is largely incoherent. If taking a stakeholder approach simply means recognising that people are more likely to take an interest in a process when they are materially involved in its outcome, then stakeholding is an important notion, but one that is neither distinctive nor new. Similarly, if stakeholding simply means recognising that a wide variety of interests must ordinarily be taken into account when pursuing organisational objectives, then all that is exceptional about it is the label; the underlying truth has long informed successful practice.

It is only when force is added to those traditional observations that the 'Stakeholder Doctrine' (also known as 'Stakeholding' or the 'Stakeholder Model') emerges as something distinctive. The Stakeholder Doctrine has two essential tenets: organisations should be run for the benefit of, and should be accountable to, all their stakeholders.³ This third version is not about motivation or functional relationships, but about entitlements. It is the one that is typically associated with, and invoked to justify, conventional business ethics. It is therefore only this third, entitlement, sense of stakeholding that will be considered and criticised here.

The definition of 'stakeholder' commonly associated with Stakeholding is the one introduced by R. Edward Freeman: "A stakeholder in an organization is (by definition) any group or individual who can affect or is affected by the achievement of the organization's objectives."⁴ Here 'achievement' refers to the activity of pursuing those objectives, not just success in doing so. Officially adopted by the European Union⁵, this definition of stakeholder excludes all criteria of materiality,

³ See, for example, the many works of R. Edward Freeman, including his 'A Stakeholder Theory of the Modern Corporation', in Beauchamp & Bowie, eds., *Ethical Theory and Business*, 7th ed., (Englewood Cliffs, NJ: Prentice-Hall, 2004), pp.55-64.

⁴ R. Edward Freeman, *Strategic Management: A Stakeholder Approach* (Boston: Pitman Publishing, 1984), p.46.

⁵ *EU Green Paper Promoting a European framework for corporate social responsibility* (European Commission Directorate-General for Employment and Social Affairs, Unit EMPL/D.1, July 2001; henceforth 'EUcsr'), Concepts Annex, p.28.

immediacy and legitimacy. Given the increasing internationalisation of modern life, and the global connections made possible by improved transportation, telecommunications and computing power, those affected (at least distantly and indirectly) by any organisation include virtually everyone, everything, everywhere. Terrorists and competitors, vegetation, nameless sea creatures and generations yet unborn are amongst the many groups which are now seriously considered to be business stakeholders. Most of the criticisms would, however, apply even if 'stakeholder' referred only to some more limited subset, such as shareowners, employees, suppliers, lenders, and customers.

a. The Stakeholder Doctrine is incompatible with business

The Stakeholder Model is typically offered as an alternative to the shareholder model of business. But far from being a sensible model of either business or other substantive organisational objectives, Stakeholding is not even compatible with them. The Stakeholder Doctrine automatically precludes substantive objectives, because it requires that what organisations be run *for*, is the benefit of *all* their stakeholders; according to Stakeholding theory, providing benefits for all stakeholders is the only legitimate organisational purpose. The Stakeholder Doctrine thus precludes all objectives that exclusively or primarily benefit particular groups. Business as the activity of maximising long-term owner value is automatically ruled out; so are the different organisational objectives of providing education for inner-city children and employment for the blind.

Once again, advocates may protest: what they champion is not dispensing with business and other particular objectives, but pursuing them while also serving the interests of all the stakeholders. If, however, that criterion could be satisfied simply by providing widespread benefits, then the Stakeholder Model would not constitute an alternative to the shareholder model. As Adam Smith famously observed in *An Inquiry into the Nature and Causes of the Wealth of Nations*⁶, 'By pursuing his own interest [an individual] frequently promotes that of the society more effectually than when he really intends to promote it.' Business pursuit of owner value routinely benefits not just owners, but employees and investors, customers and communities. But benefiting other groups incidentally is not enough to satisfy the Stakeholder Doctrine. It demands instead that benefiting all stakeholders be the purpose of the organisation.

That essential Stakeholder aim of providing benefits for all stakeholders is, however, inherently ill-defined. First, it does not indicate in which of their many overlapping and often conflicting capacities individuals or groups are to be considered stakeholders: people often are employees, customers and shareholders of the same organisation. Second, the Stakeholder Doctrine provides no criteria of what constitutes a stakeholder benefit. Despite the simplifying and often presumptuous assumptions that are commonly made, even members of the same

⁶1776: IV, Ch.2, para 9.

notional stakeholder constituency may have significantly different views as to what is beneficial. Some employees want higher wages, others want shorter hours; some regard more responsibility as a benefit, others consider it to be a burden. How are stakeholders' divergent perceptions of benefit to be discerned and coordinated?

Third, and most fundamentally, even if the relevant stakeholders and benefits could somehow be identified, the Stakeholder Doctrine provides no guidance as to how they are to be balanced. Given the divergent interests of the different stakeholders, that which benefits some will often harm others; higher wages for employees, for example, can mean higher prices for customers and/or lower returns for owners. The Stakeholder Doctrine gives no clue as to how to rank or reconcile the normally conflicting interests of stakeholders.

Lacking such a criterion, the Stakeholder Doctrine affords each stakeholder—including the managers—the flexibility to favour his own interests when holding the organisation accountable: each stakeholder can elevate his own interests over the interests of the other stakeholders and also over the ostensible organisational objective. With each stakeholder holding the organisation accountable for pursuing some distinct, different (and probably incompatible) end, the notional substantive goal of the organisation is unlikely to be achieved.

Moreover, how is the multiple accountability required by the Stakeholder Doctrine meant to operate? A Stakeholder business is supposed to be accountable to all of its stakeholders. This presumably means that the managers, employees and other agents of the Stakeholder business are accountable to all of the business's stakeholders instead of just to its owners. But the managers, employees and other organisational agents are themselves stakeholders of the business. The Stakeholder Doctrine would seem to render them accountable *inter alia* to themselves, without offering any explanation of how such multiple self-accountability might work.

In such circumstances, it becomes understandable that the role of management in a Stakeholding organisation is reduced from pursuing substantive objectives to (at most) balancing stakeholders' benefits. It is because, being accountable to all of the stakeholders, and having somehow to reconcile the stakeholders' conflicting interests, managements typically have neither occasion nor incentive to pursue substantive ends.

To the extent, therefore, that an organisation satisfies the essential requirements of the Stakeholder Doctrine, and is run for the benefit of and is accountable to all its stakeholders, it will not be pursuing the business objective. Considered abstractly, such undermining of business might well be favoured by defenders of the Stakeholder Doctrine, and by proponents of the conventional approaches to business ethics and corporate social responsibility⁷. But the massive

⁷ See, for example, Jarol Manheim, 'Biz-War: Origins, Structure, and Strategy of Foundation-NGO Network Warfare on Corporations in the United States', paper delivered at an AEI conference in 2003; www.aei.org/docLib/20040402_20030611_Manheim.pdf.

economic contraction that would result is unlikely to be as welcome. Moreover, when business is ruled out, so is the possibility of ethical business....

b. The Stakeholder Doctrine undermines accountability

The possibility of ethical business is further reduced by the Stakeholder Doctrine's incompatibility with efficacious agency and accountability. In asserting that organisations should be accountable to *all* their stakeholders, the Stakeholder Doctrine denies that agents have any special duty to their principals as ordinarily understood. Accountability that is diffuse, however, is effectively nonexistent; an organisation that is notionally answerable to everyone, is actually answerable to no one. The only way that multiple accountability can function is if everyone involved accepts a clear common purpose. But well-defined purposes are incompatible with the Stakeholder Doctrine.

c. The Stakeholder Doctrine is unjustified

Not surprisingly, a Doctrine suffering from such fundamental conceptual and practical defects is as difficult to justify as it is to implement. Stakeholder supporters typically proceed without argument from the undeniable fact that organisations affect and are affected by certain factors, to the unjustified conclusion that organisations should be run for and accountable to them. But that is neither right nor reasonable. Business must take many factors into account, including, among others, terrorists and burglars. But businesses can hardly be run for their benefit. Nor does the fact that various groups are affected by business, give them any right to control it: consider competitors. Moreover, do Stakeholder advocates appreciate that if their creed did legitimately render Shell accountable to Greenpeace, it would equally render Greenpeace accountable to the National Rifle Association?

A few Stakeholder supporters have acknowledged that their Doctrine's reductive organisational end and multiple accountability require justification. But though their efforts to support the Doctrine have invoked grounds as diverse as economic efficiency and Kantian deontology, all have been conspicuously unsuccessful⁸. The lack of justification has not, however, deterred advocates of conventional business ethics from relying upon the Stakeholder Doctrine. Indeed, perhaps the most notable achievement of academic business ethics has been the extent to which the term 'stakeholder' has become embedded in ordinary language.

⁸ It is noteworthy that R Edward Freeman, perhaps the foremost proponent of the Stakeholder approach, has progressively retreated in response to criticism: "... attempts to more fully define, or more carefully define, a stakeholder theory are misguided.... Stakeholder is thus a genre of stories about how we could live..." ('The Politics of Stakeholder Theory: Some Future Directions', *Business Ethics Quarterly*, Vol 4, 1994, pp.413-15). The normative core (the 'Doctrine of Fair Contracts') of his own preferred 'story' of 'pragmatic liberalism' (Ibid, p.415) does, however, suffer from the defects of Stakeholder Doctrine, as well as from other defects.

d. Key implications of the Stakeholder Doctrine

Despite — or perhaps because of — its defects, the Stakeholder Doctrine is extremely popular. One reason, is that those defects are seldom acknowledged. Another, is that Stakeholding attracts the promoters of worthy 'causes', who (unrealistically) believe they would be the beneficiaries if organisational (and particularly business) assets were diverted from their owners to other stakeholders. Crucially, the Stakeholder Doctrine also appeals to those who would gain from undermining accountability, in particular to the managers and politicians who want the power, prestige and perks of office without the concomitant responsibilities.

Conventional business ethics, CSR, and the Stakeholder Doctrine are well suited to serving authoritarian and collectivist political ends. Their nominal association with unobjectionable doctrines lends them a superficial plausibility; their apparent generosity encourages people to accept them uncritically. And their central features—the lack of an objective standard of action, the radical undermining of accountability—mean that they can be invoked to support almost any kind of state intervention, no matter however intrusive or restrictive. It is therefore hardly surprising that conventional business ethics, CSR and Stakeholding have increasingly informed official government policy in the United States, Britain and the European Union.⁹

4. Conventional Business Ethics is Counterproductive

So conventional business ethics and CSR are politically suspect as well as intellectually defective. In addition, they are fundamentally counterproductive. Oxy-moronic and uneconomic, they would actively undermine both the ethical

⁹ In respect of, for example, directors' duties, takeovers and pension fund investments. In the U.S., stakeholder interests had been recognised in connection with directors' duties in thirty-one states by 1999; 'From the Hustings: The Role of States with Takeover Control Laws', *Mergers & Acquisitions Journal*, 1 October 1999.

In Britain, protection of specific stakeholder interests has been enshrined in at least forty-four main U.K. statutes, in addition to statutory instruments and EU regulations (Confederation of British Industry, *Boards without tiers*, October 1996, p.23; *EUcsr*, op.cit., note 5 above, p.27). The 'stakeholder economy' was the Labour Party's initial 'defining theme' for the 1997 general election campaign (Robert Peston, 'Votes at stake over vision for economy', *Financial Times*, 11 January 1996, p.5). And disturbingly, the stakeholder doctrine was one of the 'three pillars' that underpinned the recent review of U.K. company law (Consultation Document, *Modern Company Law for a Competitive Economy*, Department of Trade and Industry Publications, 4 March 1998, especially paras. 5.1, 5.2 (i)(b)). It was designated the 'pluralist approach' in the section on the scope of company law (para 5.1.13, p.37); without any label, it was the basis for proposals for major changes in U.K. company formation procedures. Since 2000, trustees of occupation and local government pension schemes have had to disclose socially responsible investment (SRI) policies as part of the Statement of Investment Principles (SIP).

conduct they claim to support, and basic human rights.

a. Conventional business ethics is irresponsible and unethical

The fundamental responsibility of an organisation, or of individuals in their organisational capacities, is achieving the organisation's official purpose. Contracts of employment normally commit employees to supporting their employer's goals; corporate directors have an even stronger, fiduciary, responsibility to pursue the official corporate objective. Sacrificing that organisational purpose, or subordinating it to some other end, constitutes a violation of the core organisational responsibility. But that is what is required by conventional approaches to business ethics. Inciting employees to betray their employers' trust is a strange way of promoting responsibility.

Genuinely ethical conduct is also unlikely to ensue when the particular ends advocated in the name of conventional business ethics, and the methods used for promoting them, are themselves both immoral and irresponsible. Recall Greenpeace's attack on Shell over the disposal of the Brent Spar oil rig. In the name of environmental protection and 'social responsibility', ends enthusiastically endorsed by conventional business ethics, Greenpeace grossly misrepresented the dangers of disposing of the oil rig in the North Sea. As a result, the disposal was more harmful for the environment, substantially riskier for the disposal workers, and more wasteful than it would have been had Shell's original plan been followed.¹⁰ Though counterproductive, Shell's capitulation was hailed as a notable victory for social responsibility.

b. Conventional business ethics undermines human rights

An even more profound defect of business ethics as conventionally advocated, is that it would undermine basic human rights. It does so necessarily, because it subverts the private property that is essential for defending and exercising fundamental individual liberties. Conventional business ethics subverts private property by denying that owners have any special right to determine how their property will be used: insofar as assets are held or utilised by organisations, conventional business ethics stipulates that those assets must be used for 'socially responsible' purposes. And to the extent that conventional CSR encourages stakeholder appropriation of those assets, it promotes what would otherwise be regarded as theft. When corporations are highjacked from the ends determined by their shareholders, or business assets are diverted from business uses, owners are denied fundamental rights. In obliging them to serve ends other than those the owners have chosen, champions of conventional business ethics would treat the owners as slaves.

The essentially illiberal nature of conventional business ethics and CSR is

¹⁰ Jon Entine, "Shell, Greenpeace, and Brent Spar: The Politics of Dialogue" in *Case Histories in Business Ethics*, eds. Chris Megone and Simon J. Robinson (London: Routledge, 2002), pp.59-95.

further revealed by the 'social contract' argument often claimed to support them. Whereas Hobbes and Locke invoked the notion of a social contract to limit authoritarian power, the CSR version attributes authoritarian power to society. It alleges that in exchange for society's consenting to provide the resources that businesses and corporations need to exist, and granting them a 'licence to operate', organisations become accountable to society. The argument thus presupposes a society that is not free: in free societies, whatever is not expressly prohibited is allowed, and strict limits apply as to what may be officially prohibited. All the powers needed to form and run organisations—the ability to associate, to enter into commitments (including market exchanges), to enforce those commitments (by, e.g., ostracising offenders), etc.—are possessed naturally. Enlisting the willing cooperation of counterparties is indeed essential to organisational formation and operation, but consent in the sense of formal permission is largely irrelevant.

Since no 'licence to operate' is necessary, the CSR 'social contract' argument either confuses consent with functional responsiveness, or it constitutes a threat: it asserts that businesses and corporations must submit themselves to society's requirements, lest society prevent them from operating.¹¹ That challenge looks very like extortion. Requiring submission as the condition for not inflicting harm is not entering into a social contract, but running a protection racket. The fact that muggers may kill you if you do not surrender your money, does not give muggers the right to appropriate your money or to control your life; it simply means that they are capable of theft and murder. Claims to justify legitimacy require demonstrations of entitlement, not displays of brute force.

The threat to human rights is exacerbated when conventional business ethics and CSR are backed by law. Enforced CSR regulation prevents 'capitalist acts between consenting adults'¹²; it deprives stakeholders of the freedom to live their lives as they think best. That such regulation may be inspired by an ethical motive (real or otherwise), or directed at an ethical objective, may well make it more popular; it does not reduce its coercive nature, or increase its ability to produce genuinely virtuous conduct. Coercive regulation typically makes things worse for everyone, including those it was intended to benefit... as the current economic downturn has dramatically demonstrated.¹³

¹¹ Cf. the much cited 'Iron Law of Responsibility': "In the long run, those who do not use power in a manner which society considers responsible will tend to lose it."; Keith Davis and Robert L. Blomstrom, *Business and Society: Environment and Responsibility* (3rd ed.; New York: McGraw-Hill Book Co, 1975), p.50. The 'license to operate' argument goes further, in presupposing that the ordinary operations involved in conducting business are *privileges*, to be granted or withdrawn by some central authority.

¹² Robert Nozick, *Anarchy, State, and Utopia* (New York: Basic Books, 1974), p.163.

¹³ See Philip Booth, ed., *Verdict on the Crash: Causes and Policy Implications* (London:

All enforced prescriptions and proscriptions are inherently coercive. They restrict liberty, strictly defined as the absence of physical aggression or threats thereof initiated against persons or their property by other persons. In limiting liberty, however, all imposed regulation also reduces the realm of ethical action. It's a commonplace of ethical theory that 'ought implies can'. But it's equally true that normally 'ought presupposes cannot'. In order to be acting ethically, an agent must be able to do—or not do—the right thing, and must do it freely, deliberately and characteristically. Ethical conduct is thus precluded in respect of anything that is either effectively banned or made compulsory. Legal regulation to enforce business ethics significantly narrows the scope for genuinely ethical action.

c. Unethical law

The use of coercive power is especially harmful when what the law requires is itself unethical. Conventional approaches to business ethics and CSR usually assume that the requirements of law are compatible with those of ethics, though often laxer than them; the few counterexamples acknowledged—those supporting slavery or apartheid, for instance—are typically taken from jurisdictions that are temporally or geographically distant. But the United States, Britain and the European Union all have laws and regulations enacted in the interests of corporate social responsibility that actively penalise ethical business. Examples include quotas that require favouring some designated group independent of their suitability for maximising long-term owner value, and much worker/ consumer protection regulation. Many of the government policies that gave rise to the sub-prime mortgage crisis, and the government responses that have exacerbated it, were also enacted in the name of 'social responsibility', and similarly penalise ethical conduct.

Those examples may well be controversial. But the judgement that betrayal is unethical would, one hopes, be widely accepted. Nevertheless, U.S. federal law forces some businesses to choose between betraying their employees and betraying their owners; they can satisfy the law only by violating their ethical obligations. This dilemma results from the combination of the Department of Justice's post-Enron enforcement policies, strict liability for corporate criminality, and the U.S. Federal Sentencing Guidelines.¹⁴ The 1991 addition of a special chapter on

Institute of Economic Affairs, 2009), especially the Introduction, and Chapter 4 (Eamonn Butler, 'The Financial Crisis: Blame Governments Not Bankers').

¹⁴ For detailed explanation and justification of this position, see the work of John Hasnas, including "Managing the Risks of Legal Compliance: Conflicting Demands of Law and Ethics" 39 *Loyola University Chicago Law Journal*, 507 (2008); "Up from Flatland: Business Ethics in the Age of Divergence," 17 *Business Ethics Quarterly*, 399 (2007) (Best Paper, 2006 Society for Business Ethics annual conference); *Trapped: When Acting Ethically Is Against the Law* (Cato Institute, 2006); "Do Nothing", *Wall Street Journal*, September 16, 2006; "Department of Coercion", *Wall Street Journal*, March 11, 2006; "Unethical Compliance and the Non Sequitur of Academic Business Ethics," 21 *Journal of*

organizational crime to the Sentencing Guidelines is often cited as having been a major stimulant of the business ethics industry, because it counted having an ethics programme as a factor that could reduce sentences for certain federal offences. Interpreted in accordance with the Department of Justice's Thompson Memorandum, however, the results are positively unethical by almost any standards.

Under strict liability for corporate criminality, a firm can be convicted of wrongdoing simply because one of its agents did something unlawful... even if the allegedly illegal act was not intended by the business, and did not benefit the business... even if the agent was acting in direct opposition to the firm's official policy. According to the Thompson Memorandum,

Corporations can attain the lowest possible culpability score by having an effective compliance program and by cooperating with the government.¹⁵ To have an effective compliance program, a corporation must 'monitor and audit' the behavior of its employees to detect criminal conduct and impose 'disciplinary measures,' (typically firing) on those who engage in it.¹⁶ To cooperate with the government, a corporation must report any suspected wrongdoing to the government; disclose to the government 'all pertinent information known by the organization' about such wrongdoing, whether or not protected by attorney-client privilege or other promise of confidentiality; refrain from advancing legal fees to or entering into joint defense agreements with its employees; and accept responsibility for the wrongdoing, which means being willing to plead guilty because the 'adjustment is not intended to apply to an organization that puts the government to its burden of proof at trial.'¹⁷

It's hardly surprising that the Organizational Sentencing Guidelines have been described as 'an extraordinarily effective device for undermining all of the civil

Private Enterprise 87 (2006), henceforth 'Unethical Compliance'; and "Ethics and the Problem of White Collar Crime", 54 *American University Law Review* 579 (2005).

¹⁵ See United States Sentencing Commission, *Guidelines Manual*, henceforth 'USSG'), Art. 8C 2.4-2.6 (1992).

¹⁶ USSG, Art. 8B 2.1(b)(6).

¹⁷ USSG, Art. 8C2.5(g)(1) and 8C 2.5, comments 12 and 13. Full passage quoted from Hasnas, 'Unethical Compliance', op.cit., p.10.

libertarian protections of the traditional criminal law'.¹⁸ Recognising its defects, the U.S. Court of Appeals ruled on 28 August 2008¹⁹ that the Thompson guidelines were unconstitutional. While this was a welcome step, especially insofar as it protected privileged information, the old rules continue to govern the Securities and Exchange Commission²⁰ and other federal agencies.²¹

This may seem a distant danger to those without U.S. business operations. But there are no grounds for complacency elsewhere. The British government's attempts to enforce CSR through the use of Anti-Social Behaviour Orders ('ASBOs')²² are also troubling. ASBOs are civil orders, intended 'to protect the public from behaviour that causes or is likely to cause harassment, alarm or distress'; they can be issued on the basis of hearsay.²³ Nevertheless, breaches are a criminal offence, and can render violators liable to five years' imprisonment. So civil liberties are definitely at risk from policies adopted in the name of corporate social responsibility.

¹⁸ Ibid.

¹⁹ When the Department of Justice also issued new guidelines for the second time in ten months.... Department of Justice, *Justice Department Revises Charging Guidelines for Prosecuting Corporate Fraud*, August 28, 2008; <http://www.usdoj.gov/opa/pr/2008/August/08-odag-757.html>.

²⁰ Via the Seaboard Report (*Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions*, Exchange Act Rel. No. 34-44969 (Oct. 23, 2001), available at <http://www.sec.gov/litigation/investreport/34-44969.htm>); cited in <http://www.wilmerhale.com/publications/whPubsDetail.aspx?publication=3507>.

²¹ E.g., the Environmental Protection Agency; CNN Money News, 'Fed ruling: Attorney talk confidential; Justice Department ruling says federal prosecutors can't strong-arm corporate suspects into waiving attorney-client privilege.' August 28, 2008: 4:51 PM EDT; available online at http://money.cnn.com/2008/08/28/news/companies/corp_prosecutions/index.htm?postversion=2008082816.

²² Julia Pearlman, 'Head of Marketing company slams ASBO ruling in historic flyposting case', *Brand Republic*, 24-Mar-05, 11:00: <http://www.brandrepublic.com/news/467860/head-marketing-company-slams-asbo-ruling-historic-flyposting-case/>; 'Music company spared ASBO over fly-posting pledge', 14/06/2004; http://www.manchester evening news.co.uk/news/s/121/121093_music_company_spared_asbo_over_flyposting_pledge.html.

²³ *A Guide to Anti-Social Behaviour Orders*, Home Office. August 2006. Ref: 275335.

d. The dangers of appeasement

Unfortunately, despite the defects of the conventional approach to business ethics and CSR, it is endorsed by many businesses: they have perhaps sought to deflect the activists' wrath by consulting them, appearing to agree with them, and even funding them in hopes of buying approval. Such 'renegade capitalists' lend credence to the false belief that the conventional standards are legitimate, and fortify expectations that they should be generally applied. Some businesses even misguidedly seek CSR regulation, apparently believing that they will gain if the burden of fulfilling 'social responsibilities' is imposed by law on their actual and potential competitors. But pandering and appeasement are always dangerous tactics. Businesses that even appear to accept the activists' standards render themselves liable to be judged by them, and subjected to ever more stringent demands: pandering is more likely to stimulate than to satisfy the activists' requirements. As has been observed²⁴, it's like trying to convert a crocodile to vegetarianism by feeding it your leg....

5. Realist Business Ethics

Fortunately, appeasement is unnecessary as well as counterproductive. Contrary to popular opinion, what is needed for a business to be ethical or responsible has nothing to do with the conventional, oxymoronic demands.

Business ethics is about conducting *business* ethically... which means pursuing the business objective while satisfying two straightforward ethical constraints. The operative constraints are just the ones that must be respected for the purpose of business—maximising owner value over the long term by selling goods or services—to be possible. Long-term views require confidence in a future, and confidence requires trust; consequently, the conditions of trust must be observed. Equally, owner value presupposes ownership, and therefore respect for property rights. In order not to be ultimately self-defeating, business must be conducted with honesty and fairness, and without initiating physical violence or coercion. These three conditions constitute what may be called '*Ordinary Decency*'. When the Realist approach to business ethics was initially developed (in the 1994 first edition of *Just Business: Business Ethics in Action*), Ordinary Decency also included a presumption in favour of legality. But the increasingly cavalier attitude of even the U.S. and U.K. governments has made that presumption ever less plausible.

The other essential ethical constraint on business activity is classical '*Distributive Justice*'. This notion has nothing to do with modern attempts to redistribute income on ideological grounds. Rather, it expresses the fact that business is more likely to achieve its definitive purpose when it encourages contributions to that purpose, and not to some other. Though the term may be

²⁴ By Fred Smith of the Competitive Enterprise Institute.

unfamiliar, the underlying concept is widely recognised. It is implicit in the commonly held view that productive workers deserve more than shirkers; when properly structured, both performance-related pay and promotion on merit are expressions of Distributive Justice. What Distributive Justice requires is simply that within an organisation, contributions to the organisational objective be the basis for distributing organisational rewards.

The key to Realist business ethics is very simple: *business is ethical when it maximises long-term owner value while respecting Distributive Justice and Ordinary Decency*. If an organisation is not directed at maximising long-term owner value, it is not a business; if it does not pursue that purpose while satisfying Distributive Justice and Ordinary Decency, it is not ethical.

a. 'Good ethics is good business'

This Realist approach helps explain the ways in which it is (and is not) true that 'good ethics is good business'. Conventional social responsibility and business ethics require diverting assets and attention from the official organisational purpose to extraneous ends. They are therefore liable to impede, when they do not altogether prevent, achievement of the organisational purpose.²⁵ Realist business ethics, in contrast, requires business to pursue its definitive end: to be an ethical business, an organisation must seek to maximise long-term owner value, subject only to respecting Distributive Justice and Ordinary Decency. Unlike current period accounting profits, owner value automatically reflects the distant, indirect and qualitative effects of a business's actions, including the ways in which it interacts with its stakeholders. Normally, therefore, owner value is enhanced when the business acts in accordance with Ordinary Decency and Distributive Justice. Nevertheless, 'good ethics is good business' is at most a slogan. It neither constitutes an ethical justification of ethical conduct by business, nor guarantees any association between ethical conduct and business success.

²⁵ A major academic study of CSR in 2006 confirmed that in the U.K. general industrials sector, firms with the *worst* record for community and environmental 'social responsibility' produced average returns 30% and 70% *higher* respectively than firms with the most 'responsible' scores (compared with FTSE benchmarks). See Brammer, Stephen, Brooks, Chris and Pavelin, Stephen, 'Corporate Social Performance and Stock Returns: U.K. Evidence from Disaggregate Measures', *Financial Management*, Vol. 35, No. 3, Autumn 2006, p.114; <http://ssrn.com/abstract=938725>, The study was unusual because it analysed data at the level of the firm (rather than comparing investment funds), disaggregated measures of corporate social performance ('CFP') based on EIRIS (Ethical Research Services) published data, and attempted to correct the results for factors such as company size, risk and industrial sector.

b. Social responsibility as 'conscientious stakeholding'

So 'business ethics' has a genuine meaning, but one very different than that which is conventionally supposed. So, too, does 'social responsibility'. Properly understood, 'social responsibility' does not refer to any organisational responsibility *to* stakeholders. It instead designates a responsibility *by* stakeholders, to act so that their values concerning society are reflected in their actions. Social responsibility is exercised when individuals express their own values in their own acts, acting separately or in concert.

What they choose has important consequences for business conduct, because the definitive business end of maximising owner value obliges businesses to heed stakeholder preferences. When each potential stakeholder—otherwise known as every member of society—acts conscientiously in his personal capacity, and strategically bestows or withholds his economic and other support on the basis of his moral values, free market forces will automatically lead businesses to reflect those values. To the extent that the term 'stakeholder' helps remind people of their individual responsibilities to act conscientiously, it can serve a valuable function.

'Ethical' investing, the 'green' consumer movement and the growth of 'vigilante consumerism' are examples of how such 'conscientious stakeholding' can influence the way business operates. 'Conscientious stakeholding' can affect the products that businesses produce, and the conduct of business in producing them, and the strategic direction and structure of businesses. 'Conscientious stakeholding' can even influence the extent to which business, as opposed to other human activities, is pursued at all. And this accords with what is normally expected of social responsibility.

But for society accurately to reflect people's values, those values need to inform individuals' daily choices, and be reflected in their purchases and practices. The true values of a society are expressed not in what people say, or in what they are eager to do with other peoples' money, but in what they actually do with their own. Achieving social goals by way of conscientious stakeholding may be slow, and the outcomes may sometimes be disappointing, but voluntary action is a necessary condition of ethical conduct... by individuals and by organisations.

6. Conclusion

In summary, then, organisational mission statements and political rhetoric promoting conventional business ethics may seem innocuous, but they reflect confused and dangerous doctrines. As conventionally understood, business ethics and corporate social responsibility imperil not just business profitability, but the existence of business itself. Even more fundamentally, they threaten private property, and the individual liberty that is essential for genuinely ethical conduct. Combating the conventional approaches to business ethics and corporate social responsibility requires recognising two basic facts: that only a business can be an ethical business, and that to be an ethical business, an organisation must maximise

long-term owner value while respecting Distributive Justice and Ordinary Decency. The need to proclaim these fundamental truths is particularly important now, when the economic crisis is falsely being attributed to market failure rather than government action, and business is actively under attack. Liberty and the possibility of genuinely ethical business both need, and deserve, protection from conventional business ethics.²⁶

²⁶ This paper draws heavily on material that was originally published and is more fully explained and justified in Elaine Sternberg, *Just Business: Business Ethics in Action* (second edition; Oxford University Press, 2000; first edition, Little, Brown & Co (U.K.) Ltd, 1994), and in Elaine Sternberg, *Corporate Governance: Accountability in the Marketplace* (second edition; Institute of Economic Affairs, 2004). Additional material was first presented in lectures delivered at the American Enterprise Institute 3 March 2006, at the University of Leeds-IDEA-CETL 11 September 2008, and at the University of Buckingham 12 March 2009.

The Virtue of Prudence as the Moral Basis of Commerce

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1. The Need for Moral Support

There are many ways of approaching human affairs, and one of these is by considering whether what people do is morally justified. Another is to consider what causes them to act or behave as they do. One may also want to focus on the overall impact their conduct has on others or on the future state of the world.

The issue I wish to address is the first one. And more specifically, I want to explore first of all whether commerce and its professional arm, business, enjoy moral support. Certainly there is much debate about this. Recently, for example, Pope Benedict stated, on his visit to Australia, that consumerism is morally objectionable. Earlier, one of the Pope's cardinals stated that both capitalism and communism are immoral. The idea that striving to make a profit is something morally suspect is also widely propounded in novels, movies, songs, and political speeches. Even for those who generally consider commerce beneficial, the private pursuit of wealth is deemed to be a vice: Bernard Mandeville developed this idea in full in his 1714 *Fable of the Bees: or, Private Vices, Publick Benefits*.¹ In popular discussions there is a widespread conviction to the effect that while sharing is morally admirable, profiting is not. And, of course, the pursuit of profit—or prosperity or wealth—is widely denounced by champions of systems such as socialism, communism, and communitarianism.

Yet, at the same time, no one can dispute that most people eagerly pursue wealth and would far more prefer to reap profits than to suffer economic losses. Indeed, the economies of most modern societies are based on this fact. Daily discussions in the media lament it when, for whatever reason, economies falter, incomes fall, businesses contract, and development is arrested. Few are champions of economic stagnation, let alone of outright poverty.

¹ Accessed online at: http://en.wikipedia.org/wiki/Bernard_Mandeville.

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So it would be something rather peculiar if not outright tragic for commerce, certainly a vital engine of prosperity, to lack moral standing. I will argue that it does indeed have moral standing because, ultimately, it is the institutional manifestation of the moral virtue of prudence. Furthermore, I will defend the idea that commercial and business conduct must be free, voluntary, and not regimented by government, in order for it to have moral significance.

2. Some Skeptical Problems

Among economists, however, the very idea of morality is viewed with great skepticism. Economists, on the whole, regard commercial activities as the function or result of certain innate proclivities, for example, the profit motive. As the late Milton Friedman, one of the modern age's most famous and diligent students of economics, puts it:

[E]very individual serves his own private interest. . . . The great Saints of history have served their 'private interest' just as the most money grubbing miser has served his interest. The *private interest* is whatever it is that drives an individual.²

Friedman's colleague, the late George Stigler, another Nobel Prize winner, makes the point only slightly differently:

Man is essentially a utility-maximizer—in his home, in his office (be it public or private), in his church, in his scientific work—in short, everywhere.³

Finally, Nobel Laureate Gary Becker, who may be the most explicit of those who embrace this *homo economicus* viewpoint, underscores the idea as follows:

The combined assumptions of maximizing behavior, market equilibrium, and stable preferences, used relentlessly and unflinchingly, form the heart of the economic approach as I see it.⁴

² Milton Friedman, "The Line We Dare Not Cross," *Encounter* (November 1976), p. 11.

³ George Stigler, Lecture 11, Tanner Lectures, Harvard University, April 1980, quoted in Richard McKenzie, *The Limits of Economic Science* (Hingham, MA: Kluwer Academic Publishers Group, 1983), p. 6.

⁴ Gary Becker, *The Economic Approach to Human Behavior* (Chicago, IL: University of Chicago Press, 1976).

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These and many other economists insist that commercial conduct or behavior isn't a matter of a free choice by people, but something they are driven to. They are hard-wired to seek to promote their economic well-being.

It is a very interesting issue whether these and other economists advance their economic determinist theory because they are convinced that human beings are indeed so constituted as to be profit maximizers or because this approach to understanding people avoids all issues of ethics. As Kant notes, "'ought' implies 'can'." That is to say, if one ought to do something, one must be free to choose to do it or not do it in several respects (metaphysical, psychological, political, etc.). So if human beings are *driven* to pursue profit, to be consumers, profit maximizers, then there could not be anything *ethically or morally wrong or right* with their commercial behavior any more than there is anything morally wrong or right with their breathing or the circulation of their blood. These are not matters of choice, so they are amoral and not open to moral evaluation. This, in turn, would have to pacify critics of commercial conduct; in effect, consumerism is just part of the very nature of human life and to blame people for it misses the point (or as some philosophers would say, is a category mistake).

I am not suggesting that these and other economists, such as Adam Smith, David Ricardo, Ludwig von Mises, as well as many others who eschew the idea of viewing economics in ethical or moral terms, deliberately misidentify human nature so as to be able to make room for commerce, which they know to be a "private vice."⁵ It is more a matter of their finding a frame of reference that casts the field of economics within the increasingly prestigious (social) sciences instead of the humanities. Arguably, they tend to follow the lead of the English philosopher Thomas Hobbes, who purges human life of morality by means of two important ideas: he denies free will, thus making it moot to speak of how people ought to act; and he denies the objectivity of values, of considerations of what is right versus wrong, good versus bad, by consigning them to the realm of the subjective, to what we feel like doing. As he puts it, "But whatsoever is the object of any man's appetite or desire, that is it which he for his part calleth good: and the object of his hate and aversion, evil. . . . For these words of good and evil . . . are ever used with relation to the person that useth them: there being nothing simply and absolutely so; nor any common rule of good and evil."⁶ Since the sixteenth century, the dominant way of thought has shifted from the religious to the

⁵ This is something suggested by Karl Marx when he calls some of the major classical liberals "ideologues."

⁶ Thomas Hobbes, *Leviathan*, ed. C. B. Macpherson (Baltimore, MD: Penguin Books, 1968), I.6, p. 120.

secular and scientific, which most intellectuals associate with the Hobbesian determinist and the value-free approach. (This does not mean that no evaluations are justified, only that no moral evaluations can be supported. Instrumental evaluations in the areas of economic or personal health, for example, are acceptable, but none are justified concerning what actions are morally right versus wrong, who is acting ethical versus unethical.)

The social sciences have tended to aspire toward this scientific status in large measure by embracing the value-free approach to understanding human affairs. Economics has been at the forefront of this trend, although there have been a few dissenters—for example, Karl Marx, John Stuart Mill, and John Maynard Keynes.

3. Revisiting the Ethical Issues

But there has always been some uneasiness about the value-free stance in social science, since, among other things, that stance itself involves certain moral or near-moral imperatives, such as, “One ought not to make value judgments when one works in the disciplines of the social sciences.” As with logical positivism, where the principle of verification undermines itself—“One ought to verify all meaningful statements by way of sensory data,” while that statement itself cannot be so verified—so in the social sciences the value-free approach itself is highly value-laden.⁷

In consequence, the discussion about the market economy often turns to ethics, despite the insistence of many economists that it shouldn't. And those in popular culture, as well as those writing in the less-than-technical journals, constantly debate whether commerce is ethical. The Pope as well as many prominent intellectuals (“public philosophers”) widely condemn commerce as materialist and hedonist, but is this ultimately rational and well supported? How would one go about answering this question?

Without trying to traverse the entire field of moral philosophy, including all of the problems of metaethics, I will only provide a reasonably suggestive hint that indicates that commerce is indeed a morally justified endeavor or, to put it less formally, it is morally okay to be a consumer, to go shopping, to want to prosper in life. Thus, just as it is morally okay to want to be healthy, so it is to be wealthy. The term “wealth care” parallels that of “health care,” and thereby indicates the gist of the argument in defense of the morality of commerce.⁸

⁷ Few people are more avid and righteous about what people may or may not do than economic positivists. See, for example, Michael A. Walker, ed., *Freedom, Democracy, and Economic Welfare* (Vancouver, BC: The Fraser Institute, 1988), and the exchange between Milton Friedman and me on whether moral judgments are legitimate.

