Homework

Read pages 442-445 (copies attached) of Mankiw's "The Political Philosophy of Redistributing Income". Which political philosophy aligns most with your own value-system, utilitarianism, liberalism, or libertarianism? Why is this? Also, describe what specifically you don't like in the two political philosophies that you didn't pick. Please write two or three paragraphs answering these questions (between 400 and 500 words, please include a word-count).

Address concepts such as incentives, unintended consequences, Hayek's "knowledge problem", the role of a social planner, interpersonal comparisons of utilities, and be specific when using words such as "fairness", "justice", "balance", "happiness", "poor", "rich" and "class". An acceptable essay must directly address the meaning of these words, what the words-concepts mean to you and as found in the Mankiw text and class discussion.

QUICK QUIZ What does the poverty rate measure? ◉ Describe three potential problems in interpreting the measured poverty rate.

THE POLITICAL PHILOSOPHY OF REDISTRIBUTING INCOME

We have just seen how the economy's income is distributed and have considered some of the problems in interpreting measured inequality. This discussion was *positive* in the sense that it merely described the world as it is. We now turn to the *normative* question facing policymakers: What should the government do about economic inequality?

This question is not just about economics. Economic analysis alone cannot tell us whether policymakers should try to make our society more egalitarian. Our views on this question are, to a large extent, a matter of political philosophy. Yet because the government's role in redistributing income is central to so many debates over economic policy, here we digress from economic science to consider a bit of political philosophy.

UTILITARIANISM

utilitarianism
the political philosophy according to which the government should choose policies to maximize the total utility of everyone in society

utility
a measure of happiness or satisfaction

A prominent school of thought in political philosophy is **utilitarianism**. The founders of utilitarianism are the English philosophers Jeremy Bentham (1748–1832) and John Stuart Mill (1806–1873). To a large extent, the goal of utilitarians is to apply the logic of individual decision making to questions concerning morality and public policy.

The starting point of utilitarianism is the notion of **utility**—the level of happiness or satisfaction that a person receives from his or her circumstances. Utility is a measure of well-being and, according to utilitarians, is the ultimate objective of all public and private actions. The proper goal of the government, they claim, is to maximize the sum of utility achieved by everyone in society.

The utilitarian case for redistributing income is based on the assumption of *diminishing marginal utility*. It seems reasonable that an extra dollar of income provides a poor person with more additional utility than an extra dollar would provide to a rich person. In other words, as a person's income rises, the extra well-being derived from an additional dollar of income falls. This plausible assumption, together with the utilitarian goal of maximizing total utility, implies that the government should try to achieve a more equal distribution of income.

The argument is simple. Imagine that Peter and Paul are the same, except that Peter earns $80,000 and Paul earns $20,000. In this case, taking a dollar from Peter to pay Paul will reduce Peter's utility and raise Paul's utility. But because of diminishing marginal utility, Peter's utility falls by less than Paul's utility rises. Thus, this redistribution of income raises total utility, which is the utilitarian's objective.

At first, this utilitarian argument might seem to imply that the government should continue to redistribute income until everyone in society has exactly the same income. Indeed, that would be the case if the total amount of income—$100,000 in our example—were fixed. But in fact, it is not. Utilitarians reject complete equalization of incomes because they accept one of the *Ten Principles of Economics* presented in Chapter 1: People respond to incentives.

To take from Peter to pay Paul, the government must pursue policies that redistribute income. The U.S. federal income tax and welfare system are examples. Under these policies, people with high incomes pay high taxes, and people with low incomes receive income transfers. Yet if the government takes away additional income a person might earn through higher income taxes or reduced transfers, both Peter and Paul have less incentive to work hard. As they work less, society's income falls, and so does total utility. The utilitarian government has to balance the gains from greater equality against the losses from distorted incentives. To maximize total utility, therefore, the government stops short of making society fully egalitarian.

A famous parable sheds light on the utilitarian's logic. Imagine that Peter and Paul are thirsty travelers trapped at different places in the desert. Peter's oasis has much water; Paul's has little. If the government could transfer water from one oasis to the other without cost, it would maximize total utility from water by equalizing the amount in the two places. But suppose that the government has only a leaky bucket. As it tries to move water from one place to the other, some of the water is lost in transit. In this case, a utilitarian government might still try to move some water from Peter to Paul, depending on the size of Paul's thirst and the size of the bucket's leak. But with only a leaky bucket at its disposal, a utilitarian government will stop short of trying to reach complete equality.

Liberalism

A second way of thinking about inequality might be called **liberalism**. Philosopher John Rawls develops this view in his book *A Theory of Justice*. This book was first published in 1971, and it quickly became a classic in political philosophy.

liberalism
the political philosophy according to which the government should choose policies deemed just, as evaluated by an impartial observer behind a "veil of ignorance"

Rawls begins with the premise that a society's institutions, laws, and policies should be just. He then takes up the natural question: How can we, the members of society, ever agree on what justice means? It might seem that every person's point of view is inevitably based on his or her particular circumstances—whether he or she is talented or less talented, diligent or lazy, educated or less educated, born to a wealthy family or a poor one. Could we ever *objectively* determine what a just society would be?

To answer this question, Rawls proposes the following thought experiment. Imagine that before any of us is born, we all get together for a meeting to design the rules that govern society. At this point, we are all ignorant about the station in life each of us will end up filling. In Rawls's words, we are sitting in an "original position" behind a "veil of ignorance." In this original position, Rawls argues, we can choose a just set of rules for society because we must consider how those rules will affect every person. As Rawls puts it, "Since all are similarly situated and no one is able to design principles to favor his particular conditions, the principles of justice are the result of fair agreement or bargain." Designing public policies and institutions in this way allows us to be objective about what policies are just.