⁸ Tibor R. Machan, *The Morality of Business: A Profession for Human Wealth Care* (New York: Springer, 2007).

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Such an argument begins with an understanding of human nature about which there is much skepticism. Yet those who would claim that human nature is unknowable or too variable need to be reminded of the following:

If human nature is unknowable then so is human good and it is impossible to talk about human excellence in general. Indeed it is impossible to talk about man as such, since man as such could not even be identified. Barring all knowledge of human nature—that which makes a man a man—the word man would mean nothing and we could not even conceive of man as a definite being distinguishable from all other beings. Consequently anything we might say about man would be necessarily meaningless, including the statement that human nature as such is unknowable to man. Thus the postulate of the strict unknowability of man is self-contradictory. To the extent that we talk about man we obviously hold that his nature is, in some respect at least, knowable.⁹

Once it is understood that a knowable human nature exists, ethics can be seen as analogous to health, with the difference that in the case of health much of it is out of our control, whereas with ethics or the morally good life human beings are free to pursue or neglect it.

As to the similarity, just as there are very general principles of good health, so there are general principles of a morally good life, health being only an aspect of such a good life. By analogy with health, although there are general principles one may follow to attain it, there are also specific edicts having to do with one's specific, particular identity, with *who* one is, not just with *what* one is.

The principles of ethics, as those of health, can be general, stable, but also varied based on particular attributes of the agent. The practice of principles of good health is, thus, similar to the practice of principles of ethics, the moral virtues. Because of the variability of human identity, because of the great variety of ways human nature is instantiated, ethics is by no means uniform. What one person ought to do to live ethically will not be the same as what another ought to do except in some very general terms, such as “be honest,” “be courageous,” or “be prudent,” comparable to the medical advice “be fit,” “eat healthy,” “avoid overindulgence.”¹⁰

⁹ Laszlo Versenyi, “Virtue as a Self-Directed Art,” *The Personalist* 53 (Summer 1972), p. 282.

¹⁰ The approach here is akin to those found in Ayn Rand, *The Virtue of Selfishness: A New Concept of Egoism* (New York: Signet Books, 1964); Martha Nussbaum, *The Therapy of Desire: Theory and Practice in Hellenistic Ethics* (Princeton, NJ: Princeton

4. Stable Principles

Are ethical principles universal? Some are, just as some principles of health are universal, although many are binding within contexts that are variable. For example, although all parents are responsible for raising their children so as to prepare them for successful adulthood, the details of this imperative will vary depending on circumstances, historical period, technology, economic preparedness, and so on. What is reasonably well known is that some principles of conduct apply to everyone, at all times. For example, a general principle such as “One ought to be attentive to the challenges facing one’s life” is universal or, perhaps better put, generally true and stable. This is, indeed, the virtue of prudence or right reason. And it is general enough so that it applies to any human being regardless of circumstance.

It is important to keep in mind here that prudence means taking reasonable care of oneself, but what that implies depends on the sort of self we have. Suppose that we all have what we might call a dual self, one partly of this mundane or natural world, another partly of another, spiritual one. A prudently lived life would then need to attend to the needs of both of these parts of one’s self.

I will not endeavor to resolve the controversy over dualism versus monism concerning human nature, but I defend the idea that the mundane part of one’s self is significant and requires close attention, to be taken good care of. And here is where aspiring to a reasonable degree of economic—or what some call “material”—prosperity arises. It is an ethical imperative to be prudent about one’s earthly life. This includes such matters as physical well-being, fitness, a reasonable level of pleasure and happiness, as well as prosperity. And since prosperity is evidently and considerably enhanced by productivity and commerce, including the profession of business, the moral basis of business is difficult to deny. Disregard for one’s economic well-being is morally irresponsible. Since the professionals in business, whom we may designate as wealth care professionals, provide us with the services needed to maintain and achieve prosperity—just as the professionals in medicine, whom we call health care professionals, provide us with the services needed to maintain and achieve good health—their work is clearly morally well-founded.

University Press, 1996); and Philippa Foot, *Natural Goodness* (New York: Oxford University Press, 2001). Another pertinent work is Douglas B. Rasmussen and Douglas J. Den Uyl, *Norms of Liberty* (University Park, PA: Pennsylvania State University Press, 2005), which provides a novel and path-breaking account of the relationship between ethics and politics.

5. Moral Virtue and Free Choice

If morality isn't some kind of myth, as some hold, but a genuine, *bona fide* aspect of human life, then choice is clearly very much a part of it.¹¹ To claim that someone is ethical or moral implies that whatever standard of right conduct is being deployed, the agent freely chooses the right course (whatever the precise process that renders this possible). This choice is not merely a selection that one may have been forced to make, but a free decision, something one didn't have to make, wasn't compelled to make (although the choice may have amounted to an early commitment to act in certain ways, a character trait even). Without this freedom, an act is not morally significant (although it could still be more or less desirable, even valuable).

All efforts to reconcile determinism and morality are futile—ought does indeed imply can.¹² F. A. Hayek makes well the point concerning the relationship between values and liberty with this observation:

That freedom is the matrix required for the growth of moral values—indeed not merely one value among many but the source of all values—is almost self-evident. It is only where the individual has choice, and its inherent responsibility, that he has occasion to affirm existing values, to contribute to their further growth, and to earn moral merit.¹³

6. The Role of Property Rights

A basic precondition of economic liberty, or freedom of choice regarding conduct that bears on one's pursuit of prosperity, is the right to

¹¹ Contemporary neuroscience is struggling with this issue, as evidenced in Michael S. Gazzaniga, *The Ethical Brain* (New York: Dana Press, 2005); and Michael S. Gazzaniga, *Human: The Science Behind What Makes Us Unique* (New York: Ecco, 2008). A valuable collection of essays bearing on the issue is Benjamin Libet, et al., eds., *The Volitional Brain: Towards a Neuroscience of Free Will* (Thorverton, UK: Imprint Academic, 1999). So far the best estimate is that although much of brain behavior is deterministic, there is a power in the human frontal, cerebral cortex that enables human beings, as it were, to veto certain brain processes and thus exhibit what Libet and Gazzaniga call "free won't." See also, Henrik Walter, *Neurophilosophy of Free Will: From Libertarian Illusions to a Concept of Natural Autonomy* (Cambridge, MA: MIT Press, 2001).

¹² For a fuller treatment of the issues involved here, see Tibor R. Machan, *Initiative—Human Agency and Society* (Stanford, CA: Hoover Institution Press, 2000).

¹³ F. A. Hayek, "The Moral Element in Free Enterprise," in Mark W. Hendrickson, ed., *The Morality of Capitalism* (Irvington-on-Hudson, NY: The Foundation for Economic Education, 1992), p. 66.

private property. This right is the principle that everyone is free to act so as to seek, obtain, and hold valued items, the sort of items that constitute economic value. Unless this right is respected and protected, a society fails to recognize that its inhabitants ought to be prudent, to attempt to succeed in significant measure at flourishing in their economic lives. With but a few exceptions everyone needs to aspire to such success—or needs, at least, to benefit from the success of intimates (family, friends, supporters).

In other words, the acknowledgment of the right to private property is a prerequisite of economic freedom—of commerce, business, trade, investment, savings, and development. Private property rights secure for one a sphere of personal authority or sovereignty wherein one is free to act on one's own judgment and others are admitted only with one's permission. Indeed, the complex system of property law is the means of securing for citizens their sphere of personal responsibility, not just in economic but in most areas of conduct. (Just consider how the right to freedom of action in journalism, research, and even religious worship presupposes that one enjoys an area of choice others may only enter with one's permission.)

7. Capitalism and Individualism

The system of political economy wherein the right to private property is part and parcel of the rule of law is *laissez-faire* capitalism. This makes it possible for inhabitants to interact on the basis of mutually agreed-to terms of trade, be such trade economically successful or not. It also pays attention to something that has been neglected in much of human political history, namely, the importance of the individual human being. For individuals are the ones who make moral choices, including in the market place when they practice the virtue of prudence. The market, in turn, is most attentive to individual choices, more so than any other economic system.

An element of morality that is especially cared for in a free market economic system is that without freedom, there is no such thing as morality. I have already alluded to this fact, but it needs to be stressed in giving an account of the morality of capitalism. Market choices can only be subject to moral assessment if they are freely made. If market agents are regulated or regimented by the government, the moral significance of their actions disappears. So a crucial principle of market behavior or conduct is the systematic absence of prior restraint. Just as in connection with the freedom that is protected by the First Amendment of the U.S. Constitution, in terms of which no one may be acted against by the government unless there is a probable cause of criminal conduct, which is to say, conduct that violates someone's rights, so when it comes to commerce or business no burden may be imposed on any agent unless probable cause carefully has been established. And this undermines the case for government regulations, all of which amount to prior restraint.

8. How to Judge Political Systems

A free-market capitalist system is just in large part because it bans prior restraint. This is why business ethics is so important in capitalism, since it is the main instrument for critical attention to how commerce and business are conducted. Unless someone's rights are violated, the law may not intrude on free trade. But morality is very much available for deployment, for being used to criticize commercial and business conduct.

Just as in various other areas of society there is often a rush to judgment which must be resisted—which is to say, due process of law may not be abrogated—so when it comes to addressing malpractice in commerce and business, the only available means are voluntary ones. Various voluntary organizations, such as the Better Business Bureau and watchdog agents at the Fourth Estate (media), are the proper means for criticizing business misconduct, unless it involves the violation of rights (theft, fraud, embezzlement, misrepresentation, and so forth).

9. Government Regulation versus Government Nudging

No sooner does one line of defense of government interference in the economy fall into disrepute, than another is invented by people who insist that they and others with special virtues and qualities have the moral and should have the legal authority to meddle with other people's lives. Socialism and fascism have pretty much been discredited, so outright top-down management of people's lives, whether economic or spiritual, is now out of fashion. Except for some dyed-in-the-wool enthusiast for running people's lives by means of coercive force, most meddlers are now urging the deployment of less Draconian measures by which to carry out their interventions. (Such folks like to point to China's communist rulers who are far from Stalinist thugs.)

Richard H. Thaler, Professor of Behavioral Science and Economics at the University of Chicago, and Cass R. Sunstein, Professor of Law at Harvard University, are academic champions of meddling. They know that this is not a goal that too many people find attractive as public policy. (Of course, there are innumerable measures of intervention in play in this and most other societies, but the intellectual support for them is not coming off as very credible these days.) So instead of promoting even the less harsh versions of the command system (e.g., market socialism), these authors are pushing so-called libertarian paternalism or nudging.¹⁴ The idea is pretty elementary: Don't try to make people act better by threats of—or actual—

¹⁴ See Richard H. Thaler and Cass R. Sunstein, *Nudge: Improving Decisions about Wealth, Health, and Happiness* (New Haven, CT: Yale University Press, 2008).

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physical force; nudge them by subtle mandatory adjustments in their environment. An example they use to illustrate this method involves placing an image of a fly in an airport urinal, which tends to incline men to aim at it and thus prevents spillage by 80%.¹⁵ How clever and gentle. So why not have governments follow this approach as they try to make men and women behave better?

One simple answer is that it is insidious to have governments manipulate the citizenry with various tricks. Airport urinal designers operate without a captive clientele. One need not go there but could have gone at a gas station or back home before getting on the road. And, in any case, the urinals belong to the airport, so they have the authority to design them in any (harmless) way they want to.

But more importantly, there is that famous saying from Aristotle, that one swallow does not a springtime make.¹⁶ Just because there is one example of useful manipulation of people—and we use such nudging techniques all the time in our personal lives, of course, in our voluntary associations with people—it doesn't follow that they are all clever and wise. Moreover, we use them within a domain wherein we have the authority to set the rules.

Thaler and Sunstein do not fully appreciate the work of Public Choice theorists who have taught some very useful lessons about entrusting government bureaucrats with the task of guiding the rest of us in how we should live our lives. While now and then these bureaucrats—led by legislatures and consultants—may hit upon a fruitful, sensible measure that we all ought to adopt in our lives, there is absolutely no reason to think that they will do this routinely. Public Choice theorists note, very helpfully, that people in power have their own agendas and while now and then they may act as *bona fide* public servants—though not even then as necessarily skillful ones—in time most of them become simple promoters of their own goals. And they will always be subject to the very same foibles that the rest of us are subject to and which Thaler and Sunstein believe justifies their intruding upon us in typical nanny-like fashion. In short, who will nudge those doing the nudging to nudge the right way?

This faith that there are among us some few folks who just know so much better how we ought to live—how we ought to care for our wealth, health, and happiness—is a grave threat to us all. Thaler and Sunstein complain that we need the nudging because “there are limits on the number of

¹⁵ *Ibid.*, p. 4.

¹⁶ Aristotle, *Nicomachean Ethics*, trans. Terence Irwin, 2nd ed. (Indianapolis, IN: Hackett Publishing Company, Inc.), I.7.1098a19-21.

items to which we can pay attention at one time.”¹⁷ Yet that very same thing is true about all of those who would do the nudging, so their propensity to mess things up is just as great as ours. Moreover, because they are powerful, able to impose their will on others, the probability of their going astray is greater than that of us doing so—in the spirit of Lord Acton’s famous 1887 saying in a letter to Bishop Mandell Creighton, “Power tends to corrupt, absolute power corrupts absolutely.”¹⁸

Nudging has its uses, but not as public policy. It is far better reserved for how private parties might encourage those they employ and supervise to act properly.

10. The Stakeholder Challenge

In the current discussions of business ethics the most serious challenge to the position advanced here is the stakeholder, otherwise known as the corporate social responsibility (CSR) theory. The idea is that corporations must be managed so as to benefit those who may be affected by what the managers decide, independently of whether shareholders are well served by those decisions. It denies that the ownership of shares confers authority on the owners as far as giving managers directives about what are the goals of management. It denies the right of free association to shareholders by asserting that managers may impose on them associations they do not support (with various stakeholders).

In short, the stakeholder theory undermines the foundations of a free-market, capitalist system of business by supporting the violation of the property and related rights of shareholders. Ultimately, the stakeholder theory favors the kind of wealth redistribution to which those with the right to the wealth have given no consent. Arguably, the stakeholder theory is a form of market socialism, with but a bit of market and a good deal of socialism at its center.¹⁹

11. Comparative Assessment

When political systems are evaluated it is best not to hold out for utopian visions. The free-market system does not do this. It is, rather, an

¹⁷ Richard H. Thaler and Cass R. Sunstein, “Easy Does It: How to Make Lazy People Do the Right Thing,” *The New Republic*, April 9, 2008, accessed online at: http://www.nudges.org/tnr_article.cfm.

¹⁸ Quotation accessed online at: <http://www.quotationspage.com/quote/27321.html>.

¹⁹ See for a more detailed discussion of this topic, Tibor R. Machan, “Stakeholder vs. Shareholder Theory of the Ethics of Corporate Management,” *International Journal of Economics and Business Research* 1, no. 1 (2009), pp. 12-20.

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answer to how societies ought to be organized based on the best available approach. As with other matters, in this very general case the perfect is the enemy of the good.

Compared to other systems of political economy, free-market capitalism is superior because it does justice to human nature and rests the institution of commerce and the profession of business on the moral virtue of prudence.²⁰ Nevertheless, it is useful to mention here that there are quite different schools of metaethics and ethics that often serve as the foundation for business or other professional ethics or indeed for disputing whether such professions are ethical at all.²¹ Two of the most prominent are intuitionism as a metaethical view,²² and altruism as substantive ethical positions.²³ Utilitarianism also serves as the substantive ethics from which business ethics is to be derived, although altruism and utilitarianism have very similar implications for all professional ethics.

Without pretending to deal with the matter in sufficient detail, I would just like to suggest that intuitionism is seriously flawed because in different ages and under different economic circumstances people hold very different intuitions as to what is morally right and wrong. For example, not very long ago people held the intuition that public flogging of young children was morally acceptable, even required. Today our intuition is that such flogging is barbaric.

The flaw in altruism is perhaps best suggested by a quip from W. H. Auden: “We are here on earth to do good for others. What the others are here for, I don’t know.”²⁴ Let’s remember that altruism is an ethical *system* which

²⁰ For an elaboration of business ethics in the spirit of this essay, see James E. Chesher and Tibor R. Machan, *A Primer on Business Ethics* (Lanham, MD: Rowman & Littlefield, 2003).

²¹ Consider military or medical ethics; pacifism would consider the former an oxymoron, while some versions of Christian Science would consider the latter the same.

²² Robert Audi, *Business Ethics and Ethical Business* (New York: Oxford University Press, 2009).

²³ Nearly all of the currently prominent stakeholder or corporate social responsibility (CSR) business ethics positions exhibit an altruistic stance whereby the basic responsibility of all moral agents is to benefit other people first and foremost. For an entire library of such works, see the Ashgate Series, *Corporate Social Responsibility*, edited by David Crowther.

²⁴ Quotation found in *The Week*, November 16, 2002, p. 19.

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involves, as W. G. Maclagan observes, “*assuming* a duty to relieve the distress and promote the happiness of our fellows. . . . Altruism is to . . . maintain quite simply that a man may and should discount altogether his own pleasure or happiness as such when he is deciding what course of action to pursue.”²⁵ It is not the same as the moral virtue of generosity or compassion or kindness or caring for others *as elements of a virtuous life*.²⁶ To embrace the idea that an ethical life is primarily self-enhancing is not to reject the benevolent virtues by any means.²⁷

²⁵ W. G. Maclagan, “Self and Others: A Defense of Altruism,” *Philosophical Quarterly* 4 (1954), pp. 109-10.

²⁶ For more on this, see Tibor R. Machan, *Generosity: Virtue in Civil Society* (Washington, DC: Cato Institute, 1998).

²⁷ See a development of this neo-Aristotelian moral idea in Tibor R. Machan, *Classical Individualism: The Supreme Importance of Each Human Being* (London, UK: Routledge, 1998).

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Hume and Smith on the Moral Psychology of Market Relations, Practical Wisdom, and the Liberal Political Order

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1. Introduction

David Hume and Adam Smith had profound insights into some of the key features of politics, morality, and society in the then-emerging modern world. This paper will indicate and elaborate upon some of those insights, with a view to showing their continuing significance for the case for the market and a liberal political order. Many of those insights were of a moral-psychological character. I use the expression “moral psychology” broadly to refer to features of motivation, morally relevant attitudes and responses, the role of sensibility, self-regard and regard for others, and the like. Moral-psychological matters are crucial to understanding human activity in general—people’s judgments, decisions, and actions, and also such things as the structure, content, and justification of moral claims and moral theorizing. Indeed, I would argue that ultimately a plausible political theory depends upon a plausible moral psychology. Unless conceptions of and ideals of institutional arrangements are based upon a realistic moral psychology, they will be inadequately underwritten, and potentially very mischievous, as well.

2. Hume on Civil Society

My claim is not that a case for the market or for a liberal political order can be read off of facts about human nature; it is not that simple. Neither did Hume or Smith believe that it was that simple. Nor am I arguing that *only* through a market economy in a liberal order can people lead excellent and fulfilling lives. Nevertheless, the case for the market and the liberal polity is not merely ideological; it is not just an expression of arbitrary preference or just an expression of what seems desirable in a certain socio-cultural context. Realities of history, conceptual relations, as well as multiple sources of empirical evidence help make the case.

I shall use the term “liberal” in a wide but not uselessly vague way. Among the most important features of a liberal political order are that (1) it accommodates a measure of value pluralism, even if it should happen that, as a matter of contingent fact, there is a high degree of value consensus; (2) it

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accords extensive rights and liberties to individuals, leaving much of their life-plans, decisions, and actions to their discretion; (3) it protects private property as one of the more basic rights; and (4) it is a polity to which the rule of law—and one in which law reflects principles and values widely endorsed by citizens—is essential. A liberal polity—while it depends upon a widely shared scaffolding of basic values—does not comprehensively enforce morality.¹ It accommodates diverse conceptions of what is worthwhile (not just of what is pleasing) and it depends, in part, on the disposition of citizens to *value* that accommodation and to value the interaction or reconciliation of divergent interests without the exercise of coercive state power. In a liberal polity a great many of the activities in which people engage take place in contexts and arrangements independent of the state. Those contexts and arrangements constitute what is sometimes called “civil society.”

Without pursuing the matter here, I note that there are several different approaches to making the case for a liberal polity. Even when there is agreement on the merits of a liberal polity, there are complex arguments over what actually constitutes its justification. Among the more influential approaches are the Kantian, Lockean, and Aristotelian. There are several others, even including certain strands of Hobbes’s thought. While each justification of a liberal polity has merit, that is not to say that we can just combine them and thereby have an overwhelming case for a liberal polity. The present discussion does not extend to arguing for a particular justification for a liberal political order, but it will indicate some important considerations in favor of it and the market. Also, I will comment on the importance of the market to civil society and the importance of civil society to a liberal polity.

Wide scope for individual liberties without extensive enforcement of morality is supported by a shared commitment to civil society as the context that permits and, to some extent, arbitrates divergent interests and the friction they often bring with them. Increased reliance on formal political institutions, and reliance upon addressing friction legalistically, is almost certain to contract liberty and to enlarge the role of the state. An inclination to use state power—such as legislative power and the courts—as a first resort will accustom people to regarding the state as an apparatus, an instrument, to be

¹ Many defenses of liberalism include arguments for austere legal moralism; that is, for a minimal extent to which morality is enforced by law. Here I do not enter into the argument over the question of whether austere legal moralism is essential to liberalism, or the question of just how to interpret the relevant notion of austerity. In any case, it does seem plausible that a liberal polity will need a high level of commitment to certain moral principles as a framework for sustaining a liberal order. So, even on a quite austere conception of the extent to which morality is to be enforced, moral commitment to the value of liberalism is still required. The aspects of a liberal polity indicated in the discussion are intended as parts of a characterization, not a definition.

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employed to achieve their purposes, and that can encourage a culture of competitive entitlement and ideological politics. The more policy and the more saturating is administrative law, the less scope there is for free activity in civil society. I will argue that one reason civil society is very important is that it creates conditions through which people are encouraged to recognize and appreciate each other as *agents*. This is an issue in regard to which Smith has especially important insights.

Nonetheless, valuing civil society and the willingness to live more, rather than less, of life without official policy to direct it, is a disposition that needs to be learned, acquired through habit and experience. It is not the natural or default position of human beings. It is easy to be implausibly optimistic about the extent to which a liberal political order habituates people for self-determination and for resolving the issues and the conflicts that occur. The experience of the nations of the former Soviet Union and the East Bloc provides evidence that just removing statist and illiberal regimes does not lead to the flourishing of liberal democracy and a market economy, as if people were naturally disposed in that way and the removal of impediments was all that was needed to achieve them. Those are *achievements*, and a great deal of work is required in order to attain them. The dispositions that make this possible have to be cultivated, encouraged, and exercised. As Frank Knight remarks, "The human being does not achieve individuality or freedom, or the idea of freedom, except through a culture made and continued by the various groups in which he lives."²

At the same time, we should not think that because this set of dispositions is a second nature, it is *merely* a second nature, just one set of possible dispositions among a large number, and without very strong normative grounds for it. Given the distinctive, constitutive capacities of human nature, there are good reasons to encourage a second nature to which self-determination is central. Self-determination is a crucial condition for engaging in activities in ways the agent can find desirable and worthwhile in a distinctively rich manner on account of the exercise of his or her own capacities. This is a reason independent of considerations of efficiency in favor of extensive liberty, private property, and the market. And self-determination does not imply social atomism, egoism, or a narrow, strongly self-interested prudence. It primarily concerns capacities for deliberation, evaluative judgment, and articulating the reasons for one's commitments and choices. It has no essential connection with acquisitive individualism.

It is also not part of the present view that, in a liberal polity, agents will be *fully* rational calculators (whatever that means) of their interests, and

² Frank Knight, "Human Nature and World Democracy," in Frank Knight, *Freedom and Reform* (Indianapolis, IN: Liberty Fund, 1982), p. 373.

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that they will participate in social decisions and collective choices in a *purely* rational manner (whatever that means). Again, Knight comments aptly, “In fact, emotion and tradition and force have always been the main factors controlling opinion.”³ The passions and attachment to tradition often have a crucial role in shaping the exercise of self-determination. The issue is not, “What is it for an agent to be perfectly rational?” but rather, “Are there certain forms of political and economic arrangement that are especially conducive to human beings’ living well in the most fundamental senses, given historical realities and the conditions of the actual contemporary world?” The answer is, “Yes,” and the answer includes a significant role for civil society, the liberal polity, and the market.

When more, rather than fewer, aspects of people’s lives are shaped by voluntary undertakings, choice, and discretionary pursuits, people learn the habits of political life (in the broadest sense of politics) that dispose them to want to keep their liberty and to be suspicious of centralized power. And the market is especially important to civil society. Edward Shils writes:

The pluralism of institutions and institutional spheres requires the market economy quite apart from its necessity as the only way of working of a system of private ownership of the instruments of production and from its greater productivity than other modes of organizing economic life. The market is also an important precondition of a civil society because its own autonomy guarantees the autonomy of other institutions as well as business firms.⁴

He also states, “The hallmark of a civil society is the autonomy of private associations and institutions, as well as that of private business firms.”⁵ Furthermore, he notes, “The pluralism of civil society is two-fold. Its pluralism comprises the partially autonomous spheres of economy, religion, culture, intellectual activity, political activity, etc., *vis-à-vis* each other The pluralism of civil society also comprises within each sphere a multiplicity of many partially autonomous corporations and institutions.”⁶ He mentions business firms, churches and sects, universities, independent newspapers,

³ *Ibid.*, p. 379.

⁴ Edward Shils, *The Virtue of Civility*, ed. Steven Grosby (Indianapolis, IN: Liberty Fund, 1997), p. 331.

⁵ *Ibid.*, p. 330.

⁶ *Ibid.*

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periodicals, broadcasting corporations, political parties, and philanthropic and civic associations.⁷

That fabric of voluntary organizations, associations, and undertakings cannot be woven into just any setting of economic arrangements. It depends, to a large extent, upon the market. It is a social phenomenon in a complex and multi-dimensional way. The suggestion that we could have all of those other types of voluntariness and independence without the market is implausible. People would have neither the opportunities nor the access to and control of means needed to engage in those activities and shape and reshape those contexts, nor could they enter and exit them on a voluntary basis. Neither would they develop many of the capacities and dispositions that need to be exercised in a complex setting of discretionary activity and voluntary association. Perhaps in a society that is both very homogeneous and very traditional civil society could flourish without the market, because civil society would not contend with the challenges and frictions of diversity and ongoing change. But it is difficult to see how a diverse civil society could be cultivated absent the market. It is an enabling condition and a constitutive condition for the sorts of plasticity of social organization and interaction that vibrant civil society requires in most social contexts. The variety and efficacy of the various institutions and organizations mentioned by Shils could not be sustained in a command economy or one with significant state monopolies or a strongly protected system of guilds.

Hume has an optimistic view of industry and commerce and their overall social impact. He writes:

The spirit of the age affects all the arts; and the minds of men, being once roused from their lethargy, and put into a fermentation, turn themselves on all sides, and carry improvements into every art and science. Profound ignorance is totally banished, and men enjoy the privileges of rational creatures, to think as well as to act, to cultivate the pleasures of the mind as well as those of the body.⁸

He writes of the ways in which advances in the arts make men more sociable:

They flock into cities; love to receive and communicate knowledge; to show their wit or their breeding; their taste in conversation or living, in clothes or furniture. Curiosity allures the wise; vanity the

⁷ Ibid.

⁸ David Hume, "Of Refinement in the Arts," in David Hume, *Essays Moral, Political, and Literary*, ed. Eugene F. Miller (Indianapolis, IN: Liberty Fund, 1987 [1777]), p. 271.

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foolish; and pleasure both. Particular clubs and societies are every where formed. . . . So that, beside the improvements which they receive from knowledge and the liberal arts, it is impossible but they must feel an encrease of humanity, from the very habit of conversing together, and contributing to each other's pleasure and entertainment. Thus industry, knowledge, and humanity, are linked together by an indissoluble chain, and are found, from experience as well as reason, to be peculiar to the more polished, and what are commonly denominated, the more luxurious ages.⁹

Hume is on to something important, even if he overstates it. Civil society and the market can support and energize the imagination in particularly robust ways. These include a broad range of things such as envisioning possibilities and fashioning ideals and resolutions of problems, conceptualizing one's self in changed circumstances, changed largely through one's own decisions and efforts, and so forth. Various forms of involvement in civil society may be strongly traditional, highly ritualized, or otherwise very conservative. But civil society is also a sphere in which there is space to pursue aspiration and possibility. The ways in which they are pursued *makes* us the kinds of agents we are and do not just *reflect* what kinds of agents we are.

Among the general principles of politics that Hume suggests is the notion “[*t*]hat it is impossible for the arts and sciences to arise, at first, among any people unless that people enjoy the blessing of a free government.”¹⁰ People under arbitrary or despotic government “are slaves” and cannot “aspire to any refinement of taste or reason.”¹¹ The point about the demoralization of aspiration is quite important. It is a moral-psychological consideration with manifold significance because of how aspiration shapes civil society, economic activity, and the overall exercise of self-determination. The arts and sciences of a free people differ dramatically from the arts and sciences of people living in an illiberal regime. Moreover, Hume argues “[*t*]hat nothing is more favourable to the rise of politeness and learning, than a number of neighboring and independent states, connected together by commerce and policy.”¹² A free government gives rise to law—to government by principles acknowledged and endorsed as being in the interest of the

⁹ Ibid.

¹⁰ David Hume, “The Rise of Arts and Sciences,” in Hume, *Essays Moral, Political, and Literary*, p. 115 (italics in original).

¹¹ Ibid., p. 117.

¹² Ibid., p. 119 (italics in original).

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governed and as minimizing arbitrariness and tyranny—and the ties of commerce and policy give rise to emulation and competition, while also inhibiting tendencies toward arbitrary political power.

It is part of Hume's sociology of politics that, "Laws, order, police, discipline; these can never be carried to any degree of perfection, before human reason has refined itself by exercise, and by an application to the more vulgar arts, at least, of commerce and manufacture."¹³ Hume's explanation of this includes the claim that where commerce and industry are encouraged, more and more people have property and develop a concern to safeguard property; "They covet equal laws, which may secure their property, and preserve them from monarchical, as well as aristocratical tyranny."¹⁴ And he claims, "If we consider the matter in a proper light, we shall find, that a progress in the arts is rather favourable to liberty, and has a natural tendency to preserve it, if not produce a free government."¹⁵ Commerce, industry, and property sustain and enlarge "that middling rank of men, who are the best and firmest basis of public liberty."¹⁶

The market does not simply reward initiative and widen consumer choice. It also accelerates and multiplies kinds of interaction and thereby motivates innovation and problem solving and energizes imagination. A market-supported civil society multiplies the contexts in which we can recognize each other as agents. To be sure, it can also shape a social world in which there is envy, anxious competition, and formal and informal contests for political influence. But that is hardly unique to the market. It would be an error to focus too exclusively on either the positive or the negative. But because of the market's relation to the character of civil society in general, it can encourage habits of initiative in many different contexts, not just in commerce and industry. There are more sources of motivation to develop new ideas and organize new institutions.

3. Smith on Civil Society

Adam Smith argues that through the sorts of interactions made possible by commerce, industry, and the various activities constitutive of a market economy and the civil society it supports, we are enabled more fully to acknowledge and appreciate others as participants in a common moral world. In so seeing them, we are better able genuinely to include them within the

¹³ David Hume, "Of Refinement in the Arts," p. 273.

¹⁴ *Ibid.*, p. 277.

¹⁵ *Ibid.*, p. 278.

¹⁶ *Ibid.*, p. 277.

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scope of moral imagination. There are more ways in which to see the relevance of considerations of desert, accountability, and responsibility as people are increasingly acknowledged as agents.

While *The Wealth of Nations* largely concerns certain fundamental dispositions of human behavior and their overall results in economic terms, and *The Theory of Moral Sentiments* largely concerns the basis and character of moral judgment, there is an important connection between them through considerations of moral psychology. Smith has a profound grasp of the importance of understanding the modern human world as an order shaped by contingency—a world that is not to be understood directly in terms of providential governance or a fixed normative order.¹⁷ This has enormous significance for morality and economics alike.

The Wealth of Nations is in part an explication of what sorts of differences are made at the social level by the ways that individuals behave without intending that those specific differences should be brought about. *The Theory of Moral Sentiments* explicates how morality could have a naturalistic basis—how moral objectivity can be explicated in terms of sentiments and the imagination. That is a quite remarkable project. Whether or not one finds Smith's moral theory compelling, it is notable that he has an explanatory conception of the human world and basic forms of human relations that take contingency seriously and dispense with metaphysical requirements to underwrite the intelligibility of the social and moral order. He sees that human beings, through a complex interaction of individual actions with highly local intentions, achieve a complex socio-economic world that has certain regular features but is not itself the product of design. And he gives an account of how morality—how normative requirements—could nonetheless fully apply and genuinely be effective in that un-designed order, fraught with contingency. Smith recognizes how appreciating others as self-determining agents depends upon the kinds of activities that the market allows, enables, and encourages. And that, in turn, is crucial to strengthening moral imagination, to seeing others as participants with us in a common moral world.

¹⁷ I will not pursue in any detail the issue of the nature of Smith's theistic commitments. It seems clear to me (from *The Theory of Moral Sentiments*) that he has theistic commitments and that he takes them quite seriously, appealing to them as having genuine explanatory and moral significance. However, it does not seem to me that he appeals directly to specific theological claims in order to explicate moral judgment or moral motivation. Rather, he takes the notion of providential order seriously, but does not assign a role to revelation or specific theological doctrines in his account of what is morally right or in the account of why one should do what is morally required.

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If there is extensive scope for self-determination, there are more ways in which we can regard and interact with people in their status as agents. We see their self-determination being exercised in judgment, decision, choice, and action, and we find that the exercise of self-determination shapes the world. Even if simply having a human nature is a *ground* for regarding someone as an agent, exercises of self-determination supply *occasions* to do so. The market and the textured civil society supported by it create and sustain conditions for individuals more fully to *become* agents and to interact with others *as* agents. That is a crucial respect in which—as Smith, I think, sees—the market actually can educate moral imagination.

Smith writes, “Our sensibility to the feelings of others, so far from being inconsistent with the manhood of self-command, is the very principle upon which that manhood is founded.”¹⁸ And he elaborates:

The man of the most perfect virtue, the man whom we naturally love and revere the most, is he who joins, to the most perfect command of his own original and selfish feelings, the most exquisite sensibility both to the original and sympathetic feelings of others. The man who, to all the soft, the amiable, and the gentle virtues, joins the great, the awful, and the respectable, must surely be the natural and proper object of our highest love and admiration.¹⁹

He also says that the “sacred regard” to the life and the property of others is “the foundation of justice and humanity.”²⁰ Life in a liberal polity with the market provides extensive experience of the sort that is a basis for agents to acquire the virtues of self-command and sympathy (in the more, rather than less, morally complex sense of sympathy). There is nothing automatic about this. Nor am I arguing that those virtues can only be acquired in that sort of social world. But Smith is right to see that that kind of social world is particularly apt to require the acquisition of prudential self-command, and it is also a world in which the multiple and diverse interactions people have with each other can especially be conducive to that complex kind of sympathy.

Smith writes:

The desire of becoming the proper objects of this respect, of deserving and obtaining this credit and rank among our equals, is,

¹⁸ Adam Smith, *The Theory of Moral Sentiments*, ed. by D. D. Raphael and A. L. MacFie (Indianapolis, IN: Liberty Fund, 1984), III.3.34, p. 152.

¹⁹ *Ibid.*

²⁰ *Ibid.*, p. 153.

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perhaps, the strongest of all our desires, and our anxiety to obtain the advantages of fortune is accordingly much more excited and irritated by this desire, than by that of supplying all the necessities and conveniencies of the body, which are always very easily supplied.²¹

Our concern to obtain the respect of our fellow men is very powerful. It is a crucial element in attaining merited self-respect, and there is considerable gratification in being held in high regard by others. “Our rank and credit among our equals, too, depend very much upon, what, perhaps, a virtuous man would wish them to depend entirely, our character and conduct, or upon the confidence, esteem, and good-will, which these naturally excite in the people we live with.”²² Actions and interactions are the basis of our standing with others and are thereby a basis of our self-regard. Prudence and self-command have a key role in this. And prudence and self-command are both valued and encouraged in a complex, dynamic civil society and the market that underlies it. Civil society and participation in the market are intensive schools of practical rationality.

In fact, participation in civil society and the market can be crucial to developing a sense of moral responsibility to others and to regarding others as rational agents with interests and concerns much like one’s own. They are contexts in which voluntary collaboration and cooperation may be valued highly, and in which agents often have shared responsibility. It is difficult to see how the virtue of prudence can be acquired *unless* one’s activities make demands and offer challenges to practical reasoning, imagination, attention, resolve, and other capacities and skills. It is not as though a sound sense of what is worth doing, good judgment, and a capacity for deliberative excellence can be learned or imparted on their own, without actually engaging the complexities and contingencies of actual, concrete circumstances where matters of genuine importance are at issue. Self-command and prudence—the combination of which is the core of general practical wisdom—are learned in practice. Civil society and the market can multiply opportunities for emulation and examples of excellence attained by effort and initiative.

Moral education, in the sense of the most general cultivation of practical rationality, is most fully available in an open and diverse civil society, with wide scope for voluntariness. In it we are best able to learn prudence and attain the regard of others on the basis of morally estimable acts and qualities. This fact about the market is part of a strong case for it on the basis of moral-psychological considerations. The market does not ensure that

²¹ Ibid., VI. 1.3, p. 213.

²² Ibid.

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virtue is rewarded with prosperity and ill-desert with unhappiness. In fact, it is an important element of moral education that people should come to see that nothing in the natural and social world ensures that. But learning to participate in the market involves learning responsibility, initiative, and energetic self-determination. It can do this at the same time that it is understood that our lives are fraught with contingency, unintended consequences, and the vagaries of fortune, and that no natural or social mechanism or process guarantees desert in all outcomes.

To be sure, it is obvious that people's tastes may be vulgar, that they may choose to let their abilities lay idle, that they may seek enjoyments and distractions that are tedious or corrupting, and so forth—and the market can encourage this. If we are to believe advertising, it seems that it is *always* true that there has *never* been a better moment to buy a car, that there are a vast variety of opportunities to indulge yourself by eating things that are no good for you, and that now you can do all of that from the comfort of your sofa, surrounded by video games and bookless shelves. Here, too, Knight makes an important point. He observes that “one of the most fundamental weaknesses of the market system is the use of persuasive influence by sellers upon buyers and a general excessive tendency to produce wants for goods rather than goods for the satisfaction of wants.”²³

It must be admitted that the market can corrupt not only popular taste but also politics. Knight goes on to say, “Influencing men's judgment, however, is almost the essence of democratic political process, and is definitely more sinister where the advocate appeals to men in the mass, and they decide in the mass, rather than individually.”²⁴ He adds, “But under liberalism, political truth is decided by mass judgment selecting among opinions or personalities advocated under conditions of free competition.”²⁵ And, “It is surely unnecessary to explain here that what this process selects is not truth, but effective technique in persuading the crowd.”²⁶ In addition, there are often powerful tendencies on the part of political and economic groups to try to determine political and economic outcomes on the basis of factional interests and even outright corrupt practices.

There surely is truth to those observations. However, it is easy to highlight the market as the cause of moral corruption and misery in ways that

²³ Frank Knight, “Social Science and the Political Trend,” in Knight, *Freedom and Reform*, p. 39.

²⁴ *Ibid.*

²⁵ *Ibid.*

²⁶ *Ibid.*, p. 42.

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are distorting. The political, the social, the economic, and the moral are braided together in ways that can only be separated analytically, and we should have sober expectations about how much can be accomplished by focusing on one rather than another dimension of our lives. No economic arrangement will solve all of our social problems. No public policy will robustly increase virtue. No exercise of moral wisdom and courage will make the world enduringly wonderful, both just and prosperous. But the market is especially promising and resilient in respect of making possible all variety of corrections, adjustment in tendencies, and potential for attaining desirable outcomes without the exercise of coercive force. Also, we should not overlook the fact that in a market economy—because of the way it supports civil society—we are also much more likely to have a large number and variety of private institutions of higher learning, a culture of invention and entrepreneurship, and all sorts of associations and organizations for the pursuit of shared interests and the promotion of shared aims and concerns.

There are ways in which the market can corrupt the political culture, but this is not because it necessarily or inevitably does so. A political culture depends upon many factors, including what sort of education people receive, what kinds of dispositions of public service and concern for the public good are encouraged, and who is willing to serve in political office and why, among other factors. As argued above, citizens of a liberal polity with a market economy can acquire a strong interest in the rule of law and integrity in politics because of how such things protect liberty and serve people's interests in common. There are always excesses of political pandering, demagoguery, and other political vices, because of what human beings are, not mainly because of what the market is. And in a liberal polity with a market economy corruption and malfeasance stand out because they are *not* in accord with what is appropriately expected.

It is easy to be overly impressed by examples and images of acquisitive and greedy competition, corporate unconcern with worker safety, deceptive claims in advertising, and the like, while taking for granted the enormous benefits of the market for individuals and for society in a multitude of respects. Historical evidence and the insights of sophisticated theorists and critics such as Knight warn us in no uncertain terms about the ease with which we can unduly be optimistic in our assessment of the market and its tendencies. I am not simply arguing that the freer the market, the better the life for all those affected by it. Yet history also supplies considerable evidence that in the absence of the market, and where economic activity is strongly controlled by the state, there are powerfully inhibiting and repressive influences on individuals and civil society in general. Substantial restrictions of the market constrain the metabolism of civil society and hinder imagination, creativity, interaction, and initiative of many kinds.

4. The Scope of Market Values

Another objection to the market, and one that comes from a variety of critics is that “market relations tend to expand into areas of human life which had previously been outside the scope of the market.”²⁷ “‘Market relations’ here refers not only to the physical activities of exchange, but also to the legal institutions, and even ways of thinking which are characteristic of the market.”²⁸ The market, critics argue, has a tendency to enlarge the extent to which people see relations and activities in terms of the market, and this has very undesirable consequences. Peter Singer, for example, argues that “if we allow market relations to dominate most or all spheres of human activity, we may no longer be motivationally capable of certain forms of altruism.”²⁹ Allen Buchanan goes on to note that while there is considerable debate over “the scope and validity of the generalization that the market drives out altruism, there is a great deal of plausibility to the more guarded claim that human life would be greatly impoverished if all interpersonal relationships were market relationships.”³⁰

This issue should be distinguished from the issue of whether we can give an economic analysis of all forms of human behavior, even including sex between a husband and wife. Buchanan refers to work by Richard McKenzie and Gordon Tullock, in which they “hypothesized that the frequency of sexual intercourse for a couple can be viewed as the outcome of nonmonetary exchanges in which each partner,” as McKenzie and Tullock put it, strives to “consume sex up to the point that the marginal benefits equal the marginal costs. . . . If the price of sex rises relative to other goods, the consumer will rationally choose to consume more of other goods and less sex.”³¹ Ice cream is mentioned as a substitute for sex. Granted, this does take some of the romance out of intimacy. But in the first place, McKenzie and Tullock do not offer the hypothesis as a prescriptive claim. Second, while it may be that an economic analysis of any human behavior is possible, it does not follow that it

²⁷ Allen Buchanan, *Ethics, Efficiency, and the Market* (Totowa, NJ: Rowman & Littlefield Publishers, Inc., 1988), p. 101.

²⁸ *Ibid.*

²⁹ Quoted in *ibid.*, p. 102.

³⁰ *Ibid.*, pp. 102-3. Buchanan is referring here to Peter Singer’s “Altruism and Commerce: A Defense of Titmuss Against Arrow,” *Philosophy & Public Affairs* 2, no. 3 (1972), pp. 312-17.

³¹ *Ibid.*, p. 103. The quotation in Buchanan is from Richard B. McKenzie and Gordon Tullock, *The New World of Economics*, 5th ed. (New York: McGraw-Hill, 1994), pp. 48-49.

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gives a *correct explanatory account* of that behavior. We can—at the risk of significant distortion—re-describe fundamental values as preferences and speak only of preference-satisfying behavior, leaving out considerations concerning the intrinsic worth of things. Yet, the possibility of re-description does not imply that exclusively economic considerations fully account for behavior. This is an issue that is relevant to a great many contexts, that is, that description within the categories and idiom of a particular theory or approach does not in its own right indicate that that theory or idiom is properly exhaustive of the features of the phenomena being studied. For example, we could give purely behavioral descriptions of human action, but that would not show that there is nothing more to human action than the motion of bodies. That is why it is important to distinguish between a true explanatory account and the possibility of description in the vocabulary of a specific theory

However, while that distinction should be respected, we should note that encouraging people to explain phenomena in certain terms can lead to them acting in certain ways as their conceptualization of things become more fully assimilated to that perspective. That is why it is ethically important to guard against the market's setting the terms in which we understand all aspects of life. If we interpret and explain things too narrowly, we may begin to judge, decide, and be motivated too narrowly, losing or just never acquiring a richer normative idiom for thought and choice. Civil society can enormously be helpful in that regard, teaching people values that restrain them from seeing everything (or even just too many things) in exclusively economic terms.

Market-oriented thinking can sprawl into more and more departments of life, taking them over, so to speak, and that can lend plausibility to Singer's claim about the possibility of the market's disabling people for altruism. But first, there is no necessary relation between the extent of the market and the contraction of altruism. People could strongly be committed to the market as an economic arrangement without that arrangement becoming the sole or primary determinant of how they see others and themselves, and how they evaluate action, persons, and things. In addition, whether people are altruistic or not almost certainly depends upon a great many factors having to do with the nature of civil society, the society's traditions, and institutions and arrangements in addition to its economic organization. We should note, as well, that the moral-psychological phenomena to which Smith draws attention give us reason to think that the market in a liberal polity can powerfully *support* altruism. This occurs through the ways in which the regard for others as participants in a common moral world is supported by interacting with them as self-determining agents. That can be a powerful and important basis for respecting others and having a measure of concern for their well-being. The market is not bound to affect participants in just one way, encouraging them to see others through the narrow perspective of economically instrumental terms.

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We are able analytically to separate out economic considerations from moral considerations for various theoretical purposes. But the profit-orientation of a firm, for instance, does not imply that the managers or shareholders will not have philanthropic dispositions or that the profit-orientation leaves no scope for altruistic motives. People can be aggressively profit-seeking *and* very generous and genuinely philanthropic. People can be very competitive and also morally serious, alert, and responsive, and so forth. What we learn from studying Hume and Smith is that perhaps the key point is that participation in a market economy in a liberal polity can encourage regard and respect for other persons, trust and the willingness to cooperate, and an interest in civic virtue.

There are ways in which human corruption and immorality can find ways to flourish in the market, and in any human institutional arrangement whatsoever. It is doubtful that the market is outstandingly apt to fuel corruption or to supply a supportive environment for it. There are reasons to think that the market, civil society, and the rule of law in a liberal polity can contribute to moral education and to the cultivation of mature practical rationality in significant respects. Hume and Smith are owed gratitude for providing conceptual resources for understanding the ways in which the market and the liberal polity have normative bases in facts of moral psychology, and the ways in which the market and the liberal polity can well-serve some of our best interests, even to the extent of helping us learn what they are.³²

³² I am grateful to the Earhart Foundation for its generous support of my work through a Fellowship Research Grant for spring and summer 2008. I wrote this article during that period while a Visiting Scholar at the Oxford Centre for Hebrew and Jewish Studies. The grant was primarily to support my work on *Law, Reason, and Morality in Medieval Jewish Thought*, but this article and other projects of mine also benefited greatly from the research time in Oxford. In addition, I would like to thank Colgate University's Research Council for its support during that same period.

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Ethics without Profits

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“O that a man might know the end of this day’s business ere it come!”
—William Shakespeare, *Julius Caesar*, Act V, scene 1

1. Introduction

In this article I want to explore some of the essential characteristics for an ethics of non-profit or not-for-profit (NFP) organizations.¹ The impetus behind this project is to see whether there are any salient differences between business ethics and the ethics of an NFP. Both organizations need to have their revenues meet or exceed their costs and both offer value to the recipients of their products or services. In what way, if any, would ethics differ in an NFP organization as compared to a for-profit organization? More precisely, what is the fundamental guiding ethical principle of an NFP that essentially informs all normative reflections about such organizations, and does that principle differ from what is central to ethics in a business?

We could begin to examine our question by looking at NFPs as they exist today, but this seems to be a point of departure that presupposes too many questionable social/political assumptions. The main questionable assumption is that it is legitimate and appropriate for the state to give special tax considerations to organizations that provide certain benefits the state deems worthy, as opposed to other benefits provided by other organizations which do not receive such favorable treatment. That the state should be an instrument of redistribution, meliorism, selective favoritism, and the like is, from the point of view of political philosophy, hardly an uncontroversial beginning point. But even assuming that such actions by the state are legitimate and appropriate, many questions about which benefits deserve this special treatment would also be entailed.² Moreover, we take the question seriously as to whether there should be any taxes at all. Should the case for

¹ “Not for profit” is probably the more accurate expression. “Non-profit” could apply to businesses that are simply not doing well.

² In the U.S. it is likely that the principle of separation of church and state produced the first instances of favorable tax treatment by the state with respect to voluntary organizations.

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taxation fail, it would seem that the whole “not-for-profit” idea could not even get off the ground. It is certainly the case that NFPs, as they are currently functioning, could not be understood without presuming the legitimacy of taxation.

In this article, therefore, we shall begin by discussing the basic question of whether NFPs would and should exist if we do not depend upon the tax incentive assumption of current NFPs. I shall claim that there is, nevertheless, a place for them. We begin by considering the issue of the existence and nature of NFPs and then follow by exploring the nature of ethical thinking in an NFP. In the final section I shall discuss how the preceding reflections might say something of value about business ethics, or the “for-profit” world. The literature on our subject is sparse, given the sorts of parameters that I have just defined and will define below. Still, it is hoped that what is said will not be completely beside the point when it comes to the actual functioning of NFPs. If nothing else, I will have sought to raise here some of the central questions to consider when discussing the essential characteristics of ethics in NFPs.

2. The Nature of NFPs

The question of whether there would be NFPs is largely a function of one’s basic political philosophy. If, for example, one believes it is the role of the state both to tax and to tax for purposes of producing certain social benefits the state deems especially important, then there may be reasons for using tax policy to favor some organizations or programs over others. In such a world, it seems reasonable to suppose that the prime governing principle in thinking about an ethics for organizations favored by the state would have to be tied very closely to the purposes the government defines for favoring those organizations in the first place. But even if one has this political philosophy, it nevertheless might be more interesting to imagine whether there would be NFPs in a world where no special tax breaks were given to any organization, or there were no taxes at all. Would this largely “laissez-faire” world drive out all NFPs and reduce everything to the profit motive? Are there thus not analytical benefits to imagining such a world in order to see how dependent NFPs really are upon government, or, if one’s political philosophy tilts toward social engineering, how much of that engineering also defines the principles upon which ethical obligations will be built? If nothing else, by imagining a taxless or even a flat tax system, we can at least discover the “natural” condition of NFPs without having the distorting elements of the debate about which sorts of activities should be favored over others. Though this flat tax or taxless world is one more reflective of my political philosophy than its alternative, exploring our question under the assumption of such a world does not of itself imply that there may not be additional reasons for using tax policy

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to pursue certain “public” ends. That question is a question of political philosophy and beyond the scope of this article.

All organizations must take in more revenues than they spend in order to survive in the long run. Moreover, all organizations require managers, workers, customers or clients, accounting procedures, boards of directors, and the like in order to function properly and well. In these respects for-profits and NFPs are very much alike, and because of that similarity there is a strong tendency to see ethics similarly in both cases. There would, for example, be ethical issues to consider in every one of these operational dimensions just mentioned. But what then would separate the business organization from any others? Our question is actually twofold: would NFPs come into existence in such a world, and if so, how would they differ from for-profit organizations?

Our categories of analysis are, however, somewhat more complicated than originally supposed. The term “not-for-profit” fails to distinguish between charities, on the one hand, and NFPs which are not charities, on the other. So one question is whether there would be NFPs that are not charities in our world of no or flat taxes? The answer to this question seems to be “yes,” since such organizations apparently exist today irrespective of tax incentives. I, for example, belong to a cottage owners association which involves paying dues for projects of common interest among the cottage owners. We are organized into a formal organization with officers, bylaws, and projects. We try to keep a small surplus for unexpected expenses, but mainly we seek to spend pretty much what we take in and not anything further. We certainly are not trying to make money—indeed, we have these cottages in part to get away from all that. But some issues that affect all of us need to be dealt with (e.g., road maintenance, since these are private roads), and we need some regular procedures and funds for doing so. We obviously have, however, no charitable ends in this arrangement.³ We are, in other words, an NFP without being a charity.

Without much difficulty we can easily imagine such arrangements for various clubs, hobbies, or other associations where the object is to accomplish some task of common interest the costs and benefits of which accrue only to the members of the group. Members of a business organization may have common goods or interests as well, such as distributing common tasks (e.g., answering the phone) or mechanisms for maintaining common spaces, such as a lunch room. These common interests are similar to those one might find in a club, fraternal organization, or hobby group. Those sorts of

³ We have no “welfare” programs per se. We sometimes let a family that may have some difficulty paying dues be late on payments or be helped in other ways. These are acts of neighborliness because such measures are considered temporary and rare. If the family were really struggling financially, selling the second home would be the sensible thing to do.

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common activities as found in a business or an NFP differ in kind from the common interest all have in the success of the business itself and their role in attaining that success. We shall address that issue in a moment. A charity is a different kind of enterprise altogether. Here the “members” join together in order to benefit others outside the group with some service or product those others are unable to provide for themselves. Like the club or homeowners’ organization, enhanced revenues do not contribute to the wealth of the individual members, but (in the case of charities) to those outside the organization who are the object of the benefits being conferred. Enhanced revenues for the non-charitable NFP may benefit the members as new projects get accomplished that the organization could not previously afford. Yet these benefits do not enhance the individual members’ wealth, but are rather common, indirect, non-excludable benefits in which each member may participate.⁴ (A parallel in the business world might be nicer offices as a result of the success of the company.) In simplest (and perhaps somewhat oversimplified) terms, the principals of charities tend to look outward regarding beneficiaries, while clubs, fraternal organizations, homeowners’ associations, and the like, which do not seek to make a profit, tend to look inward. The principals in a business are always looking inward, even if outsiders are solicited and significantly benefited by the business’s activities.

This last point brings us right to the place where we need to be clear about what a business is, at least in terms of its purposes. First, although the distinction between an NFP that is not a charity from one which is a charity is an important one, for our purposes here we shall lump them back together and refer to them both as NFPs. Our main interest is in comparing and contrasting NFPs with businesses, and the distinction between a charity and a non-charitable NFP is not important for that comparison. So what then is a business? No better definition of the purpose of a business has been given than the following one from Elaine Sternberg: “The defining purpose of business is maximizing owner value over the long term by selling goods or services.”⁵

⁴ Alexei Marcoux has pointed me to Henry Hansmann, *The Ownership of Enterprise* (Cambridge, MA: Belknap, 1996), where Hansmann argues that the principals of an NFP cannot function like owners and share in both the control of the organization and a share in any residual income.

⁵ Elaine Sternberg, *Just Business* (Oxford: Oxford University Press, 2000), p. 32. Jonathan Macey makes a similar point, though narrower in scope: “the goal of corporations is to maximize profits for shareholders. That is the purpose for which corporations are formed and the premise upon which equity capital is raised from investors”; Jonathan Macey, *Corporate Governance: Promises Kept, Promises Broken* (Princeton, NJ: Princeton University Press, 2008), p. 100. In a rather different direction, see Alexei Marcoux, “Business Focused Business Ethics,” in J. Smith, ed.,

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It cannot be said that the distinction between a business and an NFP is the selling of goods and services. Many NFPs sell things rather than give them away. Nor can it be said that “owners” do not have their values “maximized” in an NFP. We can easily imagine a person whose greatest satisfactions come from the work she is doing for her NFP. It does, however, seem more appropriate to think of the principals who participate in an NFP as “members” versus those in a business who would likely be “owners.” Perhaps we can state the point at the limit: it is conceivable (indeed, usual) that an NFP would have no owners, but that is not conceivable for a business.

In any case, it is the *conjunction* of maximizing owner value with the selling of goods or services that compels our attention. Another way of putting the point is that in a business, the way the owners maximize their value is by selling goods and services. In an NFP, if goods or services are sold, that in itself is the “maximization” of value for the members. Thus if you buy a Liberty Fund book, that purchase alone is the realization of value for those of us at Liberty Fund (which is a private operating foundation), whereas in a business the purchase is a *means* to the realization of value. Thus we can conclude with Sternberg that:

[B]usiness’ definitive purpose is not to produce goods or services, or to add to value. Producing goods or supplying services and adding value are, of course, indispensable elements of doing business But producing goods and services and adding to value are not exclusive to business, and therefore cannot serve as business’ defining goal.⁶

Fully appreciating the difference in purposes between a business and other sorts of human endeavors is necessary for thinking properly about business ethics and presumably about ethics in other contexts as well. Saying this suggests the possibility that ethics is somewhat context-bound. Though we do not have space to argue the point here, we are opposed to the sort of ethical universalism that holds that moral norms are univocal across contexts and

Normative Theory and Business Ethics (Lanham, MD: Blackwell, 2009), pp. 17-34. Here business is “defined” as “an exchange-transaction-executing practice” (p. 23), which has certain advantages in not being too narrow a description of a business and being a practice rather than entity-oriented. I stick with Sternberg’s definition throughout, partly because my Aristotelian “four-cause” approach calls for a final cause which Sternberg provides, and also because it better highlights some of the points of difference between businesses and NFPs I wish to make below.

⁶ Sternberg, *Just Business*, p. 36.

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thus can be understood independently of context and applied equally to any context.⁷ Consequently, what might be permissible in one context, say business, may not be permissible in another such as an NFP. As we shall see below, context plays a role in thinking about business ethics versus ethics in an NFP. Indeed, Sternberg's exclusive focus on purpose ignores some contextual matters that are important to our discussion here.

In any case, if the purpose of the business is to maximize value for the owners over the long term by selling goods and services, then perhaps we need to have a statement about the central purpose of an NFP. Whether a charity or not, the purpose of an NFP is the promotion of some specified value(s) the members jointly regard as significant through activities which are in themselves an expression of that (those) value(s). There may, of course, be activities necessary for the purpose to be fulfilled, but these are recognized for what they are, namely, as means to the end of fulfilling the purpose of the NFP. Similarly, there may be those connected to an NFP who are motivated in ways identical to someone in a for-profit organization (e.g., to get a paycheck). Still, understanding that person's motivations is completely unhelpful in explaining or understanding the activities of the NFP, though it is not completely irrelevant to understanding what is going on in a business. The key point here is that in an NFP there is no formal attention paid to the distinct values of the principal individuals⁸ involved as there is in a business. Both enterprises need to unite their actors with common purposes, but in the case of the business the common purpose is a means to the end of owner (or worker) value maximization.⁹ In the NFP, the level of member value maximization is essentially irrelevant, provided the specified value(s) is pursued, though it is assumed that if one is participating in the NFP one is largely committed to its value(s). In a business, the particular mix of value maximization in the

⁷ This "we" is literal, involving of my colleague Douglas Rasmussen, who co-authors with me many of our discussions of ethical and political theory. See Douglas Rasmussen and Douglas Den Uyl, *Norms of Liberty: A Perfectionist Basis for a Non-Perfectionist Politics* (University Park, PA: Pennsylvania State University Press, 2005), for some of what is needed to make the argument in the text.

⁸ Principals for an NFP are those individuals for whom the responsibility falls for carrying out the purpose of the NFP as just defined. In some cases the principals and staff may be the same individuals. In other cases, the staff may simply be employed by the principals to help carry out the purpose of the NFP.

⁹ The purpose of the business is owner maximization, but a business's "common" purpose can be the maximized satisfaction of all in the sense that the workers too are presumably selecting their highest valued alternative in staying with their job. Management may seek to achieve that common result by making the opportunity costs of leaving too high.

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activities performed can vary from individual to individual. Thus in the extreme case in a business, one may take no pleasure at all in the particular tasks in which one is engaged, but realize maximum value from monetary rewards that accrue from those activities. Another individual may find significant satisfaction in the activities themselves. In an NFP, by contrast, it is assumed that value “maximization” for any given principal individual is realized or expressed in fulfilling the purpose(s) of the organization.

NFPs are significantly more communal and less individualistic than businesses. For this reason it is sometimes common to regard them as superior ethically. The state, for example, takes an interest in these kinds of activities because it is believed that they tend to reflect and promote the “common good.” In the last section of this article, I shall give some reasons for holding the reverse, namely, that businesses have a superior moral status to NFPs in certain significant respects. Of course, I would equally insist that we are not forced to choose between the two. Both are a valuable and necessary part of our world, and one of the benefits of imagining a world where tax policy is not driving the NFP picture is that it would allow a clearer understanding of just where the NFP ethos would function most effectively. In essence, this claim is part of a larger theory that human flourishing has a number of diverse dimensions—a point that cannot be argued here but which we have discussed elsewhere.¹⁰

So given all of these distinctions, qualifications, and arguments, would NFPs exist in a world not driven by tax policy? Answering “yes” may not be much of an answer, however. Some might hold that such organizations would be significantly less present in a taxless world. Thus, although some NFPs would certainly exist, their role in society would be significantly diminished, and that would somehow be for the bad. However, unless one is simply arguing for the good of communalism itself, the extent of NFPs in society is neither good nor bad in itself, but presumably something we wish to have in just the right amount. Thus fewer NFPs may not *imply* a worse society. Moreover, the lack of special tax incentives may not even imply a dearth of NFPs. It is worth noting in this connection that in a country where “the business of America is business,” there has been no lack of NFPs—something Alexis de Tocqueville remarked upon long ago. Indeed, compared to countries where the state supplies virtually all the “public goods” and the incentives of tax policy are downplayed in favor of direct state provision, it is arguable that those countries marshal larger amounts of public spiritedness. It is conceivable, then, that not only would NFPs exist in a world not driven by tax policy, but that the market-distorting effects of the state may have created the same problems for the good of NFPs as it does for any other good—that

¹⁰ See, for example, Rasmussen and Den Uyl, *Norms of Liberty*, ch. 6.

is, they are supplied in the wrong amounts and to the wrong ends. In any case, it seems reasonable to suppose that NFPs would exist in our free-market world, because they serve certain types of human purposes that are not as well served by for-profit organizational arrangements.

3. NFPs and Wealth Consumption

Since our purpose here is to discuss ethics as it might apply to NFPs, we might do well to begin with a look at ethics as it applies to the more familiar business context. In this respect, Sternberg notes the following:

Business ethics applies ethical reasoning to specifically business situations and activities; it is an attempt to resolve or at least to clarify those moral issues that typically arise in business. Starting from an analysis of the nature and presuppositions of business, business ethics applies general moral principles in an attempt to identify what is right in business.¹¹

Sternberg goes on to reject relativism, noting that because ethics is being applied to a special context this does not mandate that therefore ethical principles are simply relative to those contexts. Indeed, the same basic values that we normally consider when thinking about ethics are to be brought to the business context. These values, such as justice, fidelity, trust, and the like, can inform business practices and are “true” independently of the business context to which they may be applied. I have no quarrel with this approach, but I do want to argue that context can make an important difference in the way ethical principles and virtues are employed and managed and even to the approach one takes in “solving” ethical issues. Though we tend to treat NFPs and businesses similarly in many respects when it comes to ethics—e.g., we talk a lot about what fiduciary responsibilities management may have, or the organization’s obligations to workers or the presence of conflicts of interest—doing so misses an important difference in context between NFPs and businesses. It is that difference I wish to take a moment to explore.

Sternberg’s approach to business ethics is to define the problem almost exclusively in terms of the purpose of a business as determined by its nature. In Aristotelian terms, the ethical principles and obligations are determined in light of the final cause of businesses—what we noted above as being the maximization of value for the owners through the sales of goods and services. Sternberg is careful to point out that businesses must produce goods

¹¹ Sternberg, *Just Business*, p. 76. Sternberg is cited extensively here because her basic Aristotelian framework is also my own. The defense of frameworks is beyond the scope of this article, but it is perhaps of some value at least to identify it here.

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and services in order for there to be sales and thus for the realization of the final cause or purpose of business itself. We might say, therefore, that we can continue using the Aristotelian causal framework by noting that the formal cause of a business is production, the material cause the materials used in the productive process, and the efficient cause the inputs of labor and planning that transform the materials into products for sale. Discarding all of the Aristotelian baggage, we might say simply that businesses are productive enterprises. Their purpose may be to maximize value for the owners, but their effect is productive—that is, they create wealth.

Now my main point here is a simple one: *NFPs are fundamentally consumptive of wealth*. That is, their formal cause is to consume previously created value or resources. Although the efficient causes (and sometimes even the material) between the two types of organizations may be similar—and this is where a lot of the ethical attention (sometimes rightly) goes—the difference in formal cause is quite profound. To look at it at the individual level first, the difference between a productive and a consumptive activity would be the difference between one's activities at work, on the one hand, and the vacation one takes with the earnings one derived from that work, on the other. Of course, moral norms such as not lying, cheating, or harming, apply to both situations, so we tend to overlook the fact that the contexts are so different. Nevertheless, NFPs are critically dependent on production and quite distinct from it. Because they consume rather than produce wealth, a society filled with nothing but NFPs would be like an individual spending down his capital. With wealth no longer being produced, an individual—or society—would eventually become bankrupt if all activities were consumptive. And analogously, when individuals become wealthier their consumptive possibilities increase, so too might we expect NFP activities to increase as a society becomes wealthier. In both cases the opportunity to enjoy wealth is predicated upon that wealth first being produced.¹²

¹² When delivered at the April 2009 meeting of the Association of Private Enterprise Education (APEE) in Guatemala City, this portion of the article drew the most discussion. I especially thank both Dan Green and Jonathan Wight for helpful comments on this matter at that time. Basically, the issue was whether I was falling into the same mistake as Adam Smith falls into in trying to separate productive from non-productive activities (“labour”); see Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, vol. 1, ed. R. H. Campbell and A. S. Skinner (Indianapolis, IN: Liberty Fund, 1976), II.3, pp. 330–49. The former (productive) adds value to a good or activity; the latter does not, according to Smith. First of all, in making my distinction between productive and consumptive I am not necessarily speaking about the activity or enterprise considered in itself alone, but rather the purpose for which it was undertaken. Thus a school, considered in itself, might be either a for-profit or an NFP enterprise. An external observer might be unable to tell the difference without any knowledge of the purposes of the principal actors involved in these enterprises. “Productive” and “consumptive” thus are here connected to the

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If the foregoing is correct, the opportunities for NFP activities are a function of the level of production. If individuals simply consume what they produce, the opportunities for the existence of NFP-type organizations will be limited by that level of production, and since (as we shall note again below) NFPs do not exist to serve the particular needs of their individual members, those members will consume other goods before they consume the good provided by the NFP. Because NFPs exist to serve real human needs, we would expect them to exist at least to some extent at virtually any level of production above subsistence. But NFP goods are generally likely to stand behind other consumption goods in societies without much wealth. For growth to occur there must be some sort of surplus where more is produced than is currently consumed. Since businesses seek to maximize value for the owners, they tend to create wealth because owners generally want to create more and more value for themselves and often must do so to remain competitive with other owners over the long term. There is, therefore, always a tendency in businesses toward the pursuit and usually the creation of a surplus of value.

From club dues to providing aid for the poor, NFPs are heavily dependent upon there being enough *additional* wealth for people to consume in ways that accord with those purposes represented by their NFPs. Certain consumptive projects can, of course, be commanded by the state, but without a surplus, this is either a command to use up existing capital or a command to finance the operations by printing money. Either way, the long-term prospects for wealth creation are diminished. Private NFPs and government programs have in common their need to “exploit” wealth in order to function.

subjective judgments of the agents as they view the use of their own resources and opportunity costs. Those subjective judgments, however, make all of the difference in the world when it comes to determining the ethical principles and values that apply to a situation, for those purposes represent the intentions of the agent from which principles of moral responsibility are built. All this may raise the deeper philosophical issue of whether in a world with no final causes (i.e., purposes) there could be anything more than just value and disvalue such that ethical judgments are nothing but comments upon effects rather than choices. In such a world, the distinction between ends and means would disappear such that one could not tell whether an activity was a means to an end or sought for its own sake. This philosophical issue goes beyond this article, but apart from wondering about the meaning of the term “value” in this non-purposive world, one could also wonder about the role and meaning of such ethical concepts as responsibility, merit, praiseworthiness (and blameworthiness), choice, principled behavior, and the like. One might repair to a philosopher such as Spinoza for answers to these questions. For our purposes here, the presence of the purposes of the principal actors are critical to getting ethics going, whatever the overall wealth effects created by their actions of which they may or may not be aware.

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Although wealth is the basis from which NFPs can flourish, it is not our contention that the *motivation* for NFPs is a function of the presence of wealth. Natural human sympathy may, for example, motivate one toward charitable acts whatever one's wealth. But however motivated one may be, the *execution* of those charitable intentions depends on someone financing them out of wealth that either exists or is being created. In this respect, then, NFPs are predicated upon a successful productive environment, which is to say an environment suited to the creation of wealth. An ethics suitable to such an environment must be one that is suitable to the process of creating wealth. Some values, such as those mentioned above with respect to trust and honesty, are suitable to virtually all situations—business or otherwise, because they are basic to the structuring of human relations in any context. But there may be ways of thinking about those moral values that differ from one context to the next. We'll say more about this in moment. For now, the point is that the formal cause of business ethics are norms suitable to production or wealth creation.

The situation seems quite different for NFPs. Here our concern is to consume created wealth for some particular purpose. As noted, the consumption is not personal even if it is the case that our personal values may match those pursued by an NFP. I may hand money to a beggar on the street, but that is very different from my founding or joining an organization which uses resources to help the destitute. We can speak of an ethics of personal consumption, and Adam Smith does say some things about this sort of issue in *The Theory of Moral Sentiments*.¹³ The main question with respect to personal consumption is the correct balance of production and consumption in one's spending and saving habits. This is not the issue with NFPs, which, because they create value through the consumption of resources, have no issue of balance between production and consumption. Theoretically, the only limits to an NFP's spending are the resources at its disposal and the satiation possibilities of the values it pursues. If my "relief-for-the-hungry" NFP had unlimited resources, it could spend without hesitation until all hungry people disappeared. As Smith notes in contrast, however, were I personally to indulge my sympathy for the hungry in a way that excluded every other consideration, I would not be managing my personal consumption well. NFPs can effectively pursue their values without limit, if we ignore the question of the resources at their disposal; and they can do so without much concern for any other values that may otherwise compel our attention. This sort of unlimited single-mindedness is not only what often gives NFPs the incessant

¹³ A number of things along these lines are said in Part VI of Adam Smith, *The Theory of Moral Sentiments*, ed. D. D. Raphael and A. L. MacFie (Indianapolis, IN: Liberty Fund, 1976), in connection with his discussions of prudence and benevolence.

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character about the values they advocate, but also gives the illusion that they are repositories of unlimited goodness, since the admitted goodness of the value(s) they pursue is completely unqualified by any other value.

An NFP would consequently require an ethics of consumption, but one that is suited to the singular pursuit of specified values without consideration of the relative merits of those specified values against other values. Clearly, however, the “big picture” requires that values be weighed against other values, and in saying this we are raising an important question of political philosophy that can only be noted here but not discussed. That question is whether the weighing of those values will be done by individuals on a voluntary basis or by a collective entity such as the state. That is to say, are resources to be considered as completely socialized, so that our question is one of having the state decide the relative degree to which resources are devoted to supply widgets or to feeding the hungry, or do individuals make those choices for themselves and on their own assessments of which productive and consumptive activities to emphasize and to what degree? The tax-based approach we have adopted in the “real” world is something of a mixture of these two alternatives.¹⁴ Various NFPs make their appeals for the importance of their causes, and if they make the threshold of gaining favored tax status, we then decide on an individual basis of whom we wish to support.

If what we have said above is largely correct, the ethics of an NFP will not be one that should tolerate a great deal of flexibility about which ends are pursued. The integrity of the pursuit of the ends for which the NFP was established seems to be the central ethical principle of any NFP. That is quite different from businesses which often move their product lines into areas which bear little relationship to their founding products as a way of pursuing further profits.¹⁵ The integrity of a business is kept intact if the owner’s values are maximized. The integrity of an NFP is only kept intact if the value for which it was created is itself kept intact and not altered according to the values of the members entrusted to carry out its mission. We have, for example, witnessed numerous foundations pursuing ends directly contradictory to their original missions, because these ends were more in keeping with the interests of those put in charge of directing the NFP. NFP principal members, however important their stations in the organization, are not owners, and thus have a responsibility *not* to indulge their interests, but to carry out the “interests” of the organization itself. These members exist for the

¹⁴ This is less true in Europe where “public” goods are also publicly funded and private NFPs less abundant than in the U.S.

¹⁵ Alexei Marcoux has pointed out to me that F. W. Woolworth is a good example here. What began as a “five and dime” is now known to us as “Footlocker Inc.”

sake of the value(s) they have been charged to pursue, whereas in a business the values pursued are for the sake of the owners.

An ethics of consumption in the case of NFPs is thus fundamentally about mission. When we look therefore to the applicability of moral principles to the NFP context, our fundamental question is what sorts of activities and operating structures secure the values of the organization. In a business context the fundamental question is what sort of organization secures the values of the owners. In both cases, we can talk meaningfully about fiduciary responsibilities, conflicts of interest, treatment of employees, and other such topics usually associated with business ethics. But the difference of purpose between an NFP and a business may give all such considerations a different twist. Instead of looking, for example, for employees motivated by increasing their own income I may be, as an NFP manager, looking for employees dedicated to the cause being advanced by the NFP, and I may use such considerations when deciding questions of morale, equity, incentives, and employee advancement. The ethics of responsible consuming may overlap with the ethics of responsible producing, but we must be open to the possibility of divergences as well.

4. Some General Lessons for Business Ethics

I want to conclude this discussion with a few brief comments about how what I have said about NFPs might affect how we think of business ethics generally, as well as NFP ethics. My point is fairly simple: the sort of ethics appropriate to businesses should be essentially contract-based; the sort of ethics appropriate to NFPs should be essentially rule-based. What I am driving at here is that for a business the relationships and procedures needed for attaining its end are essentially open-ended. There is no predefined pattern to use to determine the organizational arrangements of a business. What works to maximize owner value is the standard, not the “appropriate” pattern or values. The differences between Google and UPS in terms of corporate ethos and managerial style are striking. Though patterns may emerge in the market, there are no “right” ways of associating or organizing, save what results from mutual interest (within a context of rights-respecting conduct and the employment of general human virtues, of course). And given that notion, whatever organization exists is always subject to change based on the changing of interests and circumstances of those who are a party to the organization itself—as well as in response to the market. As long as the basic purpose of a business is being pursued, parties can arrange themselves on whatever basis and whatever terms are mutually agreeable and seem to further the end of owner value maximization. Moreover, as a productive wealth-creating enterprise, a high degree of flexibility in adapting to market conditions is needed in order successfully to create value. It would seem, therefore, that the contract is the mode of formal association most suited to

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these ends. Contracts can be highly individualized and flexible, and they are often subject to renegotiation. Moreover, they are grounded solidly in individual interest. Businesses are most effective in carrying out their tasks when all of the parties are united by their separate commitments to their own interests.

The highly individualized, flexible ethical framework most suited to a business seems in significant respects contrary to an ethical framework suitable for an NFP. In the case of the NFP, there is a predefined, specified purpose that must constantly be referred to when considering the appropriateness of certain tasks, employments, or external relations. Alignment with mission rather than alignment of interest is the guiding principle here. An NFP devoted to saving whales, for instance, could not invest in a whaling company, however profitable such an investment would be. The mission guides the actions, and here it would seem that a rule- or duty-based ethic would be most appropriate. Rules get promulgated generally and tend to discourage individual variations. That approach, in essence, is suited to a mission-oriented structure which not only is not interested in individual variations, but also positively wants the conformity of individuals to its mission. There is no renegotiating of one's commitment to the ends of the NFP. One is either committed or not. There is no flexibility about the ends being pursued, either. An NFP stands for something and that usually implies a number of things it either stands against or which are by nature irrelevant to the ends it ought to be pursuing.

Of course, we are speaking here in archetypical ways. In the real world, businesses like to talk about their missions, and NFPs use contractual relations in many facets of their organization and activities. It is conceivable that each type could, over time, change into the other for various reasons. But the archetypical character of these reflections are not, and should not be, falsifying in nature. The specifics may sometimes obscure, but do not thereby obliterate, the essential differences between the two types of organizations. Should an NFP lose sight of its mission as its central focus in its activities, it would begin to lose its moral legitimacy. Should a business lose sight of its ends as defined above, however beneficial its activities may be, it would cease to be a business and need to be measured in other terms. In business ethics, some dimensions of corporate social responsibility and stakeholder theory have precisely this effect of drawing us away from the central purpose of business and thus from a business ethics proper. In the case of NFPs, amorphous missions and unclarified ends effectively turn managers and boards into owners with perhaps more discretion concerning the use of resources than that enjoyed by the typical business owner. The point is that productivity in a business is encouraged by rewarding individual initiative, maintaining organizational responsiveness and flexibility, and by keeping the ends pursued open-ended in nature. The appropriate use of resources in an

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NFP, by contrast, comes largely from conformity, single-mindedness, and well-defined missions.¹⁶

Due to a number of the characteristics stated above, NFPs have often been given a superior moral status to organizations which, in the end, are devoted to the advancement of the individual's own interests (namely, businesses). Businesses are allegedly "atomized" and "selfish." NFPs are organized for a good beyond the individual. In part, however, this is to compare apples and oranges. As we've said, NFPs are consumptive endeavors and businesses productive ones. Which one of those is morally superior to the other is unclear. Perhaps the ends of NFPs are superior to other sorts of consumptive activities, but in the framework of an individualistic ethics, as we have discussed elsewhere,¹⁷ even this would need to be argued in certain sorts

¹⁶ Jonathan Wight has objected to my argument here by pointing me, through an article by Timur Kuran ("Why the Middle East Is Economically Underdeveloped: Historical Mechanisms of Institutional Stagnation," *Journal of Economic Perspectives* 18, no. 3 [Summer 2004], pp. 71-90), to the problem of the *waqf* in the Islamic world. *Waqfs* are trusts originally set up to avoid government expropriation of wealth, but which later were used to finance various forms of activities and enterprises. They are characterized by strict adherence to their mission and its rules. As Kuran notes: "neither the founder nor any mutawalli would be authorized to alter its [the *waqf*'s] mission or form of management. They had to follow the stipulations in the *waqf* deed to the letter" (p. 80), and "the requirement to follow the founder's wishes to the letter limited opportunities to channel resources into broad political causes" (p. 83). The rigidity of the *waqf* led to the failure to form something like the corporate structure used in the West to organize and finance enterprises, and thus to the stagnation of Islamic economies. Hence my call for mission-centeredness through adherence to rules is a call for lack of flexibility which could, in turn, have dire social consequences as institutions fail to adapt over time. In response to the implied objection to my argument, it is important to notice that *waqfs* are essentially government institutions. It is not that the government enforces rules—that would be appropriate under any system—but rather that it does not allow competing forms of organization to exist, that it forbids mechanisms for changing the rules (indeed, considers their original form divinely sanctioned), and that it understands the mission of the *waqf* in terms of rules rather than the rules in terms of a mission. In our taxless or flat-tax world, *waqfs* as described here would either not be possible or extremely unlikely. If the general point is that we can imagine the founder of an NFP demanding, in *waqf*-like fashion, strict adherence to rules and little flexibility, then I suppose the argument here would require fidelity to those rules. However, why a founder would wish to so tie the hands of her NFP is unclear, but in any case, other less restrictive organizations focused more on the aims of the organization than rules would certainly exist. In addition, if the rules simply became intolerable or completely antiquated and there were no provisions for change, the fund could always spend itself out of existence as a number of present day foundations have done for fear of losing sight of donor intent.

¹⁷ Again, the "we" here is literal. See note 7 above.

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of ways. Unity of purpose, fellow feeling, and communal endeavors are all valuable human endeavors, and if they are to be found more readily in NFPs, then NFPs should certainly be highly valued in any society. But our foregoing discussion has also indicated the extent to which an ethics appropriate to businesses may have its own claims to the superiority of that form of cooperative endeavor. If nothing else, the prior fundamentality of wealth-creation to the works of NFPs should give productive enterprises a certain amount of moral respect. But if one, in Aristotelian fashion, takes individual flourishing to be the final cause of all ethical principles, then organizations which respect individuality and individual choice, and give structural centrality to individuality in their operations, have rather strong claims to moral legitimacy, if not to superiority. A business ethics which undermines this dimension of the moral order by treating businesses as if their proximity to moral worthiness was determined by the degree to which they acted like NFPs with “public good” missions is thus effectively misguided.¹⁸ We should instead be looking at ethics in terms of its appropriateness to the type of enterprise to which it is applied and celebrating the fact that the moral landscape is diverse enough to recognize a variety of legitimate forms of human endeavor. One of the benefits of considering the moral character of NFPs is that such an investigation may highlight the moral excellences that ought to be accorded to businesses.

The moral superiority question is not an irrelevant one to our issue here, though it begins to point us back to larger questions of political philosophy rather than institutional ethics. It is not uncommon to see NFPs referred to as purveyors of *public* good while businesses are said to be devoted to *private* good. It is a short step from this conception to thereby giving NFPs superior moral status. We have seen some reasons above for thinking such inferences are too quick if not downright mistaken. But the belief that NFPs are purveyors of the common good coupled to a tone of moral superiority is strongly embedded in the mythology of NFPs. An organization called “The Independent Sector,” for example, convened a “Panel on the Nonprofit Sector” in an effort to recommend ethical conduct procedures for all NFPs. It noted in its preamble to that project that

[n]onprofit organizations in the United States—educational, charitable, civic, and religious institutions of every size and

¹⁸ Jonathan Macey notes a similar phenomenon with respect to the importing of criteria suitable to public institutions into a corporate environment. See Macey, *Corporate Governance*, p. 100.

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mission—represent the most widespread organized expression of Americans' dedication to the common good.¹⁹

In addition, acceptance by NFPs of the recommendations made by The Independent Sector “would provide a common yardstick by which members of the public can evaluate how to direct their support.”²⁰ Although The Independent Sector's Panel is careful not to lose sight completely of the role of contributors to the various NFPs, the language of the common good and the presumption that NFPs are a kind of public trust pervade its recommendations and obscure the morally salient origins of NFPs that we have begun to identify. Furthermore, although lip service is paid to “the wide, necessary diversity of organizations, missions, and forms of activity that make up the nonprofit community,” the Panel's recommended principles are meant to apply equally to “every charitable organization.”²¹ *Prima facie*, there may indeed be moral principles that apply across the board, but these are the sorts of principles that need no special elaboration from any panel of experts. Instead, recommendations such as those made by the Panel point us to the very issue of political philosophy with which we need to close.

On the account given here, NFPs in our taxless or flat tax world would be essentially *private* organizations, funded by private individuals for their own private—though jointly held—ends. They are neither public entities, nor instruments of public entities, such as the government or state. Of course, our tax-incentivized world muddies up all of this, but it is important not to allow that muddiness in until we understand what is at stake. What is at stake turns out to be the same issue that is at the heart of any discussion of human relationships, namely, whether we should be advocating a social/political order expressed through the voluntary non-coercive associations of individuals, or whether we wish an order that considers resources to be common and which manages those resources toward ends deemed worthy by those in positions of “public trust” who wield sufficient power to secure unwavering compliance toward those ends. Obviously, which order is preferable and defensible is the “big issue” that cannot be answered here. But in a response to The Independent Sector's Panel, the Philanthropy Roundtable's worry that “some of the more problematic Independent Sector principles will not remain voluntary but will be codified into law or

¹⁹ Panel on the Nonprofit Sector, “Preamble” of “Principles for Good Governance and Ethical Practice: A Guide for Charities and Foundations,” October 2007, available online at: <http://www.nonprofitpanel.org>.

²⁰ *Ibid.*, p. 3.

²¹ *Ibid.*, p. 5.

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regulation, if it is perceived that there is a wide consensus in favor of them within the charitable community,”²² does begin to address that very issue.

A political philosophy such as the one I would adopt,²³ which advances the principles of individual liberty through voluntary association, must be wary of all endeavors to turn NFPs into public-purpose organizations, with common modes of operation and common rules defining appropriate behavior.²⁴ We should not move in this direction, because the issue of mission is one defined by those who organized the NFP in the first place and who should therefore be free to decide the rules appropriate to the achievement of their respective ends.²⁵ Interference by the state, either directly or through various “nudges” such as tax incentives or special favors of other kinds, are as distorting of the market for the kinds of goods provided by NFPs as they are of markets in goods provided by businesses. In both cases individual choice is replaced by collective command. Such interferences represent attempted substitutions of a system of voluntary individual choice with a system of coercive, centrally directed choice. In other words, they are arguably substitutions of an order consistent with a sound ethical framework with one that is not. That substitution in turn diminishes the prospects for ethics in both the for-profit and the not-for-profit sectors of the economy.²⁶

²² Philanthropy Roundtable, “We’re Not Signing It: Our Concerns About Independent Sector’s ‘Principles for Good Governance and Ethical Practice’,” December 17, 2007, available online at: <http://www.philanthropyroundtable.org/printarticle.asp/>.

²³ Argued for in Rasmussen and Den Uyl, *Norms of Liberty*.

²⁴ This sort of approach does point us back to the problem of the *waqf* and precisely the ways in which institutions get rigidified by government mandate.

²⁵ The Philanthropy Roundtable unfortunately goes on to criticize The Independent Sector for wanting to impose things like diversity among Board members. Criticisms of this type may be justified, but the central point is that NFPs are not public entities and should not be treated as if they were.

²⁶ I wish to thank Nick Capaldi, Doug Rasmussen, Dan Green, and especially Alexei Marcoux for helpful comments on an original draft of this article. I want to thank Dan Green again and Jonathan Wight for very helpful criticisms and comments on a later draft.

Is a Market for Values a Value in Markets?

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Go into the London Stock Exchange—a more respectable place than many a court—and you will see representatives of all nations gathered there for the service of mankind. There the Jew, the Mohammedan, and the Christian deal with each other as if they were of the same religion, and give the name of the infidel only to those who go bankrupt. There the Presbyterian trusts the Anabaptist, and the Anglican accepts the Quaker's promise. . . . If there were just one religion in England, despotism would threaten; if there were two religions, they would cut each other's throats; but there are thirty religions, and they live together peacefully and happily.

—Voltaire (*Letters on England*, Letter 6)

“I can be bought. If they paid me enough, I'd work for the Klan.”

—Former NBA star and Basketball Hall of Famer Charles Barkley¹

1. Introduction

To exist, a commercial culture needs the institutions championed by classical liberals: free markets, limited government, and the rule of law. To survive and flourish, however, a commercial culture must be populated in significant part by individuals possessing the virtues, habits, and dispositions that complement classically liberal institutions. Call persons possessing these virtues, habits, and dispositions *fit participants in commercial culture*. This essay addresses one of the dispositions fit participants in commercial culture possess. Thus, this essay is not about the *rights* or the *duties* of participants in a commercial culture—what actions they or their fellows are morally free to perform or are duty-bound morally to perform or refrain from performing—but about an aspect of the *character* one must cultivate in order to be a fit participant in and a supporter of commercial culture. Cultivating that character may involve refraining from actions that one has a right to perform, even

¹ David Shields, “Charles Barkley’s Head Fake: He’s Just Pretending to Be Outrageous,” *Slate*, Friday, November 22, 2002, accessed online at: <http://www.slate.com/?id=2074459>.

when one desires to perform them and even when doing so violates no one's rights. This essay is about a form of activity that, as a matter of cultivating the character appropriate to a fit participant in commercial culture, one ought to be disposed to avoid even though one has the right to engage in it and doing so violates no one's rights.

2. The Market for Morality

Business ethicists and corporate social responsibility (CSR) theorists have both heralded and celebrated the emergence of a *market for morality*.² Although not a precisely defined concept, the increasing prominence of so-called socially responsible investing (SRI), corporate mission statements emphasizing social performance, "green" consumerism, firms adopting "fair trade" initiatives, and myriad other commercial undertakings intended to respond to consumers' or others' sense of what is or what promotes the common good are all said to exemplify this market for morality. More interesting than the market for morality's exact contours or the degree to which it has flowered, however, is the evaluative response of business ethicists and CSR theorists to its emergence. For it is almost invariably treated by them as an unalloyed good, evidence of personal and moral growth transcending the impoverished sociability of *homo economicus*, the injection of an overt ethical sensibility into a commercial practice thought wrongly to be marked by amorality.³

There is a significant moral downside to at least one facet of the market for morality. Call it the *market for values*. The market for values is manifested by the practice of conditioning one's willingness to transact with others on those others sharing one's moral, religious, political, or (to use a regrettably vague but commonly invoked term) social values. To enter the market for values is to say that price, product, and commercial integrity (i.e., making good on promises made) are not enough to consummate a mutually beneficial transaction; one's trading partner must also share one's values. Although this practice (usually) violates no one's legal or moral rights, I argue that it cultivates in its practitioners dispositions inconsistent with the character of a fit participant in commercial culture. To the extent that the market for values and its corresponding dispositions become widespread, they threaten to undermine commercial society and the cornerstone of the liberal political and

² See, e.g., Thomas W. Dunfee, "Corporate Governance in a Market With Morality," *Law and Contemporary Problems* 62 (Summer 1999), pp. 129-57; David Vogel, *The Market for Virtue: The Potential and Limits of Corporate Social Responsibility* (Washington, DC: Brookings Institution Press, 2005).

³ See, e.g., Richard T. DeGeorge, *Business Ethics*, 4th ed. (Englewood Cliffs, NJ: Prentice Hall, 1994), pp. 5-7.

social order it supports, namely, liberal toleration. Encouraging the market for values's growth is encouraging the fracture and factionalization of the market. Consequently, participation in the market for values is something fit participants in commercial culture are properly disposed both to resist for themselves (because it is imprudent) and discourage in others (because in the aggregate it is socially divisive).

3. The Market for Values

People have always had to make buying and selling decisions in order to pursue their values. For example, committed environmentalists buy "green" products, moral vegetarians avoid purchasing meat, and abortion opponents avoid seeking (or providing) abortions—the failure to do these things being also the failure to practice the values they profess. However, several recent, high-profile efforts have focused on making the willingness to transact with another contingent on that other sharing one's values. That is, rather than seeking (or avoiding) *products* that express (or undermine) their values, these efforts encourage seeking (or avoiding) *trading partners* who share (or oppose) their values.

For example, in the wake of the 2004 U.S. presidential election, the website BuyBlue.org was launched to encourage "progressive" Americans to buy from firms whose officers and affiliated political action committees support Democratic candidates and to shun firms supporting Republicans.⁴ Historically, similar efforts have been launched to punish commercially specific firms or individuals for supporting political causes odious to the organizers. For example, Coors Brewing Company⁵ and Domino's Pizza⁶ have at different times been boycotted for their support of right wing views and causes, their efforts to resist workforce unionization (in the case of Coors), and so forth. However, unlike traditional boycotts, which are usually aimed at a particular person or firm for a particular grievance or complaint, these newer efforts have been undertaken to punish (or reward) wide swathes of the business community for their failure (or willingness) to support a wide array of favored views, candidates, parties, or causes. Lest this trend be thought the exclusive province of the political left, recall that in protest of the

⁴ See, e.g., the Wikipedia entry "BuyBlue.org," accessed online at: <http://en.wikipedia.org/wiki/BuyBlue.org>.

⁵ See, e.g., "Union at Coors May Be Broken But It Hasn't Halted Its Boycott," *New York Times*, May 28, 1979, p. A7.

⁶ See, e.g., Bill Shapiro and Vince Bielski, "Domino's Pizza," *Mother Jones*, March/April 1994, accessed online at: <http://www.motherjones.com/politics/1994/03/dominos-pizza>.

U.S. Supreme Court's 2005 *Kelo* decision,⁷ BB&T Bank announced that it would not lend to private development projects involving the use of properties secured via eminent domain. In other words, doing business with BB&T demands holding or acting consistently with views about property rights similar to those of its CEO, John Allison. These examples and others⁸ evidence the flowering of the market for values.

In the market for values, *like-mindedness* is a precondition to contracting. From the standpoint of getting the product one seeks at an agreeable price, this like-mindedness is gratuitous and, therefore, in a participant in commercial culture, imprudent. In the aggregate, insistence upon this gratuitous like-mindedness tears at the fabric of commercial society. To see why this is so, we must consider the market as a venue for, and the exchange transaction as an example of, social cooperation.

4. The Market as a Venue for Social Cooperation

The market is a venue for social cooperation. This has been denied by communitarians and other critics of commercial society, who decry the "naked cash nexus" between buyer and seller as a bond too weak to merit the adjective "social." It has been denied by Marxists and others who hold a zero-sum, objective-value view of market exchange, under which the give and take of bargaining and exchange is all and only the attempt to gain at another's cost. In other words, in the zero-sum view of market exchange bargaining and negotiation are not preludes to social cooperation, but acts of duplicitous aggression.

Market exchange is social cooperation in *atomic* form. It is cooperation that can be achieved by the minimum number of people necessary to engage in a cooperative venture (two), over matters as small as the participants care to cooperate, and with the minimum amount of agreement between them necessary to effectuate their cooperation. Where the communitarian despairs at the lack of social solidarity, another observer marvels at the way cooperation is achieved by people of disparate aims, views, and values, millions of times a day, without anyone being compelled to forswear his aims, views, or values. That is, people achieve often complex and far-reaching forms of cooperation with a minimum of like-mindedness between them.

⁷ *Kelo v. City of New London*, 545 U.S. 469 (2005).

⁸ Efforts by homosexual marriage advocates to punish commercially those who contributed to California's successful Proposition 8 referendum to define marriage constitutionally as a relationship between a man and a woman may be another example.

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Like-mindedness is a barrier to social cooperation. Where free people deal with other free people, the more they *have* to agree on in order to cooperate the less likely they are *to* cooperate. Free people who intend to remain free people deal with one another commercially more often than politically because it allows them to cooperate where their values and interests overlap without trampling on one party's values and interests where they don't.

Like-mindedness is similarly the enemy of trade. This may seem counterintuitive, as we characterize contract proverbially (if not wholly accurately) as a "meeting of the minds." However, in the canonical market exchange buyer and seller need only agree on a *product* and a *price*. If one wants to buy what the other is selling (or sell what the other is buying), they negotiate in order to discover whether a bargaining range (i.e., a set of prices at which they can transact in a mutually beneficial way) exists and, if one does, to settle on *one* price within the bargaining range at which they will transact. As with other forms of social cooperation, the more we must agree on in order to transact the less likely we are to transact. Consequently, savvy participants in market exchange don't go looking for like-mindedness where it is unnecessary to achieving their transactional ends. Like the London Stock Exchange traders of whom Voltaire was a keen observer, as buyers they are concerned only to get what they pay for; as sellers they are concerned only to get paid. This is illustrated in remarks from perhaps the unlikeliest source of support for the commercial ethos, British musician, Labour party activist, and committed socialist Billy Bragg. In a recent interview, Bragg says:

People do say to me, 'I love your songs, but I just can't stand your politics.' And I say, 'Well, Republicans are always welcome. Come on over!' I would hate to stand at the door, saying to people, 'Do you agree with these positions? If not, you can't come in.'⁹

5. Bargaining and Negotiation

If savvy participants in market exchange don't go looking for gratuitous like-mindedness, it is perhaps unsurprising that the evolved norms of bargaining and negotiation tend to discourage the pursuit of gratuitous like-mindedness over at least one matter likely to elicit profound disagreement between bargaining parties: distributive justice. Through the practice of reservation price deception (i.e., passively or actively misleading the other party about the least beneficial deal one will accept), the parties to a bargain

⁹ Bullz Eye interview with Billy Bragg, October 20, 2008, accessed online at: http://www.bullz-eye.com/music/interviews/2008/billy_bragg.htm.

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keep one another focused on the question, “How much is enough for me—too much to risk losing by making a counteroffer and perhaps convincing the other party that there is no mutually beneficial exchange to be had?” This question encapsulates the approach to market participation that the early twentieth-century economist and theologian Philip Wicksteed calls *nontuism*.¹⁰ For Wicksteed, the market depends for its efficacy not upon the *selfishness* of its participants (as many have claimed), but instead upon their unconcern, in the context of the bargain they pursue, with the well-being of those with whom they are bargaining.

Many regard nontuism with an unmerited suspicion because they contrast it with altruism or other forms of fellow-feeling. The problem is not that altruism or fellow-feeling cannot be contrasted with nontuism, but that altruism and fellow-feeling are not the only—and not the most worrisome—of tuistic preferences. That one is altruistic entails that one is tuistic, but that one is tuistic does not entail that one is altruistic. Differently put, tuism is consistent with altruism, but it doesn’t entail it. Similarly, nontuism is consistent with the destructive forms of egoism, but it doesn’t entail them.

Commonly, we think of other-regarding attitudes as being laudatory and the lack of other-regarding intentions as malevolent. However, a moment’s reflection reminds us that other-regarding intentions can be vicious (like Hitler’s intentions toward Jews). It reminds us also that a lack of other-regarding intentions to another (say, one’s trading partner) need not mean a lack of other-regarding intentions generally. Indeed, in most commercial contexts, participants in bargaining and negotiation do so on *another’s* account—as *agents* for others. Thus, even as they disregard the interests of those with whom they bargain (and, by extension, those on whose behalf those others bargain) in the matter over which they bargain, they do this in furtherance of another’s interests. In other words, their nontuistic bargaining is not an expression of a general lack of fellow-feeling, but of loyal service to those they are duty-bound as agents to serve.¹¹

Of course, the critic of nontuism can acknowledge that *logically* it doesn’t entail selfishness while still maintaining that bargaining relations are better if the parties are other-regarding, in a way that seeks to promote the other’s interests. However, it is not the *content* of other-regarding preferences that poses a problem for bargaining, but the presence of other-regarding

¹⁰ Philip Wicksteed, *The Common Sense of Political Economy: Including a Study of the Human Basis of Economic Law* (London: Macmillan, 1910).

¹¹ Indeed, Wicksteed uses the example of trustees to make the same basic point; see *ibid.*, p. 175.

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preferences (and the information necessary to act on them) themselves.¹² Whether bargainers are self-seekers or other-regarding altruists, preferences over what or how much the other party gets out of the bargain add a layer of like-mindedness as a further hurdle to the bargain.

To see why, recall that in order to transact, buyers and sellers must overcome two obstacles. First, they must discover whether a bargaining range exists (i.e., the highest price the buyer is willing to pay is equal to or higher than the lowest price the seller is willing to accept). Second, having discovered that a bargaining range exists (if it does), they must settle on *one* price within the range at which to transact. The bargaining range offers a menu of mutually beneficial prices; the larger the bargaining range, the larger the menu of prices. The parties are better off transacting at *any* of those prices than they are failing to transact. However, some of those prices are more advantageous to the buyer, others are more advantageous to the seller, and while both have a reason to transact at *some* price in the bargaining range rather than failing to transact, they have no reason *mutually* to prefer one price to another—for any price in the bargaining range, moving to another price is more advantageous for one of the parties. Moreover, this is true whether “advantageous” here means “gives me more” (selfishness) or “gives you more” (altruism)—for any price in the bargaining range, moving to another price is more advantageous for at least one of the parties.

Our evolved norms of bargaining ameliorate this problem, perhaps counterintuitively, by *limiting* the information of the parties. Rather than declaring their reservation prices at the outset, discovering the full contours of the bargaining range (overcoming the first obstacle), and then having it out over which of the prices they will settle on (trying to overcome the second obstacle), the processes of bargaining-range discovery and the proposal of prospective settlement prices are conducted simultaneously. Each proposal advanced by the bargainers has the potential to reveal to the other party that a bargaining range exists (by being within the range acceptable to that other party) and to reveal part of that range to the other. Through the fog of negotiation, each comes to see part of the bargaining range, but not the same part.

Consider an example: Boris (buyer) wishes to buy a house; Svetlana (seller) is selling her house. Upon inspecting her house and satisfying himself that it meets his requirements, Boris concludes that he is willing to pay up to \$300,000 for it. Boris’s reservation price is \$300,000. At or below that price he counts himself better off buying the house than not buying it. Above that

¹² See, e.g., Kay Mathiesen, “Game Theory in Business Ethics: Bad Ideology or Bad Press?” *Business Ethics Quarterly* 9, no. 1 (1999), pp. 37-45, who argues that prisoners’ dilemmas pose the same problems for altruists as they do for egoists.

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price, he counts himself better off keeping his money and looking elsewhere for a house. Upon satisfying herself that Boris has the means to pay her and seems unlikely to go litigation-happy on her after the closing, Svetlana concludes that she is willing to accept as little as \$280,000 for her house. At or above that price she counts herself better off selling the house than keeping it. Below that price, she counts herself better off keeping her house and looking elsewhere for a buyer. Thus, as Boris and Svetlana begin negotiations, there exists a bargaining range. At any price between \$280,000 and \$300,000, both Boris and Svetlana are better off transacting than not. However, as they enter negotiations, neither of them knows this. Each has only *conditional* knowledge about the bargaining range. Boris knows that, *if* there is a bargaining range, \$300,000 is its ceiling. But Boris doesn't know if there is a bargaining range. For all he knows at the outset, Svetlana's reservation price may be \$350,000. If so, no bargain is possible between them. Svetlana knows that, *if* there is a bargaining range, \$280,000 is its floor. But Svetlana doesn't know if there is a bargaining range. For all she knows at the outset, Boris's reservation price may be \$230,000. If so, no bargain is possible between them.

Boris and Svetlana go about discovering whether a bargaining range exists by proposing prices at which to transact. Because Boris hopes to get a low price, his initial proposal will be low and subsequent proposals (if he makes subsequent proposals) will go up from there. That is, his proposals will approach the bargaining range (if there is a bargaining range) from the end about which he lacks even conditional knowledge. Boris knows the ceiling of a hypothetical bargaining range, but not its floor. Because Svetlana hopes to get a high price, her initial proposal will be high and subsequent proposals (if she makes subsequent proposals) will go down from there. That is, her proposals will approach the bargaining range (if there is a bargaining range) from the end about which she lacks even conditional knowledge. Svetlana knows the floor of a hypothetical bargaining range, but not its ceiling.

Suppose that after each makes a proposal outside the bargaining range and thus not of interest to the other (Boris proposed \$270,000; Svetlana countered, proposing \$320,000), Boris offers \$285,000—a price within the bargaining range. Although Boris does not know that his offer is within the bargaining range (because he knows the possible bargaining range's ceiling, but not its floor), Svetlana now knows that a bargaining range exists. She does not know its full contours, but she knows it extends at least from her reservation price, \$280,000 up to Boris's offer, \$285,000.

It may look like Svetlana has an advantage—she knows that there is a bargaining range and Boris does not. But Svetlana doesn't know that Boris doesn't know—because Svetlana doesn't know that her previous proposal has failed to penetrate the bargaining range. Moreover, Svetlana is now aware that she has something to *lose* by making a counterproposal and running the risk of convincing Boris that there is no bargaining range (even though there is).

Svetlana's next decision is actually a difficult one. Should she lock-up the producer surplus she will enjoy by accepting Boris's offer of \$285,000, or should she press on with a counterproposal that may yield more producer surplus, but that may also be above Boris's reservation price and may convince him that further negotiations are a waste of time?

Suppose Svetlana resolves to seek a still more attractive price and proposes \$295,000, which turns out to be in the bargaining range. Now, the same analysis applies—but to Boris. He discovers, for the first time, that there is a bargaining range and it extends at least—and perhaps at most—from his reservation price, \$300,000, down to Svetlana's proposal, \$295,000. Like Svetlana before, Boris has to weigh the benefits of pressing on for a more attractive price against the risk that further proposals may scare off Svetlana and leave each with no gain.

Beneath this pedantic retelling of the negotiation process lies a point: Under reservation price deception, mutually practiced, Boris and Svetlana each come to see only *part* of the bargaining range—and not the *same* part. Uncertain about how far the bargaining range extends beyond the part each sees, but certain about the benefits accruing to him or her by accepting an offered price within that range (and, consequently, certain about the benefits forgone should negotiations break down), Boris and Svetlana are forced, finally, to answer the question: How much transactional surplus (consumer in the case of Boris, producer in the case of Svetlana) is enough for me? Although Boris and Svetlana each may have *preferences* about how much transactional surplus the other ought to get (imagine Boris is a committed egalitarian; Svetlana believes herself deserving of the lion's share), each also lacks the information necessary to make the *satisfaction* of those other-regarding preferences (which may be and often are mutually incompatible¹³) a condition of transacting. Consequently, they are more likely to transact. This means that people need not, as a matter of psychological or attitudinal fact, *be* nontuistic. They need only act *as if* they are nontuistic and reservation price deception, mutually practiced, induces participants in bargaining to act as if they are nontuistic by depriving them of the information they need to make their other-regarding preferences a condition of transacting. Differently put, bargainers need not be *affectively* nontuistic, but only *effectively* so;

¹³ In his excellent book, *The Art and Science of Negotiation* (Cambridge, MA: Belknap Press, 1982), Howard Raiffa tells of negotiation experiments conducted at the Harvard Business School wherein each party knows the other's reservation price and each knows that the other knows it (i.e., both parties know the full contours of the bargaining range and know that the other knows it). Despite this, in a not inconsiderable proportion of cases, experiment participants were unable to reach an agreement. In other words, they had divergent preferences over how much of the transactional surplus the other party should get.

reservation price deception, mutually practiced, makes them effectively nontuistic—whatever their other-regarding preferences or attitudes.

6. Fit Participants in Commercial Culture

While our evolved practices of bargaining and negotiation work to *synthesize* nontuism of one kind, with respect to one kind of other-regarding preference in market exchange, nontuism in market exchange is an attitude worth *cultivating* in its own right. In its absence, it is harder to trade with people and harder to live a flourishing life in a culture in which commerce is the principal means by which we acquire the things we use to make our lives. In a commercial culture, it is imprudent to be like Trollope's Mrs. Proudie, who "had been staunch to her own party, preferring bad tea from a low-church grocer, to good tea from a grocer who went to the ritualistic church or to no church at all."¹⁴ Far better to be like former NBA great Charles Barkley, who said notoriously, "I can be bought. If they paid me enough, I'd work for the Klan."

For many critics of the commercial ethos, to align it with Barkley's sentiment is proof positive of the psychopathy induced by, or rewarded by, the market. But what, exactly, is psychopathic about Barkley's sentiment? He has said, in effect, that he can coexist in a society with people whose views and values are utterly divergent from—indeed antithetical to—his own. What is more, he can imagine projects over which he can cooperate with them if their aims and interests touch his at a point. These are the archetypal sentiments of *liberal toleration*—a constellation of dispositions that even many of liberalism's critics concede to be virtuous. That Barkley imagines the projects over which he cooperates with those holding divergent views are *commercial* projects illustrates something important. With respect to potential commercial partners, Barkley must be nontuistic. Nontuism then, far from a commercial form of psychopathy, appears instead to be liberal toleration *in its commercial guise*. Nontuism is the way liberally tolerant people deal commercially with others in order to maintain their tolerance and the tolerance that characterizes their society.

If the foregoing is correct, then entering or encouraging the market for values is not just individually imprudent, but also collectively destructive of a liberal social order. The market for values undermines and displaces toleration in the most important venue for social cooperation in a commercial society—the market. It fractures and factionalizes the social institution that best facilitates social cooperation between people of divergent views and values by fostering cooperation on minimal terms. What is more, a culture

¹⁴ Anthony Trollope, *Barchester Towers* (1857), accessed online at: <http://www.gutenberg.org/etext/3409>.

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characterized by people with the disposition to enter the market for values will not long remain a commercial culture. If people are characteristically disadvantaged by their dispositions owing to the prevailing institutional arrangement, they will not long acquiesce in that institutional arrangement. Fit participants in commercial culture, consequently, will be ill-disposed to enter the market for values and will be disposed to discourage others from entering it. Although they have the right to do so and doing so violates no one's rights, entering the market for values is often imprudent and reinforces dispositions foreign to a commercial society. That is because the market for values is more at home in a society where one's prospects for economic success turn on who you are affiliated with politically ("us" rather than "them") and as much or more effort is expended diminishing the prospects of those who are *not* affiliated with you as is expended advancing the prospects of those who are. (Anyone who has participated in a tenure decision knows *exactly* what I'm talking about.) That is not a description of an entrepreneurial, commercial society—or at least one that is likely long to remain one. It is a description of many other social orders (e.g., Soviet socialism) that the denizens of commercial societies have been fortunate to escape and that classical liberals hope those less fortunate will someday escape. Consequently, the flowering of the market for values is not evidence of commercial society's moral progress, but of the indulgence of retrograde tendencies opponents of commercial culture (like most university academics) are understandably eager to encourage.

The Sloppiness of Business Ethics

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1. Introduction

The magazine *Business Ethics* ranked Fannie Mae as the most ethical company in America in 2004. By 2005, Fannie Mae's chairman and CEO, Franklin Raines, would be forced out as government auditors tried to sort through what they found to be "an unethical and arrogant culture" that was manipulating earnings, to the tune of a \$7 billion restatement.¹ Juniper Networks was also on the list in 2005, but by August 2006, the company issued a release explaining that its earnings back to the beginning of 2003 could not be relied upon and had to be restated because of problems with backdated stock options given to executives. The amount of the company's restatement was \$900 million.² Hewlett-Packard finished seventh on the list in 2005, but then headed down a path of boardroom spying on its directors. These pretexting activities would cost the company a \$14.5 million settlement as well as a good chunk of its executive team for their complicity in what appeared to be a strategy of "we'll fix them."³ Southwest Airlines has been on the list for the eight years of the list's existence, but in 2008, Southwest paid a \$10 million fine for its failure to conduct structural inspections on its planes.⁴ Moody's has long been part of the Top 100, but found its CEO hanging his head before Congress as an email surfaced in which an employee wrote that the firm's ratings of mortgage-based securities demonstrated that "we are incompetent at credit analysis" or "we have sold our soul to the devil for

¹ James R. Hagerty and Gregory Zuckerman, "Fannie Mae Accused of Rulebreaking," *Wall Street Journal*, April 7, 2005, p. A3.

² Juniper Networks Inc. 8-K, issued December 20, 2006, accessed online at: <http://www.sec.gov>.

³ Jim Hopkins and Michelle Kessler, "HP Gets Out of Suit for \$14.5 Million," *USA Today*, December 8, 2006, p. 1B.

⁴ Andy Pasztor and Melanie Trottman, "New Safety Setback Grounds Southwest Planes," *Wall Street Journal*, March 13, 2008, p. B1.

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revenue.”⁵ Some ironies in the list speak for themselves: Wachovia and WaMu—if only they still existed in all their ethical glory; Merck, if only its major new drug, Vioxx, were still on the market. The examples, illustrations of incongruence between accolades for ethics and hitches in simple acts of compliance with the law, are too numerous to list. Were this any other field, there would be some humiliation in touting failed companies, in product, performance, or existence, as stellar examples of performance. Rankings ought to have some predictive qualities about future performance of the companies that have been ranked.

However, this field of business ethics, a relatively new one, has taken a turn toward ideology. That turn creates a disconnection between ethical evaluations of companies and their actual ethical standards and practices. The simplicity of the criteria used for ethics rankings and ratings attracts the dashboard artists. They can meet the simplistic criteria, and then some thereby win ethical stature and perhaps elude close examination. Bernie Madoff was generous to synagogues and universities; he and his wife were known for their generosity and involvement with charitable organizations. Few companies had a finer record on diversity or community involvement than Fannie Mae. Perhaps the spit and polish with which they shone in some areas deflected attention from their financial statements and operations. Perhaps the perception of their goodness created a fog of ethical righteousness that afforded them a pass on scrutiny for the inexplicable on the financial side.

Without an appropriate level of scrutiny, company practices that harm shareholders and stakeholders continue undetected even as the extent of the harm evolves into practices that can damage markets and economies. For example, most of the Silicon Valley companies have had some form of a dust-up with stock options. Internal and external investigations, restatements, loss of shareholder value, and significant income and tax implications for the employees of these companies have been the effects of this widespread practice. Yet, a side-by-side comparison of the stock-option companies with the “most ethical” lists shows significant dual appearances. Microsoft, Apple, Brocade, and others have all been touted as forward-thinking companies in ethics evaluations. But these three companies and others have had to grapple with options issues. Companies such as Halliburton have never appeared on any list for ethical companies. Yet, Halliburton has always followed a simple practice of dating stock options as of the meeting day when the board grants them—no changes, no complexities, no revisits. Stock options are a contract and when a contract is signed, a price is included.

⁵ “Credit Rating Agencies and the Financial Crisis,” Hearings of the House Oversight Committee, October 22, 2008, p. 7, accessed online at: <http://www.oversight.house.gov>.

Halliburton, as an energy company with a former military contractor subsidiary, is pure poison when it comes to ethics rankings, but it is scrutinized by friend and foe alike. Apple, a darling of ethics rankings, has a Securities and Exchange Commission (SEC) investigation pending into what it knew and when about Steve Jobs's illness and whether it should have been more forthright with shareholders, employees, and the markets on the extent of his illness. Apple's general counsel took the hit for its stock-options issues. Did Apple escape questions and scrutiny because it has the approval and assumed goodness of the social responsibility rankings?

These inconsistencies in scrutiny may be a normal response to the halo effect of a high ethics ranking. In some cases, those halos may be well earned and deserved. But ethics may indeed be in the eyes of the beholders, these developers of screens and lists for ethics. Halo awards are grounded in ideology, are not granted on a scientific basis, and cannot be applied universally in a manner that helps shareholders or stakeholders determine whether their trust in investment, employment, or contract relations with the company is well placed. Why is Google on the list of Ethisphere's Ethical Leaders, but Amazon and Zappo's are not? Touting Starbucks as one of the most ethical companies in the world, as all such ratings lists do, does not mean that Starbucks is immune from the buffetings of markets and economic cycles. When those forces hit, Starbucks must downsize just as General Motors, Boeing, and other industrial firms do.

The sloppiness in analysis behind these rankings does not provide a means by which a vendor, a customer, a potential employee, or an investor can examine a firm for purposes of its trustworthiness. Just because a company manufactures missiles, does not mean it backdates its options grants. And just because a company sells cinnamon-sprinkled foam lattes made from only fair-trade beans, does not mean that it has a good business strategy for growth. Equating ethics rankings with success in business is not grounded in data or sound evaluation. Equating ethics rankings with ethical behavior provides too much of a shield for companies which can very easily meet the superficial screens for those rankings. The rankings and their use require a closer look at methodology and criteria. That closer look yields insight into how to improve these systems for evaluating the ethical culture and commitment of a company.

2. The Criteria in the Existing Rankings

Existing screens for these rankings are predictable. For example, the *Business Ethics* rankings are based on the following criteria of KLD Research and Analytics: Environment, Community, Corporate Governance, Diversity, Employee Relations, Human Rights, and Product Quality and Safety. Apart from the obvious observation that we have no standards for measuring most of these factors, there is the clear ideological screening that will occur. Philip

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Morris (now Altria) has one of the finest cultures for diversity that can be found anywhere in the world in any industry. If a company wanted to understand how diversity is achieved, how it is made part of the fiber of a company, and how it becomes a natural force, Philip Morris would be the company to study. Philip Morris, however, will not appear on any ethics list because it sells tobacco. It is what is called among the social responsibility folks a “sin stock.” Sin stocks include companies that sell tobacco, alcohol, and weapons, the three top killers in the world, except for terrorists with box cutters.⁶ Those who market things that could harm us need not apply for a position in the ethics rankings. Oddly, McDonald’s does appear on the list of the 50 most ethical companies in America (litigation and fast-food-nation dogma aside). KLD, in a bow to the fact that sometimes people just have to sin, has created separate rankings for the “sin stocks.” For example, there is now a ranking for ethics among alcoholic-beverage makers. These firms are not permitted to sit at the big table for ethics rankings because of what they sell, but they can be best-in-class for alcoholic-beverage makers. They earn that slot through restrained marketing efforts: They must have a marketing plan that is directed at young people, one that reminds them to be responsible when sinning, that is, drinking. They can inch even higher if they have a program that works to prevent under age people from drinking.

The original screens of no weapons or vices have given way to the newer Environmental, Social, and Governance (ESG) screens. Perhaps in a tip of the hat to the profits of vice or maybe as a means for actually tying these ethics screens to profits, the ESG screens are touted as a second layer of research for evaluating companies’ strategies for addressing these issues, the theory being that such hand-wringing on the part of a company is a proxy for evaluating creativity, which is necessary for competitive advantage and profit sustainability.⁷ While referred to as well-thought-out screens, the connecting data between those factors and Return on Investment (ROI) is not quite there. In fact, the connection lives only in the assertions of the fund managers who employ ESG screens in differing, albeit nebulous, forms: “We believe that over time the second layer of research can add significant value to a portfolio.”⁸

⁶ So strong was the former aversion to alcohol that Pax World Management sold its Starbucks holdings when Starbucks went off the tracks by allowing its name to be associated with a coffee liqueur product.

⁷ Carolyn Cuim, “For Money Managers, A Smarter Approach to Social Responsibility,” *Wall Street Journal*, November 5, 2007, p. R1.

⁸ *Ibid.*

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Goldman Sachs has attracted international attention for concluding that its ESG screens identified forty-four companies that outperformed its other companies by 25%. Goldman uses screens for human rights, labor standards, environment, and anti-corruption, where, as it notes, information is available. However, the companies in the Goldman Sachs group are not always publicized, the hoopla being that ESG improves the bottom line. Goldman has both energy (five oil companies) and mining companies (four) among its forty-four top companies, companies that are screened out of ethics ranking and often banished among the sin stocks, the sin being fossil fuels.⁹ Royal Dutch and Shell were included in the Goldman “Green is Gold” list, as were five pharmaceutical firms. Sixteen of the companies are alternative energy and environmental technology firms. It would not be difficult to predict that these companies would enjoy a boost to their bottom lines because political winds send favor and funding their way. The remainder of the Goldman forty-four portfolio has the likes of Pepsi, Nestlé, pharmaceuticals, and a slew of biotech firms, some of which, like Genentech, have been the target of criticism for the nature of their products as well as for one-year requirements for use. Goldman’s evaluation is actually more of a measure of responsible operations. A mining company that is not plagued by strikes or mandatory reclamation will indeed be more stable and profitable. A pharmaceutical firm whose products consistently reach market and remain there without recall, something that reflects adequate up-front testing and warnings, will enjoy sustainable growth. The screens, however, may simply be measuring a quality business operation that does not withhold information, is prudent in product development and testing, and focuses on long-term success over short-term profits. In other words, the business is well run, a strategy that keeps it both profitable and out of legal, ethical, and social difficulty.

ESG ratings remain fluid, with new metrics being added. Carbon emissions are a new data point, something used as a proxy for sustainability devotion, which is theorized, although not proven, to mean greater creativity at that company, thereby leading to a better bottom line, thereby leading to a competitive edge, thereby leading to long-term survival, that is, sustainability. In some evaluations, carbon emissions are not a data point, but there is a more general category of devotion to addressing climate change. This emerging screen offers no clear definition or measurement criteria.

Gender diversity is a new category that carries no definition, thereby confounding the author’s simple notion that gender diversity was long ago

⁹ The Goldman report, “Global Introducing GS Sustain,” can be accessed online at: http://www.unglobalcompact.org/docs/summit2007/g_s_esg_embargoed_until030707pdf.pdf.

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conquered with the formula: “males” + “females” working in the same place = gender diversity, something that we have had since Cleopatra was in charge near the Nile. Apparently, there are nuances in that formula that must be met to be truly gender diverse, and gender diversity means more creativity, which means a better bottom line, and so forth.

Not surprisingly, executive pay is also a new screen emerging on the rankings and ratings radar. This screen is distinct in that it does actually permit comparisons in some form across companies. However, how the numbers used in this screen will be used remains a mystery. Some advocates of this number-as-a-means-of-ethics commitment employ a ratio formula limit between the lowest salary in the company and that of the CEO, à la Ben & Jerry’s pre-Unilever. An example of this metric would be that in ethical firms the CEO’s pay cannot be greater than ten times the lowest salary or the mean or median compensation for non-executive employees in the company.

3. The Methodology in the Existing Rankings

As important as the criteria used for the ranking would be, the methodology used for gathering the information on how well the firm did on the criteria is more important. KDL, the firm that is used by *Business Ethics* for its rankings, uses a five component model:

- Communications with company officers
- Research partners (ESG firms)
- Media reviews
- Public documents (SEC 10K’s, proxy statements)
- Government and Non-Governmental Organization (NGO) information

Of the five components, only one and one-half (public documents and government information) would not carry some form of interpretation and possible bias. Which NGOs are tapped, company officer spin, ideological foundations of ESG firms, and differing media outlet standards and ideology would affect the information obtained from the remaining three and one-half sources. Ironically, the data are gathered from those who are committed to obtaining reforms, with those reforms being their view of the issue. Companies are thus rated by the research firms and organizations that have set their own standards for ethics and social responsibility and who have outlined their conclusions about appropriate courses of action on social, environmental, and governance issues. For example, an NGO committed to human rights may have a standard that prohibits companies from having any business activities in countries in which there are human rights violations. Yet the presence of companies and business activities in China may well be helping dissidents there. The ideological screens of NGOs affect the ratings, ratings

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that do not consider nuance in either the issues or in a company's expansion and presence in a particular country.

Goldman Sachs introduces its ratings with a disclaimer that covers all the methodological flaws.

Our proprietary ESG framework reflects the fact that all companies have to interact with the four pillars of: the economy in general, their industry, society and the environment. All companies will have some issues that surround them in respect of one of the pillars.

Our methodology is not designed to be comprehensive, nor is it designed to be prescriptive in judging what is good or bad practice. It is based on a consistent approach of analyzing objective, quantitative measures which can be adjusted by industry as appropriate.¹⁰

One has to respect an ESG evaluation in which the evaluator confesses up front that it is all soft data, that they are not recommending any investment prescription from the data, and that, by the way, the data are not really comprehensive. In fact, there is one additional disclaimer in the Goldman Sachs 179-page ESG report that is not found in any of the media reports on the Goldman Sachs data (namely, Green is Gold) that is pure gold in terms of summarizing the entire ethics/social responsibility ratings:

We have found no correlation across sectors or within sectors between any of our ESG metrics and share price performance. In part, we believe that this is due to the inadequate timeframe and mismatch in terms of timing in relation to the analysis: It takes some time for superior performance on ESG metrics to feed through into financial performance and stock market recognition. However, the poor performance of indexes such as Dow Jones Sustainability Index and FTSE4Good (both -10% since 2000) suggests that a simplified approach of picking stocks on an ESG basis alone will not lead to stock market outperformance.¹¹

In short, dear investor, look at the financials.

The Dow Jones Sustainability Index has a layered and weighted approach to its methodology.¹²

¹⁰ Ibid.

¹¹ Ibid.

¹² This chart can be accessed online at: http://www.sustainability-index.com/07_html/assessment/criteria.html.

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Corporate Sustainability Assessment Criteria

Dimension	Criteria	Weighting (%)
Economic	Codes of Conduct / Compliance / Corruption & Bribery	5.5
	Corporate Governance	6.0
	Risk & Crisis Management	6.0
	Industry Specific Criteria	Depends on Industry
Environment	Environmental Performance (Eco-Efficiency)	7.0
	Environmental Reporting*	3.0
	Industry Specific Criteria	Depends on Industry
Social	Corporate Citizenship/ Philanthropy	3.5
	Labor Practice Indicators	5.0
	Human Capital Development	5.5
	Social Reporting*	3.0
	Talent Attraction & Retention	5.5
	Industry Specific Criteria	Depends on Industry

The * means that only public reports are used in evaluating this issue. Other information comes from:

- Sustainable Asset Management (SAM) questionnaire¹³ (completed by the company)

¹³ SAM is a research firm based in Switzerland, and its criteria are the same as those of the Dow Jones Index.

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- Company documents (both public documents and company-furnished reports)
- Media and stakeholder reports (including commentary on the companies)
- Personal contact with the companies

Four of these resources do carry bias in some form. The SAM questionnaire is one developed by SAM Research. Its board of directors, its website, its questionnaire, the list of companies, and Goldman's comment on the financial performance reveal that the goal is not one of measuring long-term financial viability or survival of companies, but rather, companies' commitment to the ideology of those involved in creating the metrics.

4. Going Forward: A Neater Evaluation

The diagrammed models for the evaluation mechanisms employed by the ranking/rating systems look impressive. Just the translation of gathered data and responses from the sources into the model generates impressive print-outs (if indeed printing out documents is not one of the negative measures). But, as noted in the introduction, after all the evaluations, criteria, data, and interviews, what do you have when the company fails? Those who create and rely upon these ethics evaluation systems acknowledge that they are not an effective mechanism for determining what will or will not be a good investment. Indeed, the research labs are littered with the huddled and whimpering researchers who have tried to find "good" companies. This new approach of rating a company on the basis of ethics, sustainability, and other NGO factors will prove equally elusive. The reality is that you cannot effectively separate out some of the softer factors these systems try to measure. There is a whirling set of components that make up a successful business. Those components are standard across companies and industries and, perhaps surprisingly to the compulsive rankers and raters, consist of a great many ethical factors. Companies may not always understand that their devotion to ethical principles is what has brought them sustainability, but they do have these elusive qualities of goodness.

Finding and counting those elusive qualities will produce a meaningful dashboard and, as a result, some meaningful ratings. The measurements will not be found in ideological-based criteria such as human rights and climate change. Rather, they will be found in a return to measuring Aristotelian qualities, which, if present, will find their way to the critical issues. For example, if we were searching for a company that exemplified ethics, then surely accurate and transparent financial statements would be a very basic requirement. If we were to list the qualities of an ethical company, then compliance with safety standards and violation-free inspections would be part of the definitional mix. Easily addressed, easily measured, and relatively

easy to follow, these standards offer simple metrics. These straightforward qualities in a company are not a culled-out part of the rankings and ratings discussed earlier. But they do get at the specifics these other ratings try to measure. The following sections offer some ideas for standardized measures that could be put together to paint a fairly accurate picture of the goodness and sustainability of a company. No one factor is determinative. The purpose of this new approach in evaluating ethics and goodness is to be sure that we miss nothing in our evaluation. Fannie Mae was great on community and stakeholders, but fraud always throws a damper on the ethical evaluation of a company. The following metrics should serve to rate but also serve to throw down flags when a company is sliding into ethical and, too often, legal difficulty.

5. The Measures to Keep and Expound Upon from Existing Squishy Models

There are some factors measured in some of the models that are worth keeping in a goodness evaluation. Generally known as the governance factors, some of these are similar to those in the corporate governance portions of the ratings and rankings systems, because research shows that they have some relevance in a company's goodness, and they can be obtained through information sources that are not self-reported, spun, or ideological. However, this list goes beyond traditional governance measures because examination of some of the recent collapses shows that the critical role of a board is to make sure that the information employees have about unethical and illegal practices gets to them so that they have the information and can take corrective action. There are more factors that could provide additional quantitative information, but these are the factors that can be compared easily and can signal the need to ask more questions and obtain more information.

- Does the company have a code of ethics? If they write something down, they have two benefits: some rules, and the cognitive dissonance that sets in with someone when the rules are broken or circumvented. A new trend is for the company to track any waivers granted to the code of ethics and to whom.
- Does the company have a majority of independent directors? One caveat—check the directors for interconnections on philanthropic organizations. They may be independent for SEC disclosure purposes, but they may inextricably be intertwined in their community work and a great deal of back-scratching results from these dependencies for funds.
- Are the chairman and CEO two different people? The control of board agendas and processes by the CEO creates a conflict that other

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directors cannot address effectively because their access to information is limited by the control of the process by the CEO.

- Are the executives under the same medical and insurance plans as other employees?
- What are the perks? This count is a simple numbers and cost-of-perks measure. The more the perks, the greater the risk. Trends indicate that companies have gone to straight compensation from which executives can pay for their own perks. The SEC-mandated disclosures on executive perks have cut back greatly on perks.
- Does the board of directors have a separate anonymous reporting system? Does the board of directors review all issues sent in through anonymous reporting systems? WaMu, Wachovia, and Moody's all had employees who were aware of the basic flaws in their business models and that they were participating in them, but that information could not make it through the officer team that had structured the business model. This end-run access to the board is there as a pressure relief valve when employees cannot obtain responses through the usual ethics/compliance channels. Even the sales force at Merck was aware of the questions about Vioxx.
- How many board positions do the directors hold? The professional board member is less likely to devote the time necessary for effective meetings as well as interaction with employees in the company.
- Do board members have open access to officers and facilities? That old management theory of management by walking around (MBWA), is an important tool in understanding the openness, compliance, and ethics of a company.

6. Safety

Part of the human rights component that is included in many of the ratings is just the way a company treats its employees. We could rely on the availability of flex-time, on-site child-care facilities, and other ideological measures, but we could begin with a metric that takes into account well-being and respect for employees even as it provides some insight into the precision of operations. One easily measurable data point in answering the general rating question of, "How are employees treated?" that is not tainted by self-reporting, spin, or ideological parameters, is the all-injury-incident rate (AIIR). All companies have an AIIR. No one interprets, fudges, or alters this rate. Indeed, the rate is determined only after the incidents have been reported and reviewed by both the reporting agency and the company. By the time we have an AIIR, everyone agrees it represents what happened at the company in terms of the number of injuries. This metric eliminates the interpretive and ideological flaws of the other rating systems. A company with a high injury rate tells us any one or all of the following: the company's safety standards

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are lax, the company's employees are not trained effectively, the company's employees are not screened effectively, or the company's demands on employees mean employees are moving too quickly (because of incentive programs or demands of supervisors) to comply with safety requirements. If any or all of these four behaviors is present in the company, you cannot have a sustainable operation. Long-term and productive operations require safety. The measurement of goodness must be tied to the business outcome measures for the goodness = success hypothesis to be correct.

7. Financial Performance

With financial performance, we are not looking at the standard financial measures of performance. Rather, we are exploring how the company got to these numbers. This factor measures several virtues, including that of honesty, because it is looking beyond the financial reports' being in compliance with Generally Accepted Accounting Principles (GAAP) and Financial Accounting Standards Board (FASB). This factor measures the quality of earnings. In applying this metric, we would look at the following:

- What percentage of income is from one-time events, discontinued operations, etc.? What percentage of income is from core business operations and what comes from peripheral activities such as hedging? There is nothing evil about one-time profitable transactions. However, the danger is that shareholders, employees, and vendors are duped into believing that the company is making money through its core business. For example, Ford's earnings picture in 2004 looked as if it was selling a large number of trucks. In fact, much of its financial performance came from currency adjustments and other non-core business transactions. The stock jumped 6.1% when this bright earnings picture was released. But the earnings did not reflect what was going on in the core business. Bright analysts figured that out, but most of the market did not. Therein is the heart of business ethics. Are you honest in your disclosures about your financial situation? The same types of sleights of hand were used by Enron (off-the-book debt hidden in special purpose entities), NewCentury Financial, and CountryWide Mortgage (liberal interpretation of when loan values had to be written down). There is the ethical issue of a false impression here, but also the issue of how long a company can keep the sleights of hand going, that is, whether there is a sustainable revenue path present and being attended to.
- Over the past five years, how close were earnings projections to actual numbers reported? In this metric, you hope that the

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earnings were off prediction because if these numbers are too close then you have an honesty issue. HealthSouth, a company that would lose many of its officers to prison and its CEO to a bribery conviction, noted in its 2001 annual report that it had met earnings to the penny for 47 quarters in a row. One of the whistle-blower letters to the SEC about Madoff Securities read this simply, “Although I cannot point to anything concrete, consistent earnings of 12%-18% for the last 20 years tells me that something is wrong here.”¹⁴ This feat of consistent, positive, and predictable earnings over long periods is not possible and provides a fairly good measure of the honesty of those running the company.

- What is the company’s debt level? The higher the leverage, the less flexibility a company has in pursuing long-term strategies and the greater the pressure to cross ethical lines. Sustainability requires measured and reasonable growth that allows for some margin for error in the plan. Once again, this financial metric is a fairly accurate indicator of the ability to survive over the long term.
- What changes have been made in the capital stock structure? Manipulation here indicates that goodness may not be afoot, and this manipulation serves to conceal the true financial status of the company. In addition, manipulation here demonstrates a bit of callousness to existing shareholders. Dilution is an ethical issue. Dilute a shareholder, a person to whom you are indebted for your business capital, and the likelihood that you would be unfair to others increases.

8. Conditions of Facilities and Equipment

There are some business experts who say they can “smell” problems and demise when they walk into a business. Often just the levels of inventory are a give-away. Rite-Aid’s shelves were bare just before we uncovered the problems there that resulted in a \$1.6 billion restatement and the conviction of several officers. For production companies, the condition of the factories is a tool for determining sustainability. The bankruptcy of Peanut Corporation of America following the FDA’s connection of that company to salmonella poisonings in forty-four states is not a surprise to those who had once worked at the company. The company’s facilities had leaking roofs, cracks in walls and windows, and

¹⁴ Kevin McCoy, “SEC Received Numerous Warnings Over Madoff,” *USA Today*, February 24, 2009, p. 4B.

conditions that found employees complaining about the elements.¹⁵ True to the change in equity question discussed above, the once-public company went private when the owner's son bought it back.

This metric gets at the sweat shops and human rights issues as well. In fact, long before the social screens became popular, there were companies, such as L.L. Bean, that used this form of monitoring to be sure of its contractors' plant conditions, something that served to increase quality and productivity. Again, the quantitative measures provide insight for goodness but are also key drivers in the general business goals of production quality and efficiency.

9. Turn-Over: Employees and Executives

Public documents tell a story without ideology or self-interpretation: Examine the level of executive turnover in a company. Place the turnover side by side with the other factors (such as financial performance), and you have a picture of sustainability or demise. Add in the turnover among employees, particularly delineated by division, and you will generally obtain some insights into the culture of the company. Indeed, turnover in a particular plant, division, or area of the company is a signal to look more carefully. A study of Hewlett-Packard that reflected turnover there, in its board and staff, would have been a flag of the dysfunctional culture that had taken over this proud company. Yet, with all that was happening there, the metrics in the standard measures did not pick up the problem. This factor zeroes in on dysfunction.

10. Litigation and Regulation

Without exception, every company that is now in bankruptcy, has been taken over, or is the target of investigation had a precursor regulatory/litigation warning. In 2003, both employees and financial experts were issuing public warnings about the accounting practices of Fannie Mae. By 2005, Fannie Mae was given a scathing review of its accounting practices and required to restate its earnings, a reduction of \$7 billion, yet its officer team remained in place. Regulators had been concerned about AIG since 2005 when Hank Greenberg was removed as CEO. That the regulators could not find much at that time does not necessarily lead to the conclusion that all was well with this financial giant. The same can be said of any pending regulatory actions and litigations involving any company. Too many screens reach the

¹⁵ Jane Zhang and Julie Jargon, "Peanut Corp. Emails Cast Harsh Light on Executive," *Wall Street Journal*, February 12, 2009, p. A3.

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conclusion that because a suit is dismissed or the regulator finds no violations, the company has been given a clean bill of legal health. However, what generally happens is that the regulator is there and the suits have been filed prematurely. There is indeed something percolating that can be destructive to the company, but the actions are not yet legally ripe. The following measurements are critical in evaluating the ethical culture of a company.

- Regulatory investigations
- Investor suits
- Employee suits
- Vendor/supplier suits
- Competitor suits (intellectual property, antitrust)
- Regulatory and litigation settlements
- Amount in litigation reserves, particularly changes in the amounts reserved

Any ratings program needs to factor in all such actions, regardless of outcome because dismissal or closure is not a determinant of either an ethical culture or that no issues remain that require resolution for the company's continued performance and financial health. This factor is one that brings in the perception of all stakeholders as well as the shareholders, and it is Aristotelian in nature: Is this company fair to those who work with and for it? Supplier suits can indicate anything from credit problems to aggressive charge-backs, the former being an indication of financial ill health and the latter being an indication of unfairness in the treatment of stakeholders who are critical to ongoing sales and operations. An additional benefit of this metric is that it comes from public records as well. There is no ideology involved in simply examining the activity of regulators and stakeholders vis-à-vis the company.

11. Conclusion

All of the ratings and rankings for ethical companies have an important purpose: they are trying to use qualitative factors and measures to provide insight into the ongoing economic viability as well as sustainability of companies. That the purpose is noble and good does not, however, mean that the metrics are predictive. Indeed, devoting attention to and determining ratings and rankings from factors such as diversity, carbon emissions, and executive pay may be detracting from the quantifiable, readily available, and easily comparable metrics recommended here. Indeed, that seal of approval for "ethics" on the basis of metrics that do not necessarily correlate to Aristotelian ethics serves to offer an imprimatur to companies that need additional scrutiny. Dedication to climate change issues does not mean that

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the company is not heating up its own books. This sloppy conclusion has allowed a form of green hucksterism to detract from the real hucksters. If the goal is measuring ethics and sustainability, the screens, ratings, and focus should shift to the basic measures outlined here. The ratings from these metrics might have helped us see a few of the Ponzi schemes, frauds, and risky business models that escaped us in our zeal for the ideal company that catered to our ideological views.

The Business Ethics of Incarceration: The Moral Implications of Treating Prisons Like Businesses

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1. Introduction

Historically, punishment theory has attempted to resolve questions such as: What is a just penalty for crime? How severely should society punish criminals? And what are the nature and causes of criminal behavior? More recently, a subfield of punishment theory has focused upon the moral and practical implications of prison privatization—the use of privately owned and operated firms to produce, manage, and allocate the services of incarceration. Greatly debated by economists and moral theorists alike, prison privatization debates have both consequentialist and deontological components.¹

Consequentialists at heart, most economists have characterized incarceration as a *public good*. The services of law and order (imprisonment being one key component) produce positive externalities to non-payers.² If an individual paid for the production of criminal law—say, hired a security officer to patrol his house—his neighbors would presumably be safer in person and property. The logic is similar for incarceration. If a victim were to pay for a criminal to be punished as a service,³ non-payers would also

¹ See Hugo Adam Bedau, “Punishment,” *Stanford Encyclopedia of Philosophy*, accessed online at: <http://plato.stanford.edu/entries/punishment/>.

² See Tyler Cowen, “Law as a Public Good: The Economics of Anarchy,” *Economics and Philosophy* 8 (1992), pp. 249-67.

³ Under present institutional arrangements (government provision or government contracting-out of prison services), incarceration is costly. As of 2004, the United States spent over \$60 billion on correctional services; see Lynn Bauer and Steven Owens, “Justice Expenditure and Employment in the United States, 2001,” *Bulletin, NCJ 202792* (Washington, DC: United States Department of Justice, Bureau of Justice Statistics, May 2004). Were prisons completely privatized, some conclude that the

supposedly be better off. The law-breaker could not commit further crimes while he was in jail, which is the *incapacitation effect*.⁴ And other potential criminals would be deterred from engaging in crime for fear that they would also be punished, which is the *deterrence effect*.⁵ When third parties benefit from punishment services but are not made to pay for them, it is said that punishment is a *non-excludable* good. Non-excludable goods are often thus said to be *under-provided* by voluntary markets. David Friedman explains, “nobody pays and nobody gets, even though the good [in this case, additional units of incarceration services] is worth more than it would cost to produce.”⁶ Economists typically conclude that state subsidies *can* and *should* resolve the problems associated with sub-optimal output,⁷ but recent contributions to the theory of public goods have explained that it does not necessarily follow that government provision will be more efficient than the presumably inefficient market.⁸ This article takes seriously this recent development in the theory of

costs of imprisonment would be *negative*; see Bruce L. Benson, “Customary Law with Private Means of Resolving Disputes and Dispensing Justice: A Description of a Modern System of Law and Order without State Coercion,” *Journal of Libertarian Studies* 9, no. 2 (1990), pp. 25–42. That is, the revenue earned from the productivity of inmates would be greater than the overhead costs of operating prisons. Many libertarian philosophers support criminal-justice paradigms based upon *restitution* from criminals to victims as an alternative to retributive- or rehabilitation-punishment paradigms; see Randy Barnett, “Restitution: A New Paradigm of Criminal Justice,” in *Assessing the Criminal: Restitution, Retribution, and the Legal Process*, ed. Randy Barnett and John Hagel (Cambridge: Ballinger Publishing Company, 1977).

⁴ Steven Levitt and Daniel Kessler, “Using Sentence Enhancements to Distinguish between Deterrence and Incapacitation,” *Journal of Law and Economics* 42 (1999), pp. 343-63.

⁵ See Isaac Ehrlich, “The Deterrent Effect of Criminal Law Enforcement,” *Journal of Legal Studies* 1, no. 1 (1972), pp. 259-76; Isaac Ehrlich, “The Deterrent Effect of Capital Punishment,” *American Economic Review* 65, no. 3 (1975), pp. 397-417; and Isaac Ehrlich, “The Deterrent Effect of Capital Punishment: Reply,” *American Economic Review* 67, no. 3 (1977), pp. 452-58.

⁶ David Friedman, *Hidden Order: The Economics of Everyday Life* (New York: HarperCollins, 1996), p. 278.

⁷ See any standard microeconomics textbook, e.g., N. Gregory Mankiw, *Principles of Microeconomics*, 5th ed. (Mason, OH: South-Western Cengage Learning, 2008), pp. 226-30.

⁸ This critique is relevant for public goods theory in general. See Tyler Cowen, *Public Goods and Market Failures: A Critical Examination* (New York: Transaction, 1991); David Schmidt, *The Limits of Government: An Essay on the Public Goods Argument*

public goods and applies it specifically to the topic of incarceration in order to make progress in the debates concerning prison privatization.

The traditional moral analysis of incarceration arrives at a conclusion similar to the consequentialist analysis, namely, that prison services should not be left to the private market, but that these results are reached through a nearly opposite rationale. Criminal justice institutions are said to possess some unique metaphysical quality—they involve determining matters of justice and they require inhibiting the liberty of autonomous individuals.⁹ In the hands of private actors these mechanisms of force can have a corrupting influence. It was not a concern for *under*-provision but *over*-provision which motivated the moral case against market involvement in punishment.¹⁰

These arguments supporting the view that the realm of criminal

(Boulder, CO: Westview Press, 1991); and Randall Holcombe, "A Theory of the Theory of Public Goods," *Review of Austrian Economics* 10, no. 1 (1997), pp. 1-10. On the social provision of law specifically, see Bryan Caplan and Edward Stringham, "Market Provision of Law, Networks, and the Paradox of Cooperation," *Review of Austrian Economics* 16, no. 4 (2003), pp. 309-26; and David Friedman, "Law as a Private Good," *Economics and Philosophy* 10 (1994), pp. 319-27.

⁹ Richard Harding, in his "Private Prisons," *Crime and Justice* 28 (2001), pp. 265-346, cites the following authors as representative of the view "that imprisonment is an intrinsic or core state function that by definition cannot legitimately be delegated in any of its aspects to a nonstate agency" (p. 266): H. Jung, "Introductory Report," in *Privatization of Crime Control: Collected Studies in Criminological Research*, vol. 27, ed. H. Jung (Strasbourg: Council of Europe, 1990); J. DiIulio, *No Escape* (New York: Basic Books, 1991); Nils Christie, *Crime Control as Industry: Towards GULAGS Western Style?* (London: Routledge, 1993); R. Sparks, "Can Prisons Be Legitimate? Penal Politics, Privatization, and the Timeliness of an Old Idea," in *Prisons in Context*, ed. R. King and M. Maguire (Oxford: Clarendon, 1994); and M. Ryan, "Prison Privatization in Europe," *Overcrowded Times* 7, no. 2 (1996), pp. 16-18.

¹⁰ Randy Barnett (in his "Pursuing Justice in a Free Society: Part Two—Crime Prevention and the Legal Order," *Criminal Justice Ethics* 5, no. 1 [1986], pp. 30-52) summarizes this perspective held by Hobbes and Locke: "When one seriously compares the potential responsiveness of each system [government versus market-based criminal justice], many readers may concede the point and offer the opposite objection: Competing jurisdictions would most likely be too responsive to their customers . . . creating serious social disruption" (ibid., p.40). See also Randy Barnett, "Pursuing Justice in a Free Society: Part One—Power vs. Liberty," *Criminal Justice Ethics* 4, no. 2 (1985), pp. 50-72. Robert Nozick explains the same position: "Men who judge in their own case will always give themselves the benefit of the doubt and assume that they are in the right. They will overestimate the amount of harm or damage they have suffered, and passions will lead them to attempt to punish others more than proportionately and to exact excessive compensation"; see Robert Nozick, *Anarchy, State, and Utopia* (New York: Basic Books, 1974), p. 11.

justice is the appropriate domain of the state and not the market are the dominant perspectives in the literature and in practice. At present, the vast majority of criminal justice institutions in the United States and nearly all developed countries are owned and operated by governments or under their authorities.

There are two major reasons to question the dominance of the state-only prison perspective. First, the long historical record of criminal justice institutions is a direct challenge to these accepted views.¹¹ Economic historian Bruce Benson points out that government's dominant role in criminal justice is a uniquely modern phenomenon.¹² For the majority of human history, criminal justice services were produced, funded, and managed functionally—dare one say, efficiently—by private means.¹³ In various times and places, private entities creatively overcame the challenges of under-provision and non-excludability.¹⁴ Incentivized by the competitive process of profit and

¹¹ Unrelated to criminal justice *per se*, Ronald Coase offers an empirical challenge through historical evidence to traditional public goods arguments; see Ronald Coase, "The Lighthouse in Economics," *Journal of Law and Economics* 17, no. 2 (1974), pp. 357–76. This publication has been subjected to historical criticism by E. Bertrand, "The Coasean Analysis of Lighthouse Financing: Myths and Realities," *Cambridge Journal of Economics* 30 (2006), pp. 389–402. However, William Barnett and Walter Block argue that the potential for privately operated public services such as lighthouses still holds; see their "Coase and Van Zandt on Lighthouses," *Public Finance Review* 35, no. 6 (2007), pp. 710–33; and their "Coase and Bertrand on Lighthouses," *Public Choice* (forthcoming).

¹² Bruce Benson, *The Enterprise of Law: Justice without the State* (San Francisco, CA: Pacific Research Institute for Public Policy, 1990).

¹³ For historical examples of functioning private sector criminal justice services, see David Friedman, "Private Creation and Enforcement of Law: A Historical Case," *Journal of Legal Studies* (1979), pp. 399–415; and Terry Anderson and P. J. Hill, *The Not So Wild, Wild West: Property Rights on the Frontier* (New York: Stanford Economics and Finance, 2004). This list is not exhaustive.

¹⁴ This includes prisons, and much else as well. For more on this, see Barnett and Block, "Coase and Van Zandt on Lighthouses"; Barnett and Block, "Coase and Bertrand on Lighthouses"; Walter Block, "Public Goods and Externalities: The Case of Roads," *The Journal of Libertarian Studies* 7, no. 1 (1983), pp. 1–34; Tyler Cowen, ed., *The Theory of Market Failure: A Critical Examination* (Fairfax, VA: George Mason University Press, 1988); Anthony De Jasay, *Social Contract, Free Ride: A Study of the Public Goods Problem* (New York: Oxford University Press, 1989); Holcombe, "A Theory of the Theory of Public Goods"; Hans-Hermann Hoppe, "Fallacies of the Public Goods Theory and the Production of Security," *The Journal of Libertarian Studies* 9, no. 1 (1989), pp. 27–46; Jeffrey Hummel, "National Goods vs. Public Goods: Defense, Disarmament, and Free Riders," *The Review of Austrian*

loss, private criminal justice systems have been seen to promote innovation and discovery.¹⁵ While fascinating, such examples have had little influence upon real criminal justice policy today, neither in the United States nor abroad.

A second reason to doubt the state-only perspective of incarceration is that governmental dominance over criminal justice institutions has produced a wide variety of mixed results. Governments have not assured efficient, high-quality, or necessarily just outcomes. In contrast, it has been argued that quality improvements in government criminal justice institutions occur only insofar as they confront *hard budget constraints*.¹⁶ Criminal justice scholar Michael Tonry explains that “[w]ithout resource constraints many politicians will argue for more imprisonment for every kind of offender as if

Economics 4 (1990), pp. 88-122; David Osterfeld, “Anarchism and the Public Goods Issue: Law, Courts, and the Police,” *The Journal of Libertarian Studies* 9, no. 1 (1989), pp. 47-68; E. C. Pasour, Jr., “The Free Rider as a Basis for Government Intervention,” *The Journal of Libertarian Studies* 5, no. 4 (1981), pp. 453-64; Murray N. Rothbard, *The Logic of Action: Applications and Criticism from the Austrian School*, vol. 2 (Cheltenham, UK: Edward Elgar, 1997); Schmitz, *The Limits of Government*; Larry Sechrest, “Privateering and National Defense: Naval Warfare for Private Profit,” in *The Myth of National Defense: Essays on the Theory and History of Security Production*, ed. Hans-Hermann Hoppe (Auburn, AL: The Ludwig von Mises Institute, 2003), pp. 239-74; Larry Sechrest, “Public Goods and Private Solutions in Maritime History,” *The Quarterly Journal of Austrian Economics* 7, no. 2 (2004), pp. 3-27; Larry Sechrest, “Private Provision of Public Goods: Theoretical Issues and Some Examples from Maritime History,” *ICFAI Journal of Public Finance* 2, no. 3 (2004), pp. 45-73; and Larry Sechrest, “Privately Funded and Built U.S. Warships in the Quasi-War of 1797-1801,” *The Independent Review* 12, no. 1 (2007), pp. 101-13. Rothbard’s *reductio ad absurdum* of public goods is as follows: “A and B often benefit, it is held, if they can force C into doing something. . . . [A]ny argument proclaiming the right and goodness of, say, three neighbors, who yearn to form a string quartet, forcing a fourth neighbor at bayonet point to learn and play the viola, is hardly deserving of sober comment”; see Rothbard, *The Logic of Action*, p. 178.

¹⁵ Bruce Benson, “Crime Control Through Private Enterprise,” *The Independent Review* 2, no. 3 (1998), pp. 341-71.

¹⁶ Janos Kornai developed the terms “hard” and “soft” budget constraints to explain the shortages and inefficiencies of production in the Soviet Union and other socialist countries; see Janos Kornai, “The Soft Budget Constraint,” *Kyklos* 39, no. 1 (1986), pp. 3-30; and Janos Kornai, “The Concept of the Soft Budget Constraint Syndrome in Economic Theory,” *Journal of Comparative Economics* 26, no. 1 (1998), pp. 11-17. Shortages do not imply that a given good or service is not being produced altogether, but they do signal that demand is exceeding supply and there is no movement in the direction of equilibrium.

imprisonment were a free good.”¹⁷ In fact, Tonry notes that legislative references to state budgets and fiscal constraints help explain the few successful cases of criminal sentencing reform. In desperate times there is little room to be concerned about public goods theory or moral legitimacy. Policy makers will implement what works, or that is, what they think will work, or what voters think will work.

Rising crime rates from the 1960s through the mid 1990s, and the “war-on-drugs” begun in the 1980s, led to a vast expansion of prison facilities and populations.¹⁸ Earlier debates concerning the philosophy of punishment had concluded that the state was the rightful source of incarceration services, but they were resolved at times when state authorities could afford to expand. Financial conditions and public opinion have since changed. Growing crime, tighter budgets, and larger prison bureaucracies have forced decision-makers to entertain the prospect of efficiency gains via private prisons.¹⁹ Today the modern punishment discussion must resolve more nuanced questions than previously: What is the appropriate role of the state in providing incarceration, and inversely what is the proper role of the market? In other words, should prisons be privatized; how and to what extent?

At first, it was thought that market incentives would result in a “race-to-the-bottom” in terms of prison quality standards.²⁰ As firms seek ways to

¹⁷ Michael Tonry, “The Politics and Processes of Sentencing Commissions,” *Crime & Delinquency* 37 (1991), p. 324.

¹⁸ See Jesper Ryberg, *The Ethics of Proportionate Punishment: A Critical Investigation* (Boston: Kluwer Publishers, 2004), pp. 3-5; P. L. Griset, *Determinate Sentencing* (New York: State University of New York Press, 1991); Barbara Hudson, *Justice Through Punishment* (Hong Kong: Macmillan Education, 1987); Andrew von Hirsch, K. A. Knapp, and Michael Tonry, *The Sentencing Commission and Its Guidelines* (Boston, MA: Northwestern University, 1987); Andrew von Hirsch, *Censure and Sanctions* (Oxford: Clarendon Press, 1993); Martin Wasik and Ken Pease, eds., *Sentencing Reform: Guidance or Guidelines?* (Manchester, UK: Manchester University Press, 1987); and Michael Tonry and Kathleen Hatlestad, *Sentencing Reform in Overcrowded Times* (Oxford: Oxford University Press, 1997). All of these authors describe the recent empirical trends of crime and punishment similarly, which place stress and tension upon the previously established and accepted moral punishment paradigms.

¹⁹ See Glenn C. Loury, “Why Are So Many Americans in Prison? Race and the Transformation of Criminal Justice,” *Boston Review* (July/August 2007), accessed online at: <http://www.bostonreview.net>.

²⁰ See Oliver Hart, Andrei Shleifer, and Robert Vishny, “The Proper Scope of Government: Theory and an Application to Prisons,” *Quarterly Journal of Economics* (1997), pp. 1127-61. See also, Charles H. Logan, “The Propriety of Proprietary Prisons,” *Federal Probation* 51 (1987), pp. 35-40; and Samuel Jan Brakel, “Prison

reduce costs, they may erroneously cut needed portions of the production function as well. For example, too few guards coupled with too many inmates can lead to excessive violence.²¹ But the lower operating expenses of private prisons, even if only marginal, are empirically non-ambiguous. By harnessing the incentives of profit and competition, it has been shown that private prisons can hold operating expenses down while increasing the quality of operation.²² Rather than a race to the bottom, quality controls can explicitly be defined in contracts. Thus when comparing public with private prisons on the specifically empirical margins of escape rates, physical health resources, mental health programs, counseling, the amount of recreational facilities, recidivism, and other proxy variables, the latter perform no worse and sometimes marginally better than the former.²³ However, such findings have not swayed the staunch moral opposition against private prisons.

At this point we should make clear an important distinction. Those institutions referred to as “private” prisons in popular discussions do not function completely within a free-enterprise system, but are rather *contracted-out* through government funding. They successfully avoid the majority of free-rider and public goods problems, but they are constrained in their decision-making by the fact that earlier production processes within the criminal justice system (police, courts, legislations, and criminal sentencing agencies) are still monopolized by state control.²⁴ From here on, this article

Management, Private Enterprise Style: The Inmates’ Evaluation,” *New England Journal on Criminal and Civil Confinement* 14, no. 2 (1988), pp. 175-244.

²¹ See Steven Levitt, “The Effect of Prison Population Size on Crime Rates: Evidence from Prison Overcrowding Litigation,” *The Quarterly Journal of Economics* 111, no. 2 (1996), pp. 319-51.

²² See Lon Lanza-Kaduce, Karen F. Parker, and Charles W. Thomas, “A Comparative Recidivism Analysis of Releases from Private and Public Prisons,” *Crime and Delinquency* 45 (1999), pp. 28-47; and Harry P. Hatry, Paul J. Brounstein, and Robert B. Levinson, “Comparison of Privately and Publicly Operated Corrections Facilities in Kentucky and Massachusetts,” in *Privatizing Correctional Institutions*, ed. G. Bowman, S. Hakim, and P. Seidenstat (New Brunswick, NJ: Transaction, 1993), pp. 193-212.

²³ Kenneth Avio, “The Economics of Prisons,” in *Changing the Guard: Private Prisons and the Control of Crime*, ed. Alexander Tabarrok (Oakland, CA: Independent Institute, 2003), pp. 9-56.

²⁴ See Alexander Tabarrok, “Introduction,” in *Changing the Guard: Private Prisons and the Control of Crime*, ed. Alexander Tabarrok (Oakland, CA: Independent Institute, 2003), pp. 1-9.

will refer to these arrangements as *contracted-out prisons* and reserve the term *private prisons* for incarceration services nested within a completely market-based criminal justice system.²⁵ Admittedly, this distinction is overly semantic for some of our purposes because the arguments currently pressed against contracted-out prisons attempt to take issue with the essentially “market-like” features of these contractual arrangements. Profits, incentives, and lack of democratic representation would presumably all be characteristics of actual private prisons as they are characteristics of currently contracted-out prisons. Thus our analysis informs both debates.

The consequentialist debate has been fought on predominantly empirical rather than theoretical grounds. Few speculative descriptions of purely free-market prison systems have been described, argued for, or compared across institutional lines. Instead, the current literature (as surveyed above) compares contracted-out prisons with government prisons on a variety of margins pertaining to technological efficiency. The general summary of this literature is that contracted-out prisons have a marginal lead over government prisons. On the other hand, when the normative debates compare contracted-out prisons against government prisons, their predominantly theoretical observations and arguments apply not only to contracted-out prisons, but to all and any application of markets to the criminal justice system. The conclusion from the current literature awards a marginal victory to contracted-out prisons on consequentialist grounds, but it awards a significant victory to governmental prisons over both contracted-out and private prisons on deontological grounds. In other words, opponents of applying markets to criminal justice may admit to the marginal technological gains achieved by contracted-out prisons, but they view these benefits as small and insignificant compared to the overwhelmingly negative moral

²⁵ Anarcho-capitalists apply privatization arguments to the minimum operations of the state—the provision of justice. This literature began in 1849 with Gustave de Molinari, “On the Production of Security,” accessed online at: <http://www.panarchy.org/molinari/security.html>, and received new attention by Murray N. Rothbard, *For A New Liberty: The Libertarian Manifesto* (San Francisco, CA: Fox and Wilkes, 2002 [1973]); Murray N. Rothbard, *The Ethics of Liberty* (New York: New York University Press, 1998 [1982]); David Friedman, *The Machinery of Freedom: Guide to a Radical Capitalism* (La Salle, IL: Open Court Publishing, 1989); and many more recent publications. On the provision of private police, see Patrick Tinsley, “Private Police: A Note,” *Journal of Libertarian Studies* 14, no. 1 (1999), pp. 95-100; Rothbard, *For a New Liberty*, pp. 201-5 and 215-22; and Friedman, *Machinery of Freedom*, pp. 114-20. On the provision of private courts, see Benson, *The Enterprise of Law*, pp. 349-78; Rothbard, *For a New Liberty*, pp. 222-34; Friedman, *Machinery of Freedom*, pp. 114-20; and Edward Stringham, “Market Chosen Law,” *Journal of Libertarian Studies* 14, no. 1 (1999), pp. 53-77. Very little has been done explicitly to describe the potential for purely free market prisons.

essence of running prisons and any other criminal justice services as if they were businesses. It is this staunch moral opposition which is isolated and specifically addressed in this paper. One must first try to understand what are the morally essential features of state-based incarceration services compared to market-based incarceration services, and then determine whether opponents of non-governmental prisons (who are against both contracted-out and private prisons) have calculated accurately the moral costs and benefits of each.

It has been argued that there is something inherently wrong with contracted-out incarceration.²⁶ Contracted-out prisons are said to “profit off of other people’s misery.” Prison activist Paul Wright explains, “at least in public prisons, when prisoners are raped due to inadequate staffing, [etc.] no one can say prison officials did so to line their own pockets and personally profit from the misery of others.”²⁷ As best we can detect, activists against non-governmental prisons have attempted to pinpoint three characteristics of contracted-out and private prisons that they deem as essentially immoral: (1) *The existence of profits*. Judith Greene states that “the huge profits to be made by incarcerating an ever-growing segment of our population serve the system well. Profits oil the machinery, keep it humming, and speed its growth.”²⁸ And according to Nils Christie, “[p]rison means money. Big money. Big in building, big in providing equipment. And big in running.”²⁹ (2) *Bad incentives*. Closely related to profits, there is a concern that prison managers will seek their own interests at the expense of the social welfare: “Corporations with a stake in the expansion of private prisons invested \$3.3 million in candidates for state office and state political parties in forty-four

²⁶ See Christie, *Crime Control as Industry*; and Jeffrey Reiman, *The Rich Get Richer and the Poor Get Prison: Ideology, Class, and Criminal Justice* (Boston, MA: Pearson, 1979), pp. 217-20. See also references in note 3 above. In addition, Charles Logan writes, “Organizations that have either opposed or called for a moratorium on private prisons include the American Federation of State, County, and Municipal Employees (AFSCME), the National Sheriffs’ Association, the American Civil Liberties Union (ACLU), and the American Bar Association (ABA)”;

see Charles H. Logan, *Private Prisons: Cons and Pros* (New York: Oxford University Press, 1990), p. 11.

²⁷ Paul Wright, “Introduction to Section 4: The Private Prison Industry,” in *Prison Nation: The Warehousing of America’s Poor*, ed. T. Herivel and P. Wright (New York: Routledge, 2003), p. 137.

²⁸ Judith Greene, “Banking on the Prison Boom,” in *Prison Profiteers: Who Makes Money From Mass Incarceration*, ed. T. Herivel and P. Wright (New York: The New Press, 2006), p. 26.

²⁹ Christie, *Crime Control as Industry*, p. 98.

states over the 2002-04 election cycle.”³⁰ In theory, these lobbying efforts can be an obstacle to lowering crime. (3) *Anti-democratic*. Lastly, they interpret private companies as anti-democratic insofar as they fail to be responsive to the public will.

Bruce Benson relies upon methodological individualism to criticize the moral case against private criminal justice services.³¹ Individual people act; groups do not act, and society does not act. When one argues that the government must provide the services of incarceration, in real terms, she contends that a network of individuals—who happen to take on the role of government—must produce the services of incarceration. But individuals—be they private or governmental agents—can suffer from the same behavioral shortcomings as do buyers and sellers on the market. They do not have access to perfect information, nor are they motivated by perfectly benevolent incentives.

The incentives of private interest transcend the boundaries between markets and politics. Given different institutional arrangements, different expressions of these incentives emerge. It is only with reference to the systematic tendencies of different institutional arrangements and their predictably different outcomes that one can evaluate the net costs and benefits of government versus market or quasi-market prison services. Demonstrating the existence of profits, incentives, and a lack of direct responsiveness does not immediately imply a morally negative essence of non-governmental prisons, nor does it lend direct moral support for governmental prisons.

We do not directly answer the following question: Which institutional structure produces incarceration services better—governments or markets? This is mostly because we do not have sufficient answers to more particular questions: Better according to whom or to what criterion? How are the margins of quality prison services to be defined and communicated by the citizenry? How are they to be detected by institutional suppliers? How are good technological and logistical incarceration methods discovered and implemented? And lastly, how are such methods adopted and improved upon over time? We merely contend that the systematic tendencies of market processes to produce good outcomes, such as social cooperation through the division of labor, are under-recognized by anti-market prison activists. Inversely, the systematic tendencies of government to produce good outcomes through incarceration institutions are overstated within this literature.

³⁰ Greene, “Banking on the Prison Boom,” p. 4.

³¹ Bruce Benson, “Do We Want the Production of Prison Services to Be More ‘Efficient’?” in *Changing the Guard: Private Prisons and the Control of Crime*, ed. Alexander Tabarok (Oakland, CA: Independent Institute, 2003), pp. 163-217.

The remainder of this article is organized as follows. Section 2 defines and explains privatization. It is a transition policy aimed to achieve social cooperation and economic prosperity. Section 3 is an explicit response to the morally charged phrase, “profiting off of other people’s misery.” Such a phrase is meaningless when one recognizes that all for-profit businesses fulfill consumer preferences with regard to various forms of misery. States are not immune to the same accusation; they, too, profit from other people’s misery. The parallel concepts of *capture* and *rent-seeking* used throughout public-choice economics recognize this inherent fact of government action.³² Section 4 offers concluding remarks.

2. What Is Privatization?

Privatization is a free-market reform policy used to transfer production lines from the public sector into private hands. The rationale behind privatization is straightforward: Command and control economies failed to implement rational exchange, production, and distribution throughout society. Central planning repeatedly produced catastrophe. Without property rights, prices, profits, and losses, central-planners lack the incentives, information, innovation, and calculative abilities necessary to produce goods and services in proportionate qualities and quantities as they are demanded by society.³³ Without market prices to coordinate production, goods that are highly demanded are in short supply while goods that no one necessarily wants abound. Market processes are coordination devices; they dovetail the plans of otherwise unrelated and unfamiliar people with one another while avoiding conflict. On the other hand, market-based societies with high levels of economic freedom have experienced peace and prosperity at various times, around the world, and over time.³⁴

³² See James Buchanan and Gordon Tullock, *The Calculus of Consent: Logical Foundations of Constitutional Democracy* (Ann Arbor, MI: The University of Michigan Press, 1962); and Gordon Tullock, “The Welfare Costs of Tariffs, Monopolies, and Theft,” *Western Economic Journal* 5 (1967), pp. 224-32.

³³ See Friedrich A. Hayek, “Economics and Knowledge,” *Economica* 4 (February 1937), pp. 33-54; Friedrich A. Hayek, “The Use of Knowledge in Society,” *American Economic Review* 35, no. 4 (1945), pp. 519-30; Don Lavoie, *National Economic Planning: What Is Left?* (Cambridge, MA: Ballinger Publishing Company, 1985); Ludwig von Mises, “Die Wirtschaftsrechnung im sozialistischen Gemeinwesen,” *Archiv für Sozialwissenschaften und Sozialpolitik* 47 (1920), pp. 86-121; and Ludwig von Mises, *Socialism* (Indianapolis, IN: Liberty Fund, 1981 [1951]).

³⁴ See James Gwartney, Robert Lawson, and Walter Block, *Economic Freedom of the World, 1975-1995* (Vancouver: The Fraser Institute, 1996); and James Gwartney and Robert Lawson, *Economic Freedom of the World, Annual Report* (Vancouver: Fraser Institute, 2008).

The socialist calculation debate was framed as a comparative research agenda until the actual collapse of the Soviet Union. Then, policy makers and reformers were in loose agreement as to the productive merits of market-based societies over central planning. (Though the agreement was loose, it was significantly more so than in previous years; agreement was thus sufficient to implement social change.) The field of transition economics arose to investigate the question: How do we move from here to there? Privatization is one specific form of transition policy. The argument for privatization begins with the realization and admission that many of the goods and services that the centrally planned administration used to produce were in fact crucially important. Food and clothing production in the Soviet Union may have been terribly inefficient and of poor quality, but that does not change the fact that food and clothing are vitally important to human survival. Privatization simply takes production lines that were previously owned, funded, and managed by the state and gives them over to private firms and/or individual owners. As the market process unfolds, some of these will likely expand and others contract.³⁵

Once owned and operated in the private sector, producers rely on prices to harness the dispersed, tacit, and sometimes incomplete knowledge of consumers' tastes and preferences.³⁶ As consumers want more of a good or service they bid up prices, and vice versa if they demand less. Investors and producers allocate their capital assets to those items with the highest profit potential. They are sometimes consciously, but more often unconsciously, guided to make what society wants by responding to their own self-interest and profit motives. It is the rearrangement of incentives away from inefficiency and decline and toward innovation and competitiveness that matters most. Thus Peter Boettke argues in favor of freely giving away state-operated industries and assets in post-Soviet countries.³⁷ Either they stay in business as

³⁵ One must be careful to resist the notion that a privatization has failed, judged only by the fact that the firm constructed out of the government entity goes under. For example, say that a Soviet steel mill is spun off into a business firm, whereupon it promptly goes bankrupt. A failure of privatization? Not necessarily. Capital has successfully been turned over to the private sector, which is all the privatization process can accomplish. That the company later disappears from the scene (perhaps its equipment sold off to others) means, merely, that it could survive only while protected by subsidy; it was not able to satisfy customers.

³⁶ See Hayek, "The Use of Knowledge in Society."

³⁷ See Peter Boettke, *Why Perestroika Failed: The Politics and Economics of Socialist Transformation* (New York: Routledge, 1993); and Peter Boettke, "An 'Austrian' Economists Perspective on Transitional Political Economy," *Ama-gi: The Journal of the Hayek Society at the London School of Economics* 6, no. 2 (2004), pp. 12-14.

a sign of efficient operations, go under as a sign of failure, or sell off the factory to more responsive business people. In any case, improvements are not guaranteed but seem to hold more potential than previous arrangements.

In practice, privatizations have had various results and therefore mixed reviews.³⁸ Clarifying the terms of debate in a transition analysis is very important. If transitions are a matter of moving from here to there, then an effective and efficient transition is often determined by one's presuppositions as to what is so bad about here, so good about there, and the degree of patience that one is willing to afford in making the transition.³⁹ Thus some examples of privatization have been judged negatively only because they did not succeed, based on the expectations of some, in degree or speed. Such debates have resulted in a particular heuristic called the J-curve. The immediate effects of radical policy changes are often disorienting, especially to the lowest economic classes of society. As state-operated industries adjust to the new competitive climate, consumer prices and unemployment rates increase. Thus transition policies are better when they are implemented quickly with minimal opportunities for political reconfigurations and adjustments. Many of the successful transition cases have been cases of *shock therapy*—where significant crises allowed for wide-scale and pervasive institutional reforms to be implemented quickly, thoroughly, and credibly.

The general conclusion of several transition cases and attempts supports the theoretical insights of privatization: Privatization harnesses incentives and information toward peace and prosperity and away from scarcities, conflicts, and strife.⁴⁰ Short-term downturns are consequential and perhaps necessary steps to converging upon new trajectories of progress and prosperity, hence the J-like shape of J-curve graphics. One could even say that this theoretical lens helps to make sense out of the privatization literature and debates to date. The short-term results of privatization reforms were thought to be and have been empirically estimated to be negative races to the bottom. Cost-cutting was closely related to corner-cutting. When the agents within the

³⁸ See Jeffrey Sachs and Andrew Warner, "Economic Reform and the Process of Global Integration," *Brookings Papers on Economic Activity* 1 (1995); and Jeffrey Sachs and Andrew Warner, "How to Catch Up with the Industrial World: Achieving Rapid Growth in Europe's Transition Economies," *Transition* 7, nos. 9-10 (1996).

³⁹ See Boettke, "An 'Austrian' Economists Perspective on Transitional Political Economy."

⁴⁰ See Boettke, *Why Perestroika Failed*; and Timothy J. Yeager, *Institutions, Transition Economies, and Economic Development* (Boulder, CO: Westview Press, 1998).

model are guards and inmates and their social behaviors range from isolated fights to full-out riots, the real short-term effects can be violent and unsavory, difficult to endure without modifying public policy. But in the longer run it seems that states have gotten what they contracted for. For-profit prison firms have learned and adopted logistic strategies for marginal improvements.

Converting America's prison system from public to private control is slightly more complicated, but not fundamentally different from other such cases. Incarceration and other criminal justice services are likely crucial to human civilization and a prosperous economy, but the production of criminal justice services in general and incarceration services in particular is marred by moral stigma in ways that the production processes of menial consumer goods are not. There are good reasons to presume that organizing incarceration (and perhaps the entire criminal justice system) by markets rather than politics will carry technological efficiency gains. But are such marginal efficiency gains a sufficient reason to support market-based prisons in the face of the deontological shortcomings raised by theorists such as Christie and Paul? It seems obvious that the answer to this question depends upon the magnitude that one awards such deontological claims, but are these deontological concerns sound and valid?

There are two main problems with Christie's, Wright's, and others'⁴¹ perspective. First, their imputed moral case against markets rests upon an inaccurate understanding of how markets function. Market processes are characterized by profits and private incentives, but markets also possess an ability to harness these phenomena toward social harmony and a representative system of production and distribution. It is the explicit presence of profits and incentives and their interaction within competitive markets that align self-interest to the satisfaction of others' preferences. Second, in pointing out the existence of profits and incentives within markets and subsequently preferring governmental production processes, such commentators have failed to explain how governments systematically avoid the supposed moral dilemmas imputed to such qualities.

3. "Profiting Off of Other People's Misery"

Profit is the positive difference between costs and revenues. One subtracts all of the costs of operating a business from all of the money gathered by sales (price per unit times quantity sold), and the remainder is

⁴¹ Admittedly, Christie and Wright are less academics and more activists, but their general portrayal of market processes runs parallel to many prominent theorists within the field. See, e.g., sociologist David Garland, *The Culture of Control: Crime and Social Order in Contemporary Society* (Chicago, IL: University of Chicago Press, 2001), p. 204, who fails to recognize that goods and services can increase in quality and decline in price when produced in competitive markets.

profit. The expectation of earning a profit is the motivating force behind upfront investment costs. Individuals act, expend resources, and employ means so as to achieve ends. The value an individual gains from the ends he achieves in excess of the value that he imputed to the costs he endured, is another form of profit. In this sense, individuals act rationally insofar as they only partake in those behaviors in which their ends produce value in excess of costs. Given several opportunities to make a profit, an individual chooses the lowest cost and maximal benefit course of action—she strives to maximize her profits. Profit is not necessarily pecuniary, nor does it have to relate to money at all. Profit can be psychological, spiritual, moral, reputation-based, or in the forms of authority and power.

When firms compete with one another within a free-enterprise system, they bid down each other's profits over time. Holding other things constant or assuming that transaction costs are zero, all profits are eliminated. If a capital owner recognizes that other owners of similar resources are earning profits by making sales, then she too can earn profits by making sales at or below the current market price. Thus prices in competitive markets are bid down, and all firms price at the market-clearing rate.⁴² With profits defined on the one hand, and an understanding of the competitive market process on the other, it becomes easy to recognize the essential, original, or “genetically causal” source of lasting and sustainable profit levels for individual firms.⁴³ Those businesses that continuously provide value, as perceived by their customers, in excess of the prices that they charge will stand the test of time. Value-producing firms are profitable and succeed while inefficient alternatives go bankrupt. Entrepreneurship stands out as the driving force of the market.⁴⁴ A profitable company is one which possesses the best foresight into the changing and contextual tastes of consumers. Over time, the market is characterized by higher quality goods and services at lower prices.

To say that a company profits off of the misery of others is a tautology. Consumers purchase goods and services when they perceive that the value of that good or service is greater than its costs, including the opportunity costs of forgone alternatives, which is to say that consumers are rational in a similar fashion as are suppliers and firms within the market. When a consumer buys a good or service, presumably she experiences some

⁴² See any standard microeconomics textbook, e.g., Mankiw, *Principles of Microeconomics*.

⁴³ See Mario Rizzo, “The Genetic-Causal Tradition and Modern Economic Theory,” *Kyklos* 49, no. 3 (1996), pp. 273-317.

⁴⁴ See Israel Kirzner, *Competition and Entrepreneurship* (Chicago, IL: University of Chicago Press, 1973).

need or desire, some “felt uneasiness” or “misery” which she presumes will be abated by possessing the good in question. Trade is said to be *mutually beneficial* when it is voluntary. If a consumer did not prefer a good she purchased to the value of wealth she gave up, then she would not have voluntarily engaged in the exchange. Trade is a choice where options of lesser value (misery) are given up for options of greater value (alleviation). In this sense, a private prison company profits off of the misery of their consumers (victims) in no distinctive way (other than perhaps a degree of magnitude) compared to a restaurant that profits off of the misery (hunger) of its customers.

We argue that the assumption to treat political actors as rationally self-interested is valid and necessary in order to assess accurately the institutional tendencies of both governmental prison systems and contracted-out prison systems. Financial profits are the guiding motive for investments, expenses, purchases, and sales in the marketplace. But non-pecuniary sources of value instigate rational behaviors in non-market realms as well. Happiness, desire, love, or vengeance can serve as profit-like motives for noncommercial behaviors. Noncommercial behaviors, when understood from an accurate frame of reference, are also characterized by rationality: individuals attempt to maximize benefits while minimizing costs.⁴⁵

Public Choice economics, begun by James Buchanan and Gordon Tullock, seeks to understand political actions and political decision-making as guided and motivated by behavioral characteristics similar to market processes.⁴⁶ Individuals within the political sphere are well-explained when they are held to act rationally. They maximize their personal interests to be re-elected, seek political authority, and maximize political revenues while minimizing costs; they seek rents, hence the term *rent-seeking*.⁴⁷ Such assumptions have been helpful in explaining political history and courses of events in a variety of applied-topic fields.⁴⁸

⁴⁵ See Gary Becker, *The Economic Approach to Human Behavior* (Chicago, IL: University of Chicago Press, 1976); and Israel Kirzner, “Rational Action and Economic Theory,” *Journal of Political Economy* 70, no. 4 (1962), pp. 380-85.

⁴⁶ See Buchanan and Tullock, *The Calculus of Consent*.

⁴⁷ See Anne Krueger, “The Political Economy of Rent-Seeking Society,” *American Economic Review* 64, no. 3 (1974), pp. 291-303; and Gordon Tullock, *The Politics of Bureaucracy* (Lanham, MD: University Press of America, 1965), pp. 120-220.

⁴⁸ Some recent examples include, but are not limited to, the following: Eric Helland and Alexander Tabarrok, *Judge and Jury: American Tort Law on Trial* (Oakland, CA: The Independent Institute 2006), who have shown that the number of civil case rulings and their size of awards are correlated with rational political motivations; and Peter Leeson and Russell Sobel, “Weathering Corruption,” *Journal of Law and Economics*

At this point our distinction between contracted-out prisons and private prisons is more important because the customer bases of the two institutions are different from one another. Understanding how a completely private prison would operate requires a bit of creative imagination. For example, conceptualize a world where individuals and/or victims of crime are required explicitly to enlist punishment and/or incarceration as paid-for services on the market. In such a case, consumers' preferences—revealed by their expressed willingness to pay—would shape the qualities and quantities of prison services. How insecure and how pained by the occurrences of crime that victims perceived themselves to be, would determine their degree of unease when entering the market. Lastly, their perceived benefits and value, obtained by investing in incarceration or other punishment services, would determine their demand for such services.

On the other hand, contracted-out prisons attempt to satisfy the preferences of government officials, central planners, and individuals in state bureaucracies as their bases of customers. If we take seriously the presumption that both providers of prison services and their political customers are motivated by rational private interests to maximize benefits and minimize costs, then we recognize that such institutions can and likely do take on a different structural form from their market-based counterparts. Contracted-out prisons would be operationally and technologically efficient only insofar as the amount of prison contractors within the industry was plural and relatively competitive.⁴⁹ Contracted firms maximize profits by minimizing costs of operation; they under-bid each other to compete for fixed amounts of state-budgets. Contracted-out prisons represent the tastes and preferences of society for punishment and incarceration only insofar as political processes are accurate in detecting, perceiving, designing, and enforcing those preferences within contractual arrangements.

Several key concepts throughout the public-choice tradition expose sources of unresponsiveness in the political processes. Voters are said to be *rationaly ignorant*, that is, unwilling to invest time and energy to inform themselves of the full content and consequences of political issues.⁵⁰ Political

51, no. 4 (2008), pp. 667-81, who have similarly shown that federal aid funding after natural disasters flow faster and fuller to states who actively lobby and support current political authorities.

⁴⁹ There are only a small handful of companies within this industry today and since its development in the late 1970s. They include, but are not necessarily limited to, Corrections Corporation of America (CCA), the GEO Group (formerly Wackenhut Securities), Cornell Companies, and Community Education Centers.

⁵⁰ See Anthony Downs, *An Economic Theory of Democracy* (New York: Harper, 1957).

processes and voting elections can induce *political business cycles*, where appointed decision-makers exploit the value of resources during their tenure only to impose costs on later regimes.⁵¹ Politicians appeal to *median voters* where they support the lowest common denominator of public policy, perhaps in conflict with costs and consequences.⁵² Elections contain *voting paradoxes*, when the number of platforms and candidates lead to deterministic outcomes as a principle of mathematics rather than social preferences.⁵³ Voters also fail to update their false perceptions of political phenomena because they bear a disproportionately small portion of the costs compared to the benefits—they are “rationally irrational.”⁵⁴

In addition, a purely governmental prison system without private corporate providers would be similar to a contracted-out institution, except that they would lack the incentive for operational efficiency motivated by competing agencies. Similar competition may come from other sovereign governments attracting citizens with superior public services.⁵⁵ Finally, one would expect the flaws of political processes explained within the Public Choice literature listed above to be exaggerated when political processes were used as decision-making criteria for the sum total of all prison operations.

How do these concepts operate specifically within the criminal justice system and the practices of incarceration? Benson explains that the incentive structures produced and insulated by government bureaucracy have impeded rather than facilitated the efficient production of security in person and property.⁵⁶ Robert Higgs argues that the war on drugs is fueled by

⁵¹ See Michal Kalecki, “An Essay on the Theory of the Business Cycle,” in *Collected Works of Michal Kalecki*, ed. J. Osiatynski, vol. 1 (New York: Oxford University Press, 1990 [1933]), pp. 65–81; and Patrick Minford and David Peel, “The Political Theory of the Business Cycle,” *European Economic Review* 17, no. 2 (1982), pp. 253–70.

⁵² See Roger Congleton, “The Median Voter Model,” in *The Encyclopedia of Public Choice*, ed. C. K. Rowley and F. Schneider (The Netherlands: Kluwer Academic Press, 2002).

⁵³ See Kenneth Arrow, “Alternative Approaches to the Theory of Choice in Risk-Taking Situations,” *Econometrica* 19, no. 4 (1951), pp. 404–37.

⁵⁴ See Bryan Caplan, *The Myth of the Rational Voter: Why Democracies Choose Bad Policies* (Princeton, NJ: Princeton University Press, 2008).

⁵⁵ See Charles Tiebout, “A Pure Theory of Local Expenditures,” *The Journal of Political Economy* 64, no. 5 (1956), pp. 416–26.

⁵⁶ See Benson, “Crime Control Through Private Enterprise.”

political interests.⁵⁷ Russell Sobel, Matt Ryan, and Joshua Hall show a correlation between criminal case decisions and political cycles.⁵⁸ Specifically on the topic of incarceration, Kenneth Avio summarizes research by Peter Nardulli and Fred Giertz: “Citizens of the local government derive benefits (protection and retribution) from longer sentences, which happen to be specified by local authorities. . . . The tendency to prison overcrowding in the federal part of the system and to underbuilding in the local part follows directly.”⁵⁹ And Daniel D’Amico describes the process of calculating criminal sentencing lengths to suffer from knowledge problems, rent-seeking, capture, and political interests.⁶⁰ Public servants in the prison industry respond to incentives; they act according to subjectively determined profit motives. The expression of these private interests within the political/public sphere have led to outcomes that conflict with many commentators’ perceptions of social welfare.

What systematic tendencies are at play in a purely private prison system? A variety of case studies have recently emerged that offer a partial vision of private criminal law enforcement and incarceration without governmental control. First, David Friedman researched ancient Iceland’s privately operated legal system, where punitive sentences were apparently held in proportionate check by social norms and a price system of restitution.⁶¹ Similarly, classicists Danielle Allen and Virginia Hunter posit that criminal punishments and the practices of incarceration pre-dated formal

⁵⁷ See Robert Higgs, “Lock ‘Em Up!” in Robert Higgs, *Against Leviathan: Government Power and a Free Society* (Oakland, CA: The Independent Institute, 2004), pp. 95-100.

⁵⁸ See Russell Sobel, Matt Ryan, and Joshua Hall, “Electoral Pressures and the Legal System: Friends or Foes?” in *Law Without Romance: Public Choice and the U.S. Legal System*, ed. E. Lopez (Oakland, CA: The Independent Institute, forthcoming).

⁵⁹ Avio, “The Economics of Prisons,” p. 16, summarizing Peter F. Nardulli, “The Misalignment of Penal Responsibilities and State Prison Crises: Costs, Consequences, and Corrective Actions,” *University of Illinois Law Review* 2 (1984), pp. 365-87; and J. Fred Giertz and Peter F. Nardulli, “Prison Overcrowding,” *Public Choice* 46 (1985), pp. 71-78.

⁶⁰ See Daniel J. D’Amico, “The Prisoner’s Dilemma: The Political Economy of Proportionate Punishment,” Ph.D. Dissertation (George Mason University 2008).

⁶¹ See Friedman, “Private Creation and Enforcement of Law.”

governance in ancient Greece.⁶² Stephen Schafer surveys a variety of similar restitution-based criminal justice systems.⁶³ Historian David Rothman argues that many of the ends currently sought by America's incarceration institutions were traditionally accomplished by private individuals and organizations during the colonial periods of American history; most of them avoided the bureaucratic inefficiencies that plague their modern counterparts.⁶⁴ Most recently, scholars are investigating the rational decisions and economic implications of organized crime with surprising results. There appears to be much order among thieves, even in calculating and doling out punishments amid thieving social groups. Diego Gambetta, Maerk Kaminski, Sudhir Venkatesh, and Peter Leeson all expose a structure similar to retaliatory and punitive processes in stateless contexts.⁶⁵ It is the explicit presence of profits, losses, and incentives that interact in order to constrain punishment levels, avoid escalating violence, and maintain social order. Informal social norms and emergent institutional rules in various contexts can maintain a link between the preferences of society, on the one hand, and the functionally constrained level of law enforcements/punishments, on the other.

These case studies are not presented as viable alternatives to the current political provision of criminal law. They are merely presented in order to expose how punishments and criminal incarceration procedures operate

⁶² See, respectively, Danielle Allen, "Imprisonment in Classical Athens," *The Classical Quarterly* 47, no. 1 (1997), pp. 121-35; Danielle Allen, *The World of Prometheus: The Politics of Punishing in Democratic Athens* (Princeton, NJ: Princeton University Press, 2000); and Virginia Hunter, "The Prison of Athens: A Comparative Perspective," *Phoenix* 51 (1997), pp. 296-326.

⁶³ See Stephen Schafer, *Compensation and Restitution to Victims of Crime* (Montclair, NJ: Patterson and Smith, 1970).

⁶⁴ See David Rothman, *Discovery of the Asylum: Social Order and Disorder in the New Republic*, rev. ed. (New York: Aldine Transaction Publishers, 2002).

⁶⁵ See Diego Gambetta, *The Sicilian Mafia: The Business of Private Protection* (Cambridge, MA: Harvard University Press, 1993); Maerk M. Kaminski, *Games Prisoners Play: The Tragicomic Worlds of Polish Prison* (Princeton, NJ: Princeton University Press, 2004); Sudhir Venkatesh, *Off the Books: The Underground Economy of the Urban Poor* (Cambridge, MA: Harvard University Press, 2006); Peter Leeson, "An-arrgh-chy: The Law and Economics of Pirate Organization," *Journal of Political Economy* 115, no. 6 (2007), pp. 1049-94; Peter Leeson, *The Invisible Hook: The Hidden Economics of Pirates* (Princeton, NJ: Princeton University Press, 2009); Peter Leeson, "The Calculus of Piratical Consent: The Myth of the Myth of Social Contract," *Public Choice* (forthcoming); and Peter Leeson "The Invisible Hook: The Law and Economics of Pirate Tolerance," *New York University Journal of Law and Liberty* (forthcoming).

without the oversight of government and are more directly infused with the qualities of profits and private interests. Here in these cases, one notices that profits and private incentives interact to constrain and check power rather than exaggerate it. When comparing the institutions of state-only prisons with contracted-out prisons and purely private prisons, one recognizes that profits and private interests operate in all three contexts; it is the way they operate that makes all the difference. Whereas several commentators have derided private prison firms as unchecked by public oversight, our analysis casts the same accusation against the state, and perhaps in greater magnitude.

4. Conclusion

This article has produced neither a consequentialist nor a deontological case in support of current prison privatization, nor one for a fully free-market criminal justice system, though such arguments have been presented by others.⁶⁶ Instead, we offer a comment on the current moral component of the modern private-prison debate. While several theorists have concluded that public prisons are morally preferable to contracted-out prisons because of the unsavory tendencies for private firms to “profit off of other people's misery,” we contend that the latter may be true but the former does not necessarily follow therefrom.

While discussing Logan as a supporter of prison-privatization, Christie asks, “Why is it that what is so clear to Logan is so utterly unclear to me?”⁶⁷ The answer to Christie is revealed in part by explaining that his perception of human rationality is short-sighted. Individuals act rationally insofar as they are purposeful. They choose means to pursue their subjectively valued ends; this holds true for politicians as well as businessmen. Christie erroneously upholds government agents as behaviorally distinct: “The civil servant represents more than himself, she or he represents the community, that is me. The servant of the state is thus under greater responsibility and control than those who only serve the private firm.”⁶⁸ His description of the incentives and motivations behind government representatives suffers from a *nirvana fallacy*. We can only make accurate comparisons between the market setting and the governmental alternative when we use realistic models for both.

First, the ethical focus of private-prison debates should be re-aligned

⁶⁶ See Barnett, “Pursuing Justice in a Free Society: Part One”; Barnett, “Pursuing Justice in a Free Society: Part Two”; Rothbard, *The Ethics of Liberty*; and Morris Tannehill and Linda Tannehill, *The Market for Liberty* (Lansing, MI: Tannehill, 1970).

⁶⁷ Christie, *Crime Control as Industry*, p. 100, discussing Logan, *Private Prisons*.

⁶⁸ Christie, *Crime Control as Industry*, p. 102.

with Feeley's topical question: "[T]o what extent does privatization expand and transform the state's capacity to punish?"⁶⁹ Second, one must recognize such effects in both the short and long run. And lastly, one must take account of how various institutional structures—purely state, contracted-out, and purely private—may each bear their own unique influences to “expand” or “transform” the fundamental practices of punishment in society.

Many commentators have attempted to identify the moral dilemma of private prisons by attacking the profit motive, but we have presented theory and alluded to evidence gathered elsewhere which suggests that the profit motive transcends the boundary between public and private incarceration. Thus if one is confident in her net assessment that modern punishment institutions suffer a significant degree of immorality, then she must look elsewhere beyond the profit motive for a culprit. Such issues have caused moral philosopher David Boonin to conclude that it is the punishment paradigm itself which is morally flawed.⁷⁰ As Buchanan writes, “good economics is better than no economics . . . [but] applied within a bad or misguided conception of legal process need not promote the structural, procedural changes that may be urgently required.”⁷¹ It may not be the existence of profits and incentives which sully the moral legitimacy of private incarceration practices, but rather, that profits exaggerate the negative moral qualities of the presumed institutional environment already set in place by legislative fiat.

The field of comparative institutional analysis began during the socialist-calculation debates. Within those debates and in its several subsequent applications, comparative analyses have continuously shown consequentialist support for market processes over political decision-making. For example, Friedrich Hayek's closing insights of the socialist-calculation debate describe markets as dynamic and adaptive systems.⁷² Entrepreneurs are continuously inclined to search for and discover innovative profit opportunities. Such incentives are explicitly disrupted when politics replaces markets in certain decision nodes. Thus the costs and unintended

⁶⁹ Malcolm M. Feeley, “The Privatization of Prisons in Historical Perspective,” *Criminal Justice Research Bulletin* 6, no. 2 (1991), p. 109.

⁷⁰ See David Boonin, *The Problem of Punishment* (Cambridge: Cambridge University Press, 2008).

⁷¹ James Buchanan, “Good Economics, Bad Law,” *Virginia Law Review* 60, no. 3 (1974), p. 484.

⁷² See Friedrich A. Hayek, “Socialist Calculation: The Competitive ‘Solution’,” *Economica* 7, no. 26 (1940), pp. 125-49.

consequences of central planning are inherently shortsighted. Christie's presumption that government agents are more attuned to societal preferences than are market agents is a natural conclusion, but it is drawn from a biased and incomplete understanding of social structures. If similar institutional characteristics held for the task of providing incarceration services, they would set a radically different stage for deontological conclusions to begin from.

Take Wright's pointed concern which opened our discussion: "[A]t least in public prisons, when prisoners are raped due to inadequate staffing, [etc.] no one can say prison officials did so to line their own pockets and personally profit from the misery of others."⁷³ Could we not say, instead, that at least in private prisons, when prisoners are raped due to inadequate staffing, etc., no one can say that improvement will never occur so long as the citizenry remains apathetic. At least he will have endured his suffering in a context where his offenders systematically suffer losses and their competitors are systematically rewarded. At least he suffered in a system that appeared to be enjoying a trend of innovation and improvement over time.⁷⁴

⁷³ Wright, "Introduction to Section 4," p. 137.

⁷⁴ We would like to thank Walter Block, who provided helpful comments and criticisms throughout the writing process.

Review Essay: Brian Doherty's *Radicals for Capitalism: A Freewheeling History of the Modern American Libertarian Movement*, Paul Starr's *Freedom's Power: The History and Promise of Liberalism*, and Arthur A. Ekirch, Jr.'s *The Decline of American Liberalism*

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1. Introduction

All three of the books under review are (in some sense) recently published histories of liberalism, describing the transformation of classical liberalism between the eighteenth and twenty-first centuries.¹ Doherty's and Starr's books are somewhat triumphalist in spirit, recounting classical liberalism's evolution into something new and better. Ekirch's book is more pessimistic, describing classical liberalism's devolution into illiberalism. All three are "recently published" only in the academic reviewer's sense, the first two having made a splash in their initial reviewing cycle in 2007, the third being a 2009 re-issue of an old classic. Though already widely discussed, they are, I think, worth a fresh look in comparative perspective for the light they shed on liberalism, and on liberty.

2. Doherty's *Radicals for Capitalism*

Brian Doherty's *Radicals for Capitalism* pretty much delivers what its subtitle says it will: a freewheeling history of the modern American libertarian movement. Freewheeling as it is, Doherty's history has two definite strands, one intellectual, and one institutional.

¹ Brian Doherty, *Radicals for Capitalism: A Freewheeling History of the Modern American Libertarian Movement* (New York: Public Affairs, 2007); Paul Starr, *Freedom's Power: The History and Promise of Liberalism* (New York: Basic Books, 2008); Arthur A. Ekirch, Jr., *The Decline of American Liberalism*, with a new foreword by Robert Higgs (Oakland, CA: Independent Institute, 2009). Starr's book was first published in 2007 with a different subtitle.

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The intellectual history is a story of the development and radicalization of classical liberalism. “The libertarian vision is all in Jefferson,” Doherty writes:

Read your Declaration of Independence: We are all created equal; no one ought to have any special rights and privileges in social relations with other men. We have, inherently, certain rights—to our life, to our freedom, to do what we please in order to find happiness. Government has one purpose: to help us protect those rights. And if it doesn't do that, then it has to go, by any means necessary. (p. 21)

Jefferson was, of course, preceded in this vision by Locke, and exceeded in it by his contemporary Paine. On Doherty's reading, classical liberalism then found further elaboration in the work of John Stuart Mill, Herbert Spencer, and the classical economists, as well as in the polemics and theorizing of the radical American individualists of the mid- to late-nineteenth century (William Lloyd Garrison, Lysander Spooner, William Graham Sumner). By the dawn of the twentieth century, however, and certainly by the end of the First World War, classical liberalism seemed an embarrassing anachronism with little to say of relevance to the problems of its time. The Depression confirmed the sense of failure, and the rise of the New Deal seemed to provide the death blow. It fell to the eccentric writers of the American “Old Right”—Albert Jay Nock, John Flynn, Rose Wilder Lane, Isabel Paterson, H. L. Mencken—to defend (eccentric versions of) classical liberalism in its darkest hour, and to set the stage for what Doherty regards as libertarianism proper.

Though a precise date would be misleading, what Doherty calls “modern American libertarianism” effectively comes into existence with World War II, in part as a more sophisticated continuation of the Old Right's resistance to the New Deal, and in part as a response to the evils of fascism and communism. What characterizes this modern libertarianism is a distinctive radicalization of classical liberalism, reconceived for the complexities of modern life. The central libertarian figures in *Radicals* are Ludwig von Mises, Friedrich Hayek, Ayn Rand, Murray Rothbard, and Milton Friedman. Doherty gives us biographical sketches of each of them, along with detailed accounts of their intellectual development, their contemporary standing in American intellectual life, and the twists and turns on their thought offered by their contemporary followers.

The book's institutional history is a chronicling, sometimes problematically reminiscent of Monty Python's “Life of Brian,” of attempts to put libertarian ideas into practice over the last six or seven decades. It's a dizzying list of names, factions, and squabbles, but Doherty offers a generally well-researched and informative account of the circumstances giving rise to the most important activist efforts, as well as the principals' sources of

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funding, their aims, their actions, the in-fighting that arose during their careers, and the outcomes of their efforts. This aspect of the book seems to have bored non-libertarians to tears,² but is must-reading for anyone sympathetic to libertarianism, and is of value to anyone interested in the history of American political thought, or the sociology of the American right.

There is a lot to like about Doherty's book, and I had a lot of fun reading it. For one thing, Doherty's knowledge of the subject is encyclopedic. He seems to have read almost everything ever written about libertarianism—pro and con, momentous and trivial—and found a way of putting it into the book. At the simplest level, then, the book is an unequalled bibliographical resource, an entertaining chronicle of tidbits and anecdotes, and a useful (if overly detailed) synopsis of the story of the libertarian movement. But there are some deeper contributions here as well.

One of them is epistemological. If we step back from the details of Doherty's narrative, it becomes clear that four ideological disputes have characterized libertarian thought from its very beginnings. A first is whether the libertarian conception of rights leads to limited government or to anarchy. A second is whether the defense of liberty ought to be carried on in narrowly political terms, or whether it requires allegiance to a broader philosophical or cultural outlook. A third issue concerns the relationship between ideological purity and political efficacy. In other words, should libertarians be uncompromising sticklers for principle, or should they be open to compromise, and if so, of what sort? A fourth issue concerns foreign policy. Does the concept of a libertarian foreign policy make sense? If so, what form should it take? How should libertarians think about warfare?

Doherty usefully puts these questions in historical context, and in so doing, shows us the steps by which the contemporary party lines on them first formed and hardened. We thereby get to see the experiences, evidence, and arguments that led people to reach the conclusions they reached, and induced them to formulate the positions to which we're now heir. In some cases, the perspective of distance allows us to look at the old debates dispassionately enough to see who committed which fallacies or errors, and which interlocutors talked past one another or past the issues themselves. Given how often debates about these issues get stuck in a rut, that is a real contribution, and one potentially facilitative of intellectual progress in the here and now.

A second contribution is moral. Though *Radicals* devotes inordinate space to the “freak show” elements of libertarianism, the book also showcases men and women who, whatever their flaws, deserve more moral credit than they ever get from mainstream commentators. I was particularly impressed by

² See, e. g., David Leonhardt's review, “Free for All,” *The New York Times*, April 1, 2007.

the tenacity, acuity, and courage of nine individuals discussed in *Radicals*: Ludwig von Mises, Isabel Paterson, Leonard Read, William Mullendore, Ayn Rand, Thomas Szasz, Richard Fink, Paul Jacob, and John Mackey. All nine took positions far outside of the mainstream of American political thought and practice, paying the price for it in the way of ridicule, intimidation, and marginalization, but all nine had the foresight to stick to their guns—to their benefit and ours.³ In reading *Radicals*, it occurred to me that I had myself subconsciously dismissed Thomas Szasz’s views on the basis of totally unreflective prejudices; Doherty’s brief account of Szasz’s thought convinced me that I was wrong. Multiply my anti-Szasz dogmatism by the millions and you get some attenuated sense of the intellectual inertia Doherty’s libertarians have had to confront.

A third contribution is historical: *Radicals* draws salutary attention to now-forgotten episodes of American history that ought more assiduously to be remembered. Who today remembers or wants to talk about Hollywood’s mid-century apologetics for Stalin (pp. 187-89), the depredations of the Buchanan Commission (pp. 195-98), the merits and contemporary relevance of the Bricker Amendment (p. 258), the libertarian role in the abolition of conscription (p. 303), the free-speech implications of *Buckley vs. Valeo* (p. 398), or the track record of urban renewal (p. 448)? Centrist liberals, in particular, might want to check some of their premises on these issues, having been on the wrong side of history in every one of these cases.

A fourth and somewhat unwitting contribution is the flip side of the previous two. Though he makes less of it than he might have, Doherty also shows us that the libertarian movement has had a dark side from its very beginnings. It is hard not to cringe at libertarian flirtations with neo-Confederate versions of states’ rights, or at their morally equivalent flirtations with the New Left. Milton Friedman’s apparent co-optation by the Pinochet regime still seems problematic, as does the embarrassing weakness of Ronald Reagan’s dealings with such right-wing regimes as Zia-ul-Haq’s Pakistan and *apartheid* South Africa (unmentioned by Doherty in the generally admiring pages he devotes to Reagan).⁴ Murray Rothbard provides decades’ worth of moral insanity on his own, with his praise for Joseph McCarthy and Strom Thurmond in one decade and for Black Power in the next (pp. 245, 254-56, 341); his apologetics for the Soviet Union (p. 383); his rejection of the rights of children (p. 560); his radical re-definition of the concept of assault (p. 559);

³ My use of the past perfect is a bit misleading here, since Mackey’s is a current case with contemporary consequences. See the interview with Mackey by Matt Welch and Nick Gillespie in “Whole Foods Health Care,” *Reason* (January 2010).

⁴ Doherty elsewhere discusses Friedman and Pinochet; see “The Economist and the Dictator,” *Reason Online* (December 15, 2006).

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and his insouciant avowal of the thesis that in the absence of plaintiffs against them, violent criminals ought to be allowed to go unprosecuted for their crimes (pp. 559-60). Over and above this one can't help noticing the general decadence and eccentricity of the libertarian movement as a whole. I give Doherty credit for presenting the uglier sides of the movement's history, but can't agree with the somewhat cavalier way in which he presents it.⁵ After a while the malfeasances cease to be amusing, and start to get scary.

Though I found Doherty's book likeable and informative, I have to confess to some philosophical misgivings, some of them at odds with his project as such. In a much derided but little discussed essay (badly misinterpreted by Doherty, pp. 438-40), the Objectivist writer Peter Schwartz once notoriously described libertarianism as a "perversion of liberty."⁶ Taking Rothbard's libertarianism as paradigmatic of libertarianism as such, Schwartz argued that since Rothbard's libertarianism was nihilistic, nihilism was the defining essence of libertarianism. Canvassing libertarian writing of the 1970s and 1980s, Schwartz found what he took to be ample confirmatory evidence for his thesis, and in consequence, anathematized libertarianism for all time.

I don't entirely agree with Schwartz, but I found it useful to read his essay while reading Doherty's book, if only because doing so brought out Doherty's tendency to go to the opposite extreme. Where Schwartz insisted that libertarianism was a single unified doctrine with an essence identifiable via the writings of a single author, Doherty seems content with the thought that libertarianism is whatever libertarians say it is (p. 19). This cheerfully nominalistic attitude may come across as pleasingly inclusive to some—no one is allowed the final say about the identity of libertarianism, not even its chief historian⁷—but it leads to some problems.

One widely noted problem is that Doherty has given us a 741-page history that steadfastly refuses to distinguish the significant from the insignificant. This leads to tediously long discussions of ephemeral topics, and problematically brief discussions of important ones. Should a book on libertarianism really devote more space to the antics of Karl Hess than to the combined scholarly and analytic efforts of the Institute for Humane Studies

⁵ Leonhardt makes the same criticism in "Free for All," but ignores the second and third contributions I note above.

⁶ Peter Schwartz, "Libertarianism: The Perversion of Liberty," in Ayn Rand, *The Voice of Reason: Essays in Objectivist Thought*, ed. Leonard Peikoff (New York: New American Library, 1988), pp. 311-33.

⁷ Actually, this is a bit misleading, as Doherty *agrees* with Schwartz in regarding Rothbard as the paradigmatic libertarian (p. 13), and literally gives Rothbard the book's last word (p. 619).

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and Mercatus Center? Is Jerome Tuccille's *It Usually Begins With Ayn Rand* (five index entries) really more important than David Kelley's *Truth and Toleration* (none)? Does any serious person have reason to care about the crackpot musings of Andrew Joseph Galambos (pp. 323-26, 401, 474), the Discordian political "theorizing" of Kerry Thornley (pp. 265, 328, 522), or the political fortunes of Howard Stern (pp. 516-17)?

At a deeper level, the failure to define "libertarianism" raises a question that Doherty doesn't address: How can one write a history of an ideological movement without a precise sense of its identity? In lieu of an answer to that question, Doherty uncritically accepts a version of what is perhaps the only doctrine shared in common by Murray Rothbard and John Rawls: the thesis of the overlapping consensus. The idea here is that exponents of divergent and incommensurable moral perspectives can achieve a consensus on political questions—on liberty, say—by focusing on the agreements that they happen to have despite the disagreements that divide them. "Citizens have conflicting religious, philosophical, and moral views," Rawls writes, "and so they affirm [a common] political conception from within different and opposing comprehensive doctrines, and so, in part at least, for different reasons."⁸ Rothbard puts the point this way:

As a political theory, Libertarianism is a coalition of adherents from all manner of philosophic (or nonphilosophic) positions: including emotivism, hedonism, Kantian *a priorism*, and many others. My own position grounds Libertarianism on a natural rights theory embedded in a wider system of Aristotelian-Lockean natural law and a realist ontology and metaphysics. But although those of us taking this position believe that only it provides a satisfactory groundwork and basis for individual liberty, this is an argument within the Libertarian camp about the proper basis and ground of Libertarianism rather than about the doctrine itself.⁹

Both Rawls and Rothbard assume that the content of a doctrine can be detached from its justification. If I endorse liberty on, say, Aristotelian-

⁸ John Rawls, *Justice as Fairness: A Restatement*, ed. Erin Kelly (Cambridge, MA: Belknap Press, 2001), p. 32. See also John Rawls, "The Idea of an Overlapping Consensus," in *Collected Papers*, ed. Samuel Freeman (Cambridge, MA: Harvard University Press, 2001), ch. 20; and John Rawls, "The Idea of an Overlapping Consensus," in John Rawls, *Political Liberalism* (New York: Columbia University Press, 1996), Lecture 4.

⁹ Murray Rothbard, "Frank S. Meyer: The Fusionist as Libertarian Manqué," *Modern Age* 25, no. 4 (Fall 1981), p. 355.

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Lockean grounds and you endorse it on, say, emotivist grounds, we need not worry about the justificatory questions that divide us; we ought instead to focus on the substantive agreement that unites us. We can (on this view) still agree in endorsing liberty while disagreeing about its justification.

Unfortunately, this “agreement” is an illusion. If you are an emotivist and I am an Aristotelian, we don’t just disagree about the “proper basis” of a doctrine on which we otherwise agree. We disagree about the relationship between doctrines and reality as such. In that case, we disagree about the *reality* denoted by the term “liberty.” If so, our supposed “agreement” about liberty conceals fundamental disagreement about it, and collapses into purely verbal formulas to which we give incompatible meanings. And what is true of the disagreement between Aristotelians and emotivists is, I suspect, also true of the other normative disagreements that divide “libertarians.” Utilitarians, Kantians, Hayekians, and Objectivists may all profess a love of “liberty,” but they surely do not mean the same thing by it.

This problem has stark implications for Doherty’s book. The five libertarians at the heart of *Radicals* adopt wildly divergent, incompatible positions on questions of epistemology, ethics, and politics. So what exactly do all five have in common that entitles all of them to be called “libertarians”? Presumably, they share a common commitment to liberty. But is it the same commitment? Is it a commitment to the same thing? Doherty writes as though these questions didn’t much matter. The five writers’ theoretical commitments may differ, he implies, but if so, surely the five of them can achieve some approximation to an overlapping consensus that justifies our calling them “libertarians” despite that.

Can they? To answer that question, we’d need to compare what each author says about liberty with the comparable claims of the others. And that brings us to a strange anomaly in *Radicals*. While it spends hundreds of pages discussing the views of its protagonists, it devotes surprisingly little space to their claims about the nature of liberty. The reader could get through the book without ever learning how Mises, Rand, Rothbard, and Friedman defined “liberty,” what they excluded from those definitions and why, and how each author’s definition compares with those of the others.¹⁰ This is only partly Doherty’s fault, however, for the fact is, Hayek aside, none of the authors have *themselves* offered sustained discussions of the nature of liberty. It’s an amazing fact that the *nature of liberty* is one of the least-discussed topics in what libertarians like to call “the literature of liberty.” But if so, the assumption that all five of Doherty’s protagonists must be agreeing with one

¹⁰ Hayek is a partial exception (pp. 219-22, 306), but Hayek is the least libertarian of the book’s five protagonists.

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another about liberty is unjustified—particularly so if one of them, Rand, explicitly insisted that she was disagreeing with the others.

Mention of Rand brings me to my final complaint about Doherty's book, namely, his treatment of Rand's Objectivism. I give Doherty credit for his praise of Rand, and for the parts of his discussion that do genuinely convey what's important about her work. But on the whole, Doherty's discussion of Rand is chatty and superficial in ways that contrast conspicuously with the substantive and issues-based approach he takes in his discussions of Rothbard, Mises, Hayek, Friedman, and others. Too much of his discussion of Rand consists of gossip and rumor-mongering, too little is directly focused on her ideas, and where he does focus on the ideas, he is too quick to dismiss claims that he has scarcely bothered to explain.¹¹ No serious

¹¹ Though Doherty is by turns respectful of and snarky about Rand, Rand-hating reviewers have had a field day with his book, exploiting the gossip in it to generate—or confabulate—mythologies expressing their prejudices. A typical example is Jonah Goldberg's review: "In some cases, as with the chapter dealing with Rand, one could argue that Doherty lets the damning facts speak for themselves" ("Live Free or Else!" *National Review* [May 24, 2007]). Unfortunately, the "facts" in Doherty's account don't speak for themselves, chiefly because they lack a clear title to being factual. Much of Doherty's account attempts to recreate the atmosphere of the early Objectivist movement, a daunting task for an outsider under the best of circumstances, but close to impossible under current circumstances. Doherty relies for much of his account on the testimony of disgruntled insiders, some named (Barbara and Nathaniel Branden, Robert Hessen, Joan Kennedy Taylor, Murray Rothbard) and some anonymous, but doesn't seem to have interviewed any of the Rand-positive people from the same milieu. Without even disputing the disgruntled insiders' claims, it ought to be obvious that one cannot recreate the atmosphere of highly personal, heated, and controversial events five decades in the past without interviewing people who have different recollections of the same events. No such testimony appears in Doherty's book, who seems to regard it as axiomatic that the early Objectivist movement is whatever his interviewees say about it. I see no reason to accept this assumption.

A different sort of example comes by way of Kay Hymowitz's review of *Radicals* in *Commentary*, according to which "Ayn Rand was predictably wary of kinship ties and, like radical feminists, saw the family as a soul killing prison" ("Freedom Fetishists," *Commentary* [September 2007]). As common experience suggests, some families can be soul-killing prisons, but nowhere does Rand suggest that the family as such is one. I asked Hymowitz by email for the textual evidence in Rand's works for her claim about Rand; she had none. The source for her claim appears to be an article by the libertarian journalist Cathy Young, which asserts: "In her 1964 *Playboy* interview, Rand flatly declared that it was 'immoral' to place family ties and friendship over productive work; in her fiction, family life is depicted as a stifling, soul-killing, mainly feminine swamp" ("Ayn Rand at 100," *Reason* [March 2005]). The similarities of wording suggest that Hymowitz has merely appropriated and re-written Young's claim, passing it off as her own. In any case, both Young's and Hymowitz's claims are misrepresentations. For one thing, Rand's fictional depiction of

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Objectivist would regard his account as fair or accurate, and no one previously unfamiliar with Objectivism could come, by Doherty's account, to see what it is that has convinced anyone of its truth. I grant that the task of writing a primer on Objectivism is a difficult one—there really is no better guide to Objectivism than Ayn Rand—but the task is inevitably overcomplicated by a book, like Doherty's, that so systematically privileges gossip over doctrine, and so quickly brushes aside the very topics that Rand regarded as fundamental.

Oddly, then, though I liked *Radicals*, I often found it a frustrating book to read. My hunch is that the book will remain of enduring interest to libertarians and their fellow travelers, but have little impact outside of that relatively closed circle. For non-libertarians, *Radicals* will likely confirm their sense that libertarianism is an interesting anomaly on the American political scene—intriguingly consistent in the pursuit of liberty, but ultimately too wacky to be taken seriously.

3. Starr's *Freedom's Power*

Paul Starr's *Freedom's Power* (hereafter *FP*) is at once remarkably like and radically unlike *Radicals*. It begins, like *Radicals*, with an appeal to the preamble of the Declaration of Independence and with the Lockean-Jeffersonian vision that animates it:

Liberalism is deeply rooted in American soil, so much so, in fact, that in the years after World War II many historians and social scientists regarded the liberal project and the American civic creed as more or less identical. The two share the same aspirations. The proposition that each of us has a right to "life, liberty, and the pursuit of happiness" remains as good a definition as anyone has ever come up with of liberalism's first principle and America's historic promise. For some time, however, contemporary liberalism has been under political siege in the United States, and liberal ideas have lost the high ground they once commanded in moral argument and public life. (p. 1)

Given this, Starr's aim in *FP* is to restore to liberals what he claims that they've lost. Like *Radicals*, *FP* is an intellectual and institutional history—"a

families cannot be equated with her considered view of the family as such. Second, both Young and Hymowitz ignore Rand's positive remarks on parenting in the very interview to which Young alludes. Third, Young's claims about Rand's fiction are themselves highly disputable: if couples count as families (and why shouldn't they?), Rand's depictions of the family are highly *positive*. The failures of research, reading comprehension, and intellectual honesty involved here strike me as downright pathetic.

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historical interpretation of the liberal project” (p. ix)—and like *Radicals*, the story it tells is one about the interface of ideas and institutions in recent Anglo-American history (though with far greater attention to England than Doherty attempts). Like Doherty, Starr begins his history by discussing the classical liberals, and traces the evolution of their doctrines across the nineteenth and twentieth centuries with a view to showing how those ideas were updated in theory and practice to better fit the circumstances and moral conceptions of modern life. And like *Radicals*, *FP* is committed to the thesis that political history is in some sense structured by intellectual history without being literally reducible to it; contrary to both Marxist determinism and Machiavellian cynicism, we understand politics best in Aristotelian fashion by studying the interface of normative principles and contingent events as embodied by constitutions (pp. 29-32).

But *FP* is, for all those similarities, a strikingly different sort of book than *Radicals*, and to my mind a much better one. Some of this is a function of its purely formal virtues. The book is written with erudition and clarity, and contrary to some of its critics, does a very good job at integrating the theoretical and historical parts of the story it tells. Unlike *Radicals*, it is an intensely serious book, written with a refreshing moral passion. It’s also ruthlessly single-minded. Unlike Doherty, Starr wastes no space on the merely amusing or frivolous; he has a good sense of the difference between the essential and the dispensable. Perhaps the explanation for all of this is that, unlike *Radicals*, *FP* is a book with a well-defined doctrinal agenda, and a thesis formulated to serve it; the book is, Starr tells us, “a defense of the modern and egalitarian form” of liberalism, and a “rebuttal” of its conservative critics (pp. ix, x). (Starr refers to this egalitarian form of liberalism as “democratic liberalism.”) On this view, we might say, modern history has been an experiment with a single central finding: Where “democratic liberalism” has flourished, so have freedom, justice, and prosperity; where that liberalism has been thwarted, those values have suffered. Whether one agrees or disagrees, one can’t help but admire the form and method of the argument.

What then is “democratic liberalism”? Ironically, despite Starr’s own call for “clarity about what liberalism stands for” (p. 12), he is no better at defining it than Doherty was at defining libertarianism. “Liberalism,” he tells us, “is notoriously difficult to define” (p. 1); echoing the “overlapping consensus” thesis discussed above, he canvasses a few definitions and concludes that “[l]iberals are defined more by their shared political principles than by agreement on the ultimate grounds on which those principles rest” (pp. 4, 237-38 n. 1). I’ve already explained why I think this gambit fails, and to the extent that Starr relies on it, his doing so muddies the waters. But he’s not *that* committed to it; contrary to his official view, his liberalism is defined

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both by a set of shared principles and by an implicit conception of the grounds for them.

Starr's conception of liberalism is rich and complicated, but I think it can be reduced to four central theses, each harking back in some way to the sort of liberalism historically developed by L. T. Hobhouse, and associated today with the work of Ronald Dworkin, William Galston, and Amy Gutmann.¹² A first thesis asserts that liberalism presupposes an objective conception of well-being and the virtues:

A liberal government, like any other, must operate on the basis of substantive values, not just in the criminal law but in every phase of its activities. . . . There are excellences and virtues that a liberal society must promote if it is to survive. Far from being silent on the good, liberalism is intensely concerned with it, though that concern is not always fully expressed or conveyed through the state. (pp. 176-77)

A second thesis asserts a commitment to an egalitarian conception of equal liberty as a necessary condition of well-being:

Liberalism regards the well-being of the least well-off as a central criterion for a just society, and it seeks to provide individuals with some degree of protection against risks beyond their control, but it accepts inequalities insofar as they are to everyone's long-run advantage and therefore aims for sustainable growth with widely shared gains. (pp. 148-49)

A third thesis, which supplies the book's title, holds that the promotion of equal freedom requires the sort of power that can only be supplied by a strong, albeit constitutionally limited, state. And a fourth thesis extends the preceding three into international affairs: A liberal state ought, compatibly with the requirements of equal freedom, to advance liberal values abroad. Sometimes that will require warfare in defense of liberty, but more often it will require the projection of so-called soft power and multilateral diplomacy.

The package certainly conveys the impression of overall coherence, and for the most part, Starr manages his case well. It's a tribute to *FP* that its conservative critics have done little damage to the book's main thesis. Indeed, most of them have been astonishingly concessionary, and equally unaware of what they've been conceding. As Wilfrid McClay puts the point in a putatively critical review in *Commentary*, "One of the oddest features of *Freedom's Power* is that almost any conservative can read large chunks of it

¹² See L. T. Hobhouse, *Liberalism* (London: Oxford University Press, 1964 [1911]).

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and find little substance to disagree with.”¹³ If that’s so, it follows that the specifically conservative criticism of the book has been pretty insubstantial. But no self-respecting libertarian or Objectivist could get past p. 2 of the book without raising an eyebrow, or past p. 4 without settling in for a fight.

An initial weakness of *FP* is its virtual imprisonment by the conventional dichotomy between liberalism and conservatism. Though the book begins with a discussion of classical liberalism, Starr uses “classical liberal” throughout the book narrowly to denote the views held by the original classical liberals (e.g., Locke, Mill, the American Founders, etc.), freighting the term with all of the racist, sexist, and otherwise reactionary baggage associated with the most idiosyncratic features of their thought (pp. 79-82, 88-95, 98-99). He regards “modern democratic liberalism” as the sole heir to classical liberalism, giving it exclusive credit for its reform, but doesn’t allow for the possibility of a non-conservative, non-socialist, and non-democratic liberal aspirant to the same inheritance. The four references to libertarianism in the book all assimilate libertarianism to conservatism (pp. 20, 85, 123, 164), and the various references to “laissez faire” in *FP* merely repeat Hobhouse’s critique of the Manchester School.¹⁴ The book makes passing reference to Hayek and Friedman, but none at all to Mises, Rand, or Nozick. Dialectically speaking, then, Starr makes life relatively easy for himself: in assimilating libertarianism to conservatism and ignoring Objectivism altogether, he ignores the most fundamental challenges to his views. But there are challenges to be made.

Consider Starr’s interpretation of the principle of equal liberty. As we’ve seen, his view entails that the relatively disadvantaged have a claim on the labor and property of the advantaged to be advanced by the coercive powers of the state. A common criticism of this view, unacknowledged by Starr, asserts that it treats the advantaged as mere means to the welfare of the disadvantaged:

Seizing the results of someone’s labor is equivalent to seizing hours from him and directing him to carry on various activities. If people force you to do certain work, or unrewarded work, for a certain period of time, they decide what you are to do and what purposes your work is to serve apart from your decisions. This process

¹³ Wilfrid McClay, “The Right Left?” *Commentary* (May 2007). See also Peter Berkowitz, “Proudly Liberal,” *Policy Review* (April-May 2007). For a more contentious but still concessionary review, see Fred Siegel, “Blinded by the Left,” *Democracy: A Journal of Ideas* (Summer 2007). Starr responds at length to his critics on the book’s website, <http://www.freedomspower.com>.

¹⁴ Hobhouse, *Liberalism*, ch. 4.

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whereby they take this decision from you makes them a *part-owner* of you; it gives them a property right in you. . . . [Such] principles involve a shift from the classical liberals' notion of self-ownership to a notion of (partial) property rights in *other* people.¹⁵

Richard Arneson, among others, concedes this point in his defense of redistribution, and the late G. A. Cohen devoted a good part of his career to the task of rebutting it.¹⁶ Starr ignores it, and yet to a remarkable degree, he regards the promotion of equal freedom as the progressive appropriation of persons by persons,¹⁷ a claim that he justifies with the mantra-like assertion that "property has rights but brings obligations." He seems to think it entirely obvious that what A gains by partially appropriating B counts as a net gain for both of them:

To paraphrase Hobhouse, it is just to tax B to help A because when the good of all concerned is considered, among whom B is one, there will be a net gain in the arrangement as compared with any alternative. (p. 102; see also pp. 18, 101, 103, 203)

It's not as obvious as Starr thinks. For starters, it's hardly obvious that B benefits from being appropriated by A. If not, there's no gain in the arrangement for B, or for anyone circumstanced like B. Neither is it obvious that it's *just* to appropriate persons. If not, then the proceeds of such an appropriation are ill-gotten gains. Now suppose (as Tara Smith argues)¹⁸ that ill-gotten gains are *not* beneficial to those who try to get them. In that case, there's no gain for A, either, or for those circumstanced like A. If the proposed taxation doesn't benefit A-type or B-type people, it is unclear whom it does benefit, or why there are no better alternatives to it. Where, then, is Starr's "net gain"? Contrary to Starr, economic growth and political meliorism

¹⁵ Robert Nozick, *Anarchy, State, and Utopia* (New York: Basic Books, 1974), p. 172.

¹⁶ See Richard Arneson, "Property Rights in Persons," *Social Philosophy and Policy* 9, no. 1 (1992), pp. 201-30; G. A. Cohen, *Self-Ownership, Freedom, and Equality* (Cambridge: Cambridge University Press, 1995). For a contemporary libertarian discussion, see Tom Palmer, "G. A. Cohen on Self-Ownership, Property, and Equality," in *Realizing Freedom: Libertarian Theory, History, and Practice* (Washington: Cato Institute, 2009), ch. 6.

¹⁷ See *FP*, pp. 4, 76, 81, 87, 88, 93, 94-95, 100-6, 120, 129, 139-50, 165-75, 197, 198, 200, 221, 228-30, 234.

¹⁸ Tara Smith, *Viable Values: A Study of Life as the Root and Reward of Morality* (Lanham, MD: Rowman and Littlefield, 2000), pp. 167-74.

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are not obviously beneficial if gotten by methods that make property of persons—any more so than decreases in the crime rate would be self-evident progress if achieved by violations of procedural justice.

The preceding point about self-ownership obliges us to take a closer look at what Starr really means by “equal liberty.” Like Doherty, Starr offers no definition or analysis of liberty, but it’s useful to reflect on what he does say by way of an influential definition in an account close to his. Consider Dworkin’s view. According to Dworkin, “*liberty is the right to do what you want with the resources that are rightfully yours.*”¹⁹ If we apply this to Starr’s account, it follows that the advantaged suffer a drastic diminution of liberty: none of us is *ourselves* “rightfully ours” qua advantaged—at least not fully so, since others are free to appropriate us. We thus lack the liberty to do what we want with ourselves, and what we want with our labor, actions, or property. The disadvantaged, by contrast, are free to receive and use the proceeds of coercive redistribution—free, at any rate, unless they become advantaged. Then *they* become candidates for appropriation by those currently disadvantaged, and the cycle continues.

Starr writes as though each successive intensification of coercive redistribution—each attempt to take more from the advantaged and give more to the disadvantaged (or to more of the disadvantaged)—made everyone more free. Yet he ignores the fact that each such redistribution reduces what advantaged agents can regard as rightfully theirs. Crudely put, as the disadvantaged get stuff from the advantaged, the advantaged lose options for independent action; as the disadvantaged get enough stuff to count as advantaged, they too start to lose options for action so that the (currently) disadvantaged can get more stuff. One could only regard this as a net gain for freedom if one ignored the conflict between two incompatible kinds of freedom: (a) the freedom to act on those options you have when you fully own yourself, and (b) the freedom you have to act on those options you have when no one fully owns himself, but almost everyone owns some part of someone else.

Starr seems to suggest that the conflict between (a) and (b) can be averted by regarding “equality” and “liberty” as correlatives and interpreting the principle of equal liberty so that it integrates both without loss to either.²⁰

¹⁹ Ronald Dworkin, *Is Democracy Possible Here? Principles for a New Political Debate* (Princeton, NJ: Princeton University Press, 2006), p. 69. Starr favorably cites Dworkin’s book in a somewhat different context (p. 238 n. 2). Unlike Dworkin, I use “freedom” and “liberty” interchangeably throughout to refer to what Dworkin calls “liberty.”

²⁰ *FP*, pp. 86, 87, 99, 118, 140, 197, 200. See also Starr’s response to the review by *The Economist* on the book’s website (April 27, 2008).

But that claim is a red herring. Let's grant that equality and liberty *are* correlatives, and that a defensible principle of equal liberty integrates them. The question is whether Starr has articulated such a principle. He has not. What he has done is to endorse something like (a) in contexts involving speech, sex, religious observance, and scientific inquiry, and something like (b) for economic life. He then implicitly regards the conjunction of (a) and (b) as a proxy for an interpretation of equal liberty. But (a) flatly *contradicts* (b). What needs an explanation is why (a) governs a few ad hoc slices of life, while (b) governs the rest. In the absence of an explanation, Starr cannot claim to have reconciled equality and liberty. What he's done is to sacrifice liberty in sense (a) to liberty in sense (b). He himself notices this on one isolated occasion (p. 103), but makes nothing of it. In fact, the concession signals a fundamental defect in his treatment of equal liberty.

This may all seem very abstract, but its consequences in liberal jurisprudence and policy have been quite vivid. Democratic liberalism claims that we have rights to receive goods, but also claims that we lack a comparable right to produce or keep them. The result is not an expansion of freedom, as Starr claims, but a kind of political schizophrenia. Thus democratic liberalism tells us that we have the "right to a decent home," but also tells us that no one has a right to keep the home he owns: a chain of liberal jurisprudence from *Parker vs. Berman* (1954) to *Kelo vs. New London* (2005) has legitimated the forcible expropriation and destruction of hundreds of thousands of homes under urban renewal, and ultimately led in jurisprudence to the outright nullification of private property rights.²¹ Democratic liberalism gives us the right to "fair competition" in business contexts where economies of scale might concentrate wealth, but it also imposes on us a legal apparatus that routinely applies vague and retroactive laws, that reverses the presumption of innocence in criminal trials, and that ascribes criminal liability to persons who play no causal role in bringing about the crimes for which they stand accused.²² In one breath democratic liberalism

²¹ This last claim may sound "extreme" to some, but the case for it is cogently laid out in Justice O'Connor's dissent in the *Kelo vs. New London* decision (2005). On urban renewal, see Martin Anderson's classic *The Federal Bulldozer* (Cambridge, MA: MIT Press, 1964). See also Richard Epstein, *Takings: Private Property and the Power of Eminent Domain* (Cambridge, MA: Harvard University Press, 1985); Richard Epstein, *How Progressives Rewrote the Constitution* (Washington, DC: Cato Institute, 2006); and James V. DeLong, *Property Matters: How Property Rights Are Under Assault—And Why You Should Care* (New York: Free Press, 1997).

²² On retroactivity in antitrust law, see Ayn Rand, "Antitrust: The Rule of Unreason," in *The Voice of Reason*, pp. 254-59. The other points are made in John Hasnas, *Trapped: When Acting Ethically Is Against the Law* (Washington, DC: Cato Institute, 2006), ch. 4. Thanks to Carrie-Ann Biondi for bringing Hasnas's book to my attention.

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promises us “security” against risk via a “compact between generations”; in the next, it confesses that the “security” it offers is actuarially unsound, hence impossible to deliver.²³ Starr calls this the raising of “the equilibrium of power and liberty to a higher level” (p. 159). Considering his demotion of property rights to relative insignificance (p. 10), his conception of those rights as almost infinitely malleable (p. 71), and his deference to democratic majorities in economic matters (p. 162), I’m more inclined to call it a local train to totalitarianism.²⁴

I mentioned above that Starr takes the principle of equal liberty to require promotion by a strong, though constitutionally limited, state. One might think that despite the preceding criticisms, the commitment to constitutionalism ought to put to rest worries about totalitarianism. Indeed, Starr repeatedly insists that “freedom’s power” can only be realized if the state is limited in its functions. He spends a chapter criticizing socialism, giving democratic liberals the lion’s share of the credit for seeing its errors and correcting them.²⁵ He has praise for deregulation as well, giving democratic liberals credit for coming up with the idea and successfully putting it into practice (p. 158).

But despite the frequent allusions to “limits” on state power (which I tracked through the text), I didn’t find a single passage or combination of them that straightforwardly posed or answered the essential question: What is the function of the state, and what are its limits? Starr’s discussion of this topic is, with certain ad hoc exceptions (speech, sex, religion, science), vague to the point of vacuity or narrow to the point of irrelevance. The closest he comes to a view about the state’s *function* is a passage that suggests that the primary purpose of social policy is redistribution (p. 197)—but this articulates a power, not a limit. The closest he comes to a discussion of *limits* is a brief passage on the separation of powers, but this is a purely procedural principle that sets no substantive limits on state power (pp. 59-60). Despite this, Starr

²³ From “What Social Security Means To You,” Form SSA-7005-SM-SI (01/10), Social Security Administration.

²⁴ I borrow this metaphor from Ayn Rand’s title, “Censorship: Local and Express,” in Ayn Rand, *Philosophy: Who Needs It?* (New York: Signet, 1982). For further discussion, see Timothy Sandefur’s review of *The Dirty Dozen* in this issue.

²⁵ I found this claim more than a little puzzling. “The consequences of tightly coupling economics and politics,” Starr writes of socialist regimes, “were not immediately apparent” (p. 187). Not apparent to whom? Mises’s first discussion of the “consequences of tightly coupling economics and politics” dates to 1920, Rand’s to 1936. Both writers were ridiculed for decades by left-liberals for drawing undesired attention to the topic.

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insists that constitutional liberalism “imposed limits on state power” (p. 53): though the American constitution “magnified the powers of the state,” it also “clarified and codified the limitation of those powers” (p. 48). Ad hoc exceptions aside, I found no such clarification or codification in Starr’s discussion. He cites with apparent approval Alexander Hamilton’s claim from *Federalist* #31 that there are “no fixed limits” on the government’s power of taxation (p. 48), and asserts soon after that the “Constitution’s endowment of powers created an elastic state” without limits as such (p. 51).²⁶ Though Starr praises “the Madisonian view . . . that the Union ought to guarantee liberty all the way down” (p. 51), “all the way down” really seems to mean “part of the way down”: property rights get low priority, even when written into the Constitution and endorsed by Madison himself (p. 10).²⁷

This open-ended account of state power has problematic ramifications for Starr’s discussion of foreign policy, as well. Starr calls his conception of foreign policy “liberal internationalism,” broadly defined as the rejection of pacifism and imperialism, and the promotion in international contexts of human rights, free trade, and the defense of liberal governments against anti-liberal threats to them (pp. 112-15, 127-38). Fleshing this out a bit, he endorses Woodrow Wilson’s conception of national self-determination as expressed in the Fourteen Points (p. 115); “containment” as formulated by George Kennan and implemented by the Truman Doctrine and Marshall Plan (pp. 130-38), and “multilateralism” of the sort associated with the League of Nations and the U.N., understood less in terms of the actual working of these institutions than with the ideals motivating their creation (p. 116).

Some of what Starr says here is reasonable. He is right in a broad way about what we should want to achieve in our foreign policy, and critical both of the excessive militarism of the right and the appeasement-propensities of the left. But little of what he says about this is unique to democratic liberalism as he conceives of it; libertarians have been defending views like his for decades. On the other hand, the differences between liberal and libertarian/Objectivist internationalisms are perhaps as instructive as the similarities, especially with respect to warfare. The Objectivist position holds that warfare is justified exclusively as a matter of self-defense. Force-initiations by external powers demand a retaliatory response, but such responses are themselves constrained by the limited character of government. A nation’s military policy exists to protect its citizens’ rights; it is not a blank

²⁶ Actually, *Federalist* #31 goes much further than Starr indicates. In it, Hamilton asserts that questions about the scope of government are beyond the province of reason, a fact he inexplicably takes to imply that government has unlimited scope. Hamilton’s claims are profitably contrasted with Locke’s in his *Second Treatise*, ch. 9.

²⁷ For Madison’s views on property, see his 1792 essay, “Of Property,” available online.

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check for foreign adventures, whether of the humanitarian-rescue or nation-building varieties (e.g., Somalia, Bosnia, Kosovo, Darfur, etc.).

Though I found his discussion rather vague, I got the distinct sense that Starr would find the Objectivist position overly constraining (p. 217). On his view, the function of the state is as open-ended in foreign affairs as it is in domestic affairs. Ironically, though he castigates conservatives for their unilateralist hyperactivity, his brand of multilateralism is from this Objectivist perspective equally hyperactive (pp. 206-17). On the Objectivist view, there are definite limits to what the state can permissibly do in foreign affairs. Given this, we need an iron-clad guarantee that *our* Constitution (and our interpretation of it) are the last word when it comes to our blood, treasure, prestige, or carbon footprints—hence the attractions of unilateralism. By contrast, since Starr sees no need for strict limits on state power, he has little problem with the open-ended obligations foisted on us by multilateralism (p. 210). But it is hardly obvious that multilateralism so construed promotes freedom better than unilateralism.²⁸

I've been critical here of *FP*, but I should emphasize that my criticisms of the book do not contradict my praise for it. I've focused my criticisms on the basic premises of Starr's argument, but granting those premises, he has fashioned a powerful and important case for his brand of liberalism. I'm reminded of a claim of Ayn Rand's about the New Dealers that Starr celebrates in *FP*: "I disagreed with everything they said, but I would have fought to the death for the *method* by which they said it: for an *intellectual* approach to political problems."²⁹ Starr's book deserves the same compliment. Any intellectually robust movement needs a book like this, and offhand I can't think of a comparable book by a contemporary libertarian or Objectivist. Anyone wishing to write such a book would do well to study the virtues and flaws of *FP*, and put the former into practice.

4. Ekirch's *Decline of American Liberalism*

In the lecture of Ayn Rand's to which I just alluded, Rand drew her audience's attention to "a very interesting book" that she thought it would profit them to read: "With so illustrious a start," she asked, "how did the

²⁸ John Bolton's *Surrender Is Not an Option* (New York: Threshold Editions, 2008) provides a good rebuttal of Starr's claims for multilateralism. Unfortunately, though Bolton's book was reviewed in *The American Prospect*, the review there makes little effort to engage Bolton's arguments, substituting transparent fallacies for the attempt to do so (Mark Leon Goldberg, "The John Bolton Agenda," *The American Prospect* [November 8, 2007]).

²⁹ Rand, "The Intellectual Bankruptcy of the Age," in Rand, *The Voice of Reason*, p. 85.

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United States descend to its present level of intellectual bankruptcy?” Arthur A. Ekirch, Jr.’s *The Decline of American Liberalism*, she argued, “provides the material, the historical evidence, for the answer to that question.”³⁰

Ekirch’s *Decline* went through two editions, the first in 1955 and the second in 1967, before fading into the background of discourse on liberalism. (Doherty makes favorable reference to it, but Starr ignores it.) A new third edition of *Decline* has been re-issued by The Independent Institute in an attractive paperback edition with a Foreword by historian Robert Higgs. The front matter lists some twenty-three enthusiastic kudos for the book from prominent scholars, journalists, and journals, and Higgs offers a concise and admiring appreciation in his Foreword.

The book takes the form of an intellectual history of the United States in the grand old style of Merle Curti’s *The Growth of American Thought* (1943) and Louis Hartz’s *The Liberal Tradition in America* (1955). The first six chapters begin by discussing the antecedents of American liberalism in “the European Experience,” working through the ideology of the American Revolutionists, moving to a discussion of the centralization of power under the Federalists, and ending with critical discussions of the “Jeffersonian Compromise” and Jacksonian Democracy. The next three chapters focus on slavery, the Civil War, and Reconstruction. The remainder of the book offers an account of the rise of Progressivism, the Progressives’ support for and disillusionment by the First World War, a narrative and critique of the New Deal, and an attack on what Ekirch saw as the creeping militarism of American life in the twentieth century, stretching across both World Wars and into the Cold War. The then-nascent civil rights movement makes an appearance near the end.

True both to Rand’s description and the book’s own title, Ekirch’s story is one of moral and political retrogression. The ideal of liberalism for Ekirch appears to be a kind of romanticized Jeffersonianism—small-scale agrarianism combined with limited and decentralized government. Given this ideal, liberalism’s decline seems to have set in early with the consummation of the Revolution: “Somehow the dreams of an agrarian society seemed always to come into conflict with the realities of American economic development” (p. 39). Having defined liberalism as a mere “collection of ideas or principles which go to make up an attitude or ‘habit of mind’” (p. 3), and conceived its social expression in terms of an agrarian fantasy, it’s unsurprising that on Ekirch’s account, liberalism’s decline consists essentially in its successive confrontations with two centuries of hard reality.

Though Ekirch doesn’t put it this way, I think it’s clear that on the narrative he presents, liberalism declined because it lacked the clarity and rigor to offer solutions for the problems of its day. For all their good

³⁰ *Ibid.*, p. 89.

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intentions, Ekirch's liberals do not seem to have grasped how to reconcile their agrarian conception of property with the requirements of industrial capitalism. Nor were they able to reconcile their commitment to constitutionalism with a strong federal government, or their commitment to civil liberties with the need for a strong military response to totalitarianism. Throughout Ekirch's account, then, we see liberals swinging from one side of a false dichotomy to the other—from agrarian quasi-anarchism to nationalist socialism, from abolitionism about slavery to abolitionism about Reconstruction, from imperialist militarism with Spain to quasi-pacifist appeasement of the Axis and the Soviet Union. The book might well have been subtitled "Episodes in the History of Muddled Thinking."

Unfortunately, Ekirch is himself a captive of many of the same confusions. He criticizes the illiberality of Reconstruction after the Civil War but says nothing about how, without a military occupation of the South by the Union, Southern blacks were to be protected against the lynchings and Jim Crow laws that he deplores a few pages later (pp. 141, 145). He complains that the Fourteenth Amendment's due process clause "vastly extended the domain of the Federal government," but doesn't consider the possibility that an extension of due process might have extended freedom as well (pp. 161-62). He regards the modern corporation as an agent of predation, but naively regards the antitrust laws as a legitimate method of domestication (pp. 197, 286). And his discussion of nineteenth-century property conflicts—railroads, homesteaders, Indians—is a confused muddle (pp. 90-94, 152-60). Were homesteaders' rights violated by the "disposal of public lands" to railroad companies or by the subsidies granted them? Was the Homestead Act of 1862 a granting of Lockean rights or a violation of them? What exactly happened when "the white man" exerted "pressure upon Indian lands"? Is "pressure" a form of market competition or is it a rights violation? In the absence of a conception of rights more precise than a mere "habit of mind," such confusions are inevitable.

Though useful for the glimpse they give into the workings of wartime discourse, Ekirch's discussions of the World Wars and Cold War are notably long on polemics but short on facts. It is, after all, unclear how we are to judge Woodrow Wilson's decision to enter World War I, as Ekirch does, while ignoring questions about the rights of neutral shipping (p. 201). It is likewise unclear that Nazi, Japanese, and Italian aggression were *merely* a reaction to the unfairness of the Treaty of Versailles (p. 288), that domestic fascism was a "more real threat" to the United States than the Axis (p. 295), that American domestic policy was the moral equivalent of Soviet domestic policy (pp. 320, 334), or that mid-century fears of Communist subversion in the U.S. can be dismissed as mere "hysteria" (p. 336). In this respect, Ekirch's rhetoric prefigures Rothbard's unattractive synthesis of Old Right dudgeon and New Left nihilism.

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This is not to say that *Decline* is without value. In some ways, Rand was right to say that the book shows how liberals “betrayed their own liberal ideals,”³¹ It shows, for one thing, that the seeds of liberal self-defeat began with confusions embedded in the Founders’ own ideology, and shows how these confusions ramified through history. The book also offers a usefully critical perspective on the Progressives, interestingly at variance with Starr’s, emphasizing the continuities between American Progressivism and European anti-liberalism, both fascist and socialist.³² And Ekirch’s discussion of the confusions of Progressive discourse on war and imperialism around the time of World War I is both valuable and topically relevant. There are probably dissertations waiting to be written on the parallels between the wartime discourse of the Progressives and that of our contemporary “liberal hawks”; chapter 12 of *Decline* might not be a bad place to begin research.

Having said all this, it is not clear that *Decline* has, on the whole, held up after fifty years, as Higgs claims in his Foreword (p. xix). Much of what is uncontroversial in Ekirch’s account is now common knowledge (e.g., the expropriation of Native Americans, the excesses of McCarthyism), and much of what is controversial has been better handled by subsequent scholarship (e.g., Reconstruction). Beyond that, too much is missing from Ekirch’s narrative, and the book’s ratio of claims to factual support is problematically high. If as Higgs claims, “no good substitute for *The Decline of American Liberalism* is available” (p. xix), perhaps one thing the book shows us is the real need for one, beginning where *Decline* leaves off, supplying what it leaves out, and correcting what it gets wrong.

5. Conclusion

What then *do* we learn about liberalism and liberty from the 1,400+ pages under review? Three interconnected lessons, I think.

A first lesson is that democratic liberals and libertarians/Objectivists have to stop talking past one another on economic matters. The issue that divides them is whether liberty and well-being are better promoted by a regime of capitalist self-ownership or by redistributive/regulatory interferences in capitalist markets. This is a complex and contentious dispute, but it cannot be discussed if each party to the debate ignores the normative claims of the other, as all three of our authors do. Doherty writes as though the meaning of “liberty” were self-evident. Starr writes as though Hobhouse were both the first and last word on the subject. And Ekirch writes less from a

³¹ *Ibid.*, p. 90.

³² Cf. *FP*, pp. 99-116. Ekirch’s discussion is usefully compared with Leonard Peikoff’s in his *The Ominous Parallels* (Briarcliff Manor, NY: Stein and Day, 1982), ch. 14.

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spirit of analysis than of nostalgia. Better analyses would have to take the relevant disagreements more seriously.

Having said that, I think Starr's book offers a good *general* model for how to discuss the issues. What we need are histories, like Starr's, that integrate historical narrative and social science, taking competing conceptions of liberalism as independent variables in normative-historical experiments, and values like liberty and well-being as dependent variables in the same experiments. In an account of this sort, the conception of liberalism shown to be *best* conducive to liberty and well-being wins the day.

But if liberalism is effectively to function as an independent variable in such an experiment, it needs to be defined with greater precision than Doherty, Starr, or Ekirch give it. We cannot, after all, learn very much from an experiment whose independent variable is left undefined (à la Doherty and Starr), or is defined (à la Ekirch) as a "mere collection" of disparate items. Relatedly, if liberty is effectively to function as a dependent variable in such an experiment, it needs to be defined as well; we cannot learn much from an experiment in which liberty figures as a dependent variable but means several incompatible things. If so, we need historical and social scientific work on liberalism that draws more explicitly on *philosophical* analyses of the nature of liberty than any of the works under review.³³

If there is a single overarching lesson here, perhaps it is this: even after 1,400+ pages of elaboration, liberalism remains an "unknown ideal," and much more work has to be done before we achieve knowledge about it.³⁴

³³ For a good philosophical starting point, see Gerald C. MacCallum, Jr., "Negative and Positive Freedom," *Philosophical Review* 76 (1967), pp. 312-34.

³⁴ Thanks to Carrie-Ann Biondi for helpful editorial feedback, and to Carrie-Ann Biondi, Jason Raibley, and Michael Young for helpful discussion.

Bloomfield, Paul, ed. *Morality and Self-Interest*. New York: Oxford University Press, 2008.

This volume comprises an Introduction by the editor and fourteen essays (including one by the editor) on the topic of the title. While the title's breadth could accommodate several different questions and concerns, the editor's introduction explicates the topical focus of the volume as a certain conceptual framework for understanding morality and theorizing about it. Distilling this to its essential elements, it is that "[t]here are two conceptions of 'morality' currently at play in the philosophical literature" (p. 3), and these are a social conception of morality, which "begins with the question of how one ought to behave toward others" (p. 3), and a "Socratic" conception in which "morality is defined within the terms of self-interest, given that it is assumed that living as well as possible is in an agent's self-interest" (p. 4). The editor points out that the "Socratic" conception is "formally" egoistic but need not be "substantially egoistic if one determines that one must treat others well in order to have a well-lived life" (p. 4). The Introduction concludes with the editor remarking that "[t]he editorial claim is that a justified determination of the relation between morality and self-interest ought to precede normative and (more familiar) metaethical theorizing" (p. 9).

That is an important claim, and it invites a certain sort of formulation of some key issues concerning moral theorizing. In some respects, it almost seems as though some of the essays make a somewhat different point. Contributions such as Julia Annas's "Virtue Ethics and the Charge of Egoism" and Joel Kupperman's "Classical and Sour Forms of Virtue," explore important issues of moral psychology in a way that shows those issues to be vitally important to a textured, illuminating conception of morality. The same could be said of T. H. Irwin's "Scotus on the Possibility of Moral Motivation" and Michael Stocker's "Shame and Guilt." These essays are included in sections with headings such as "Morality as Necessary to Self-Interest" and "Morality as Indistinguishable from Self-Interest." Those make good sense, given the aim and the central concern of the volume. But at the same time, some of the essays seem to suggest that perhaps the claim for the priority of the relation between morality and self-interest is somewhat exaggerated. It may be that a number of topics in moral psychology and philosophical anthropology illuminate the morality/self-interest relation in important ways, rather than the latter relation being fundamental.

To be sure, central problems of moral theorizing can analytically be diagnosed in a manner such that a definition of morality without reference to self-interest, on the one hand, is contrasted with a conception of morality to

which an agent's interests are central, on the other. A number of the essays address this concern directly. These include Samuel Scheffler's "Potential Congruence" and Stephen Finlay's "Too Much Morality," for instance. Scheffler critically discusses Joseph Raz's arguments that perhaps it is not the case that either "morality or self-interest is a sufficiently unified concept for there to be any interesting question about the relation between them, or for questions about the rational authority of either to make good sense" (p. 127). Scheffler's notion of potential congruence is intended to show that morally motivated individuals are not thereby hindered from leading "good and fulfilling lives" in terms of their own projects (p. 133). Finlay argues that, "in addressing the normative question, 'Ought we comply with morality or with self-interest?' we are left with the psychological question: 'Which do we care more about, anonymous others' interests or our own?'" (p. 154). He concludes that, "for virtually all of us, most of what we morally ought to do—like what we self-interestedly ought to do—is less important than the pursuit of certain of our *selfish* concerns" (p. 154). Richard Joyce's "Morality, Schmorality" engages with the editor's contribution ("Why It's Bad to Be Bad") in which Bloomfield argues that being immoral is harmful to the immoral agent: "it keeps one from seeing the value of human life, and if one is human, then one is kept from seeing the value of one's own life" (p. 271). Bloomfield's discussion is shaped by Thrasymachus's challenge to the claim that it is bad (for oneself) to be bad. Joyce argues that "moral badness and imprudence are nonidentical" (p. 63). His argument is embedded in a fictionalist interpretation of morality—one that denies "the truth of any moral proposition if pressed in an appropriately serious manner . . . thus deflating a host of well-thumbed philosophical problems concerning the ontology of moral facts and our access to them" (p. 68). In the view Joyce defends, "moral judgments are useful because they influence motivation" (p. 75). Moral discourse can be a "bulwark against various kinds of practical infirmity—for example, weakness of will, discounting future gains, and so on" (p. 73).

The range of the volume and variety of approaches is notable. There is Thomas Nagel's "The Value of Inviolability," which is concerned with the basis for a conception of rights, registering a notion of inviolability, which is "a version of Kant's idea that persons should not be treated merely as means" (p. 105). Mathias Risse's "Nietzsche on Selfishness, Justice, and the Duties of the Higher Men" is a study of the development of some of Nietzsche's thought concerning duties, placing it in relation to some other modern thinkers (e.g., Rousseau and Kant) and exploring its role in his conception of higher men. Michael Stocker's "Shame and Guilt" connects those topics with self-interest and morality through psychoanalytic handling of relevant considerations. The main upshot of Stocker's discussion is to have shown "the inadequacy of various attempted characterizations of shame and guilt and

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especially the differences between them” (p. 301). Stocker presents a textured, critical discussion of several proposals concerning the differences between them, pointing out their defects.

There are some very strong essays in this volume and the strengths are of different sorts. Some of the essays make valuable points concerning the history of moral thought; others make illuminating conceptual distinctions; others are penetrating explorations of issues in moral psychology. David Schmidtz’s “Because It’s Right” has particular strengths of the second kind, exhibited in the course of examining H. A. Prichard’s claim that we keep promises simply because it is right, without reference to why keeping promises is right, which is a place where good reasons have a role. Schmidtz argues that there is a “recognition rule” (which is a notion borrowed from H. L. A. Hart) for right actions, picking them out as “actions for which there are good reasons” (p. 101). In Schmidtz’s view, “there is no mistake in asking whether being moral is prudent” (p. 83) and “we can intelligibly ask whether following categorical imperatives is to our advantage” (p. 101). Such a question has an answer. Christopher Morris’s “The Trouble With Justice” combines analytical argumentation with a good deal of historical reference, and argues that “the norms of justice are *authoritative*; that is, they are *preemptive* reasons (to act or to refrain from acting, to adopt certain attitudes, to assign responsibility, etc.) to all (to whom they apply) on all occasions (when they apply)” (p. 27). His account relies extensively on basically Humean resources. His view takes seriously the question of why we need justice and have reason to be just.

W. D. Falk’s “Morality, Self, and Others” presents a textured diagnosis of the concept of morality and its relation to other types of obligation, and of the role of mores. He argues that “[t]he hard fact is that the rational and autonomous mode of life overlaps, but no longer necessarily coincides, with the moral mode of life as conceived from the point of view of the social interest” (p. 250). “The *moral* and the *definitive* commitments on the mature level need not then coincide” (p. 250). In leading to his conclusion, he argues that “there is one commitment whose ground is intimately personal and which comes before any other personal or social commitment whatsoever: the commitment to the principled mode of life as such” (p. 241). Much of Falk’s discussion is an exploration of the form of the “preservation of oneself as a capable ego” (p. 240) and the relation of this to social obligations. He concludes that the “multiple associations” of the concept of morality, which have developed through its “conceptual evolution” are “a bar to summing it up in any one way” (p. 25).

In “Butler on Virtue, Self-Interest, and Human Nature,” Ralph Wedgwood argues that “there are pressures arising from morality itself to accept something like Butler’s claims about the general harmony between virtue and happiness” (p. 203). However, he adds that “Butler’s arguments for

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the harmony of virtue and self-interest seem to me pure wishful thinking” (p. 203). Wedgwood explores numerous aspects of Butler’s normative claims and moral psychology and concludes that we must “face the hard fact that a virtuous life is the right or proper life for us to lead—even though by living such a life we expose ourselves to various sources of pain and anxiety that the vice of callousness would spare us from” (p. 204).

In some respects, the range of topics and approaches is broader than the focus indicated by the editor. The moral-psychological claims and arguments of some of the essays suggest that the framing formulation (involving the “social” conception of morality and the “Socratic” conception) may be inadequately responsive to the texture of the issues discussed. The contrast may be drawn somewhat too sharply and several of the arguments in various essays suggest that the way that the modern distinction is drawn may say more about some modern philosophers’ formulations than about fundamental, enduring questions concerning values and practical rationality. One could also imagine the volume being organized differently, perhaps with a section on the history of moral philosophy, a section on practical reason, a section on egoism, and a section on metaethics—or some other organization of the essays. This is not to suggest any deficiency in its organization. It is just a point about the multiplicity of important issues addressed by the contributions to the volume. If the two conceptions of morality are meant to supply one crucial dimension of moral theorizing, the rationale for the volume and its organization makes very good sense. If the elements of the contrastive pairs of conceptions are meant to define the core concern of moral theorizing, that seems to me an overstatement—a point one might infer from some of the essays.

The volume has points of contact with many issues in moral theory, moral psychology, and metaethics. In general, the essays are somewhat beyond the reach of most undergraduates except perhaps some in upper-level courses or those writing honors theses or research papers. The contributions presuppose a fluent grasp of several important debates in moral philosophy and a familiarity with the history of philosophy exceeding what could be expected of most undergraduates. Scholars and graduate students will find the volume a valuable resource. Its being a combination of historically informed studies as well as conceptual analysis makes for strength and interest despite the fact that I have raised some critical concerns about the formulation of its rationale. Even if the reader does not find that formulation compelling, the book could be of considerable interest, and it speaks to people working in a number of different areas of moral philosophy.

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Levy, Robert and William Mellor. *The Dirty Dozen: How Twelve Supreme Court Cases Radically Expanded Government and Eroded Freedom*. New York: Sentinel, 2008.

Several years ago, law professor Gary Lawson published an article asking what should be done about the fact that American legal and political institutions have now drifted so far from the actual meaning of the Constitution.¹ Returning to the Framers' design of limited and decentralized government would require such extreme political measures at this point that it seems unrealistic even to suggest the possibility. The best that can now be done, Lawson concludes, is for America's political leaders to declare honestly that the Constitution no longer figures into their decisions in a serious way. Admitting it, as they say, is the first step.

Robert Levy and William Mellor are not quite so resigned. As practicing attorneys who have won significant Supreme Court victories in recent years, they still have confidence in the legal system's ability to reform. But looking over their list of the twelve worst Supreme Court decisions of the twentieth century, and seeing how deeply lie the errors in those decisions, is enough to shake anybody's faith. How could so much law be so backward, and what can we do about it?

Levy and Mellor present twelve Supreme Court flops, along with eight runners-up. They categorize the cases by the individual right or constitutional provision at stake. In the hands of less sophisticated writers, this format would degenerate into a list of partisan complaints, but Levy and Mellor approach their task from a solid theoretical base. As a result, their book is actually more of a rigorous critique of the current state of constitutional law than the title might suggest. The "dozen" format is a device that draws readers into understanding the nature of some of the fundamental errors that have been absorbed into constitutional law. It is not surprising, therefore, that six of the dozen and three of the runners-up date from the period of the New Deal, when the Supreme Court formally adopted the jurisprudence first formulated during the Progressive Era, a jurisprudence that overthrew the classical liberal model of American law. The Court's embrace of the new approach in the 1930s marked a geological shift in law, uprooting

¹ Gary Lawson, "The Rise and Rise of the Administrative State," *Harvard Law Review* 107 (April 1994), pp. 1231-54.

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centuries-old protections for property rights and economic freedoms and fundamentally altering the American political process.

The American Founders believe that individual liberty is a fundamental good; they even refer to it as a “blessing” in the text of the Constitution itself. As the Declaration of Independence makes clear, government exists only as a tool to protect that blessing, and if it ever becomes destructive of natural rights, the people retain the right to alter or to abolish it. In their view, freedom is a primary principle, and government a secondary institution, designed to serve that end, and kept in harness by a variety of complicated checks and balances.

The Progressives inverted this model. For them, the authority of the collective is primary; indeed, it is the source of the individual’s “freedom.” To suit this scheme, the Progressives redefined the very word freedom. No longer did it mean, in John Locke’s words, a citizen’s ability “to dispose and order freely as he lists his person, actions, [and] possessions . . . and . . . not to be subject to the arbitrary will of another, but freely follow his own.”² Instead, in the words of John Dewey, the leading philosopher of Progressivism, freedom means the individual’s ability to grow as a full member of the collective. “[T]he problem of achieving freedom,” in his eyes, is “a problem of establishing an entire social order, possessed of a spiritual authority that would nurture and direct the inner as well as the outer life of individuals,” and the goal is to create a “form of social organization, extending to all the areas and ways of living, in which the powers of individuals shall not be merely released from mechanical external constraint but shall be fed, sustained and directed.”³

Thus did the Progressives replace liberty with democracy as the central constitutional value—with democracy understood not simply as a form of politics allowing citizen participation, but as a style of nationality, a way of living, in which the individual is simultaneously subsumed and fostered by the collective. Individual rights are recast as privileges (revocable ones) that the state gives to individuals to serve social needs. “Any merely individual right,” writes Dewey,

must yield to the general welfare. As long as freedom of thought and speech is claimed as a merely individual right, it will give way, as to other merely personal claims, when it is, or is successfully represented to be, in opposition to the general welfare. Liberalism

² John Locke, *Second Treatise of Civil Government*, ed. Peter Laslett, rev. ed. (Oxford: Oxford University Press, 1963), ch. 6, para. 57, p. 348.

³ John Dewey, *Liberalism and Social Action* (New York: Capricorn Books, 1963), pp. 30-31.

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has to assume the responsibility for making it clear that intelligence is a social asset and is clothed with a function as public as is its origin, in the concrete, in social cooperation.⁴

It took a while for the Progressive model to be adopted by the legal profession, and its epigones on the Supreme Court, such as Louis Brandeis and Oliver Wendell Holmes, regularly found themselves writing dissenting opinions. But between 1934 and 1938, the Supreme Court gave it a formal imprimatur in a series of decisions upholding the constitutionality of New Deal programs and announcing that in the future, judges would simply presume the constitutionality of restrictions on individual rights in all but the most extreme cases. It devised the so-called “rational basis” test, under which laws are held to be constitutional if any rational person could have believed they would advance some public goal. And it declared that certain categories of rights, such as free speech or the right to vote, would receive greater judicial protection than other rights, such as private property or economic liberty. With some slight modifications, this scheme still governs the judiciary today.

Levy and Mellor’s theme is the impact of these Progressive premises on American constitutional law. This is obvious in chapters 1, 2, and 3, in which they criticize New Deal-era decisions that expanded Congress’s powers under the General Welfare and Interstate Commerce clauses, and allowed states to override the language of private contracts despite the explicit prohibition of such acts in Article I, section 10, of the Constitution. This is also clear in chapters 7 and 11, which discuss the 1944 *Korematsu* case, upholding the internment of Japanese-Americans in prison camps during World War II, and the 1938 *Carolene Products* case, allowing legislatures almost limitless power to deprive citizens of the freedom to make economic choices.

But this impact is seen even in chapters that address more recent decisions. In Chapter 5, for example, they criticize *McConnell v. Federal Elections Commission*, the 2003 decision upholding the constitutionality of the Bipartisan Campaign Reform Act (commonly known as “McCain-Feingold”). The Constitution forbids Congress from enacting any law which shall abridge the freedom of speech, and the ability to make financial contributions to a political candidate or organization is the most effective means of political speech that most Americans have. Yet the justices upheld the law’s restrictions on financial contributions to political candidates, partly on the ground that they represent an improper influence on democratic government. Such contributions, the Court notes, are often “motivated by a

⁴ *Ibid.*, pp. 66-67.

desire for access to candidates and a fear of being placed at a disadvantage in the legislative process relative to other contributors, rather than by ideological support for the candidates and parties.”⁵

What could possibly be wrong with citizens in a democracy seeking to influence political representatives and to avoid being placed at a disadvantage in the legislative process? As Levy and Mellor observe, this can be considered corrupt only by those who interpret the First Amendment as requiring “*fair* speech . . . instead of ensuring *free* speech, as intended by the framers. That egalitarian impulse, utterly at odds with the idea of individual liberty that animates the Bill of Rights, was at the core of the Court’s opinion” (p. 97). That impulse was the product of Progressive intellectuals like Dewey, who argue for the overthrow of “the old habit of defending liberty of thought and expression as something inhering in individuals apart from and even in opposition to social claims.”⁶ When he and other Progressives argue that freedom of thought and speech are “social assets” rather than individual rights, they mean that citizens’ ability to criticize political policy is an instrumental good serving the goal of effective democratic management. Freedom of speech is therefore a license given to citizens by the state for the state’s own purposes. And, on those premises, it makes sense that government should expand or contract the citizens’ freedom of political expression in order to make it serve social goals. The problem is that government itself determines what those goals are, so the state will ultimately decide which criticisms are and are not “good for society,” and restrict freedom accordingly. In short, the government becomes the judge in its own case. “[T]he real effect of the regulations upheld in *McConnell*,” Levy and Mellor conclude, “has been to protect incumbents from upstart challengers. The careers of sitting politicians can more easily be perpetuated if the speech of their opponents can be repressed” (p. 106).

In the end, it is not surprising that so much constitutional law could turn out to be so wrong. The prevalence of error is the result of certain fundamental intellectual missteps taken at a particular time, which have reverberated in the form of judicial decisions ever since. Given the legal system’s reliance on precedent, it is predictable that specific, central errors would have long-lasting and unanticipated consequences.

The authors’ criticisms are principled and effectively argued in terms accessible equally to lawyers and laymen. Nor can one quibble much with their choice of targets; specialists might add less influential cases to the list, and one might argue that such nineteenth-century disasters as *Dred Scott* and

⁵ *McConnell v. Federal Elections Commission*, 540 U.S. 93, 124-25 (2003).

⁶ Dewey, *Liberalism and Social Action*, p. 67.

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The Slaughterhouse Cases deserve to be addressed also, but the authors' selections are well made to avoid reducing the book to a parlor game.

And yet the book leaves us with a very difficult problem. If so much law is so deeply wrong, and if the flaws have stayed in place for more than seven decades, what if any remedy can be hoped for? Levy and Mellor conclude with a "call for the appointment of justices who are willing to take clear and consistent stands in favor of the framers' understanding of the Constitution" (p. 215). Such a change in personnel, however, is unlikely, given a political standoff that turns every Court nomination into a frenzy. That problem is complicated by the fact that many political leaders are ignorant of important intellectual disputes within the legal profession. The differences between the jurisprudence of Justice Scalia and Justice Thomas, for example, are important ones, but they are beyond the understanding of many presidents and congressmen. As a consequence, judicial nominations are often managed without any serious understanding of a nominee's intellectual orientation: witness the nomination of Justice David Souter.⁷

More fundamentally, though, Levy and Mellor urge courts to employ textualism—the commonsense willingness to enforce the meaning of the Constitution's text—rather than seeking clever ways to reconcile the Constitution with perverse modern institutions, or to ignore the text when inconvenient, as today's judges do. "[W]hat is the purpose of a written document—whether a private contract or a Constitution—if we act as though it does not exist?" (p. 217). The "cavalier attitude toward government powers" that prevails today should be replaced by a jurisprudence that enforces the Constitution's promises, puts real limits on government, and protects individual rights—both "economic" and participatory rights—not as privileges but as inviolable and universal principles. The authors acknowledge that this would lead courts to practice so-called "judicial activism," if activism means "willing engagement in applying the law and the Constitution to scrutinize the acts (or omissions) of the executive and legislative branches" (p. 222). Nothing less is called for by the Constitution.

But as Gary Lawson recognizes, reengaging with our nation's political principles would be a major undertaking. This is true in the crude sense that federal agencies have proliferated since the New Deal, acquiring concentrated constituencies made up not only of citizens who benefit from their largesse, but also of government employees and their unions. A graph measuring the size of the government payroll since 1934 would be tilted steeply upward, due both to voter ignorance and to the inertial effects of self-

⁷ See, e.g., Jan Crawford Greenburg, *Supreme Conflict: The Inside Story of the Struggle for Control of the United States Supreme Court* (New York: Penguin Press, 2007).

seeking by interest groups. It is also true in the broader sense that American intellectuals, and particularly lawyers, have by now lost even the memory that there ever was another way. The very concept of a free society is alien to them; few understand how it might even be possible for free markets to provide bridges, health care, or safe airline travel. Having been raised within the New Deal paradigm, they mistake it for the very handiwork of nature, and regard any proposal for change as irresponsible radicalism. Cass Sunstein even titled his recent book attacking conservative judges *Radicals in Robes*.⁸

This fact suggests an important lesson for those who hope for a change in the jurisprudential *status quo*: libertarians are *not* looking to set America back in time or to return to some long-lost Eden. Talk of a “constitution in exile” is both self-defeating and inaccurate. The United States has never in fact had a political system that accorded in all respects with the Constitution’s promises. Whether it be the deprivation of women’s right to equality, or the institutions of slavery and segregation, the American nation has long shown a capacity for institutional dissonance—a willingness, whatever the motive, to allow political leaders to violate those principles to which the nation has explicitly pledged itself in its founding documents. Making our government obey those principles would be a step forward, not backward. And the path of reform might follow the route of the Second Amendment decision issued after *The Dirty Dozen* was published (*DC v. Heller* [2008]). Before then, the Court had never decided whether and to what degree the Constitution protected an individual’s right to possess firearms. But a strong consensus had congealed in the legal community, to the effect that it protected only a collective right of political entities, not of individual citizens. This consensus, however, was overthrown with a strong opinion relying heavily on the original meaning of the Second Amendment and asserting strong protections for individual rights against government encroachment. It did so as a result of energetic and creative litigation by principled and scholarly attorneys, one of whom was Robert Levy.

Yet, central to any reform attempt is the need for a philosophical reorientation, particularly with regard to individual rights. Among the Progressives’ most important victories was their redefinition of rights as privileges which exist for social purposes, rather than as central political principles to which all human beings have a just claim. This idea is now ubiquitous in the law and in the academies, where the Declaration of Independence is studied only for its “influence,” rather than its truth value. But regular Americans still cherish the belief that it is indeed the case that all men are created equal, with certain inalienable rights which any just

⁸ Cass R. Sunstein, *Radicals in Robes: Why Extreme Right Wing Courts Are Wrong for America* (New York: Basic Books, 2005).

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government must protect. It is only by restoring that principle to its rightful place in our intellectual commitments that lasting change for the better can come.

Our legal institutions, like everything else about the government of the United States, are ultimately the products of public opinion. The Progressives' attack on the classical liberal foundations of the U.S. Constitution was extraordinarily successful and its effects are today deeply rooted. But even that was a gradual effort; starting in the late-nineteenth century, the Progressive revolution culminated only fifty years later. Libertarians, too, must patiently and gradually influence the public's understanding of the role of government and the fundamental importance of individual liberty, both in the courtroom and in the public arena. This will be a long and sometimes seemingly hopeless task, but in the end a restoration of our constitutional commitment to individual freedom and limited government is possible. Levy and Mellor's intelligent critique of the prevailing theories of constitutional law is an excellent contribution to that effort.

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