Rawls then considers what public policy designed behind this veil of ignorance would try to achieve. In particular, he considers what income distribution a person would consider fair if that person did not know whether he or she would end up at the top, bottom, or middle of the distribution. Rawls argues that a person in the original position would be especially concerned about the possibility of being at the *bottom* of the income distribution. In designing public policies, therefore, we should aim to raise the welfare of the worst-off person in society. That is, rather than maximizing the sum of everyone's utility, as a utilitarian would do,

maximin criterion
the claim that the government should aim to maximize the well-being of the worst-off person in society

Rawls would maximize the minimum utility. Rawls's rule is called the **maximin criterion**.

Because the maximin criterion emphasizes the least fortunate person in society, it justifies public policies aimed at equalizing the distribution of income. By transferring income from the rich to the poor, society raises the well-being of the least fortunate. The maximin criterion would not, however, lead to a completely egalitarian society. If the government promised to equalize incomes completely, people would have no incentive to work hard, society's total income would fall substantially, and the least fortunate person would be worse off. Thus, the maximin criterion still allows disparities in income because such disparities can improve incentives and thereby raise society's ability to help the poor. Nonetheless, because Rawls's philosophy puts weight on only the least fortunate members of society, it calls for more income redistribution than does utilitarianism.

social insurance
government policy aimed at protecting people against the risk of adverse events

Rawls's views are controversial, but the thought experiment he proposes has much appeal. In particular, this thought experiment allows us to consider the redistribution of income as a form of **social insurance**. That is, from the perspective of the original position behind the veil of ignorance, income redistribution is like an insurance policy. Homeowners buy fire insurance to protect themselves from the risk of their house burning down. Similarly, when we as a society choose policies that tax the rich to supplement the incomes of the poor, we are all insuring ourselves against the possibility that we might have been a member of a poor family. Because people dislike risk, we should be happy to have been born into a society that provides us this insurance.

It is not at all clear, however, that rational people behind the veil of ignorance would truly be so averse to risk as to follow the maximin criterion. Indeed, because a person in the original position might end up anywhere in the distribution of outcomes, he or she might treat all possible outcomes equally when designing public policies. In this case, the best policy behind the veil of ignorance would be to maximize the average utility of members of society, and the resulting notion of justice would be more utilitarian than Rawlsian.

LIBERTARIANISM

libertarianism
the political philosophy according to which the government should punish crimes and enforce voluntary agreements but not redistribute income

A third view of inequality is called **libertarianism**. The two views we have considered so far—utilitarianism and liberalism—both view the total income of society as a shared resource that a social planner can freely redistribute to achieve some social goal. By contrast, libertarians argue that society itself earns no income—only individual members of society earn income. According to libertarians, the government should not take from some individuals and give to others to achieve any particular distribution of income.

For instance, philosopher Robert Nozick writes the following in his famous 1974 book *Anarchy, State, and Utopia:*

> We are not in the position of children who have been given portions of pie by someone who now makes last minute adjustments to rectify careless cutting. There is no *central* distribution, no person or group entitled to control all the resources, jointly deciding how they are to be doled out. What each person gets, he gets from others who give to him in exchange for something, or as a gift. In a free society, diverse persons control different resources, and new holdings arise out of the voluntary exchanges and actions of persons.

Whereas utilitarians and liberals try to judge what amount of inequality is desirable in a society, Nozick denies the validity of this very question.

The libertarian alternative to evaluating economic *outcomes* is to evaluate the *process* by which these outcomes arise. When the distribution of income is achieved unfairly—for instance, when one person steals from another—the government has the right and duty to remedy the problem. But as long as the process determining the distribution of income is just, the resulting distribution is fair, no matter how unequal.

Nozick criticizes Rawls's liberalism by drawing an analogy between the distribution of income in society and the distribution of grades in a course. Suppose you were asked to judge the fairness of the grades in the economics course you are now taking. Would you imagine yourself behind a veil of ignorance and choose a grade distribution without knowing the talents and efforts of each student? Or would you ensure that the process of assigning grades to students is fair without regard for whether the resulting distribution is equal or unequal? For the case of grades at least, the libertarian emphasis on process over outcomes is compelling.

Libertarians conclude that equality of opportunities is more important than equality of incomes. They believe that the government should enforce individual rights to ensure that everyone has the same opportunity to use his or her talents and achieve success. Once these rules of the game are established, the government has no reason to alter the resulting distribution of income.

QUICK QUIZ Pam earns more than Pauline. Someone proposes taxing Pam to supplement Pauline's income. How would a utilitarian, a liberal, and a libertarian evaluate this proposal?

POLICIES TO REDUCE POVERTY

As we have just seen, political philosophers hold various views about what role the government should take in altering the distribution of income. Political debate among the larger population of voters reflects a similar disagreement. Despite these continuing debates, most people believe that, at the very least, the government should try to help those most in need. According to a popular metaphor, the government should provide a "safety net" to prevent any citizen from falling too far.

Poverty is one of the most difficult problems that policymakers face. Poor families are more likely than the overall population to experience homelessness, drug dependence, health problems, teenage pregnancy, illiteracy, unemployment, and low educational attainment. Members of poor families are both more likely to commit crimes and more likely to be victims of crimes. Although it is hard to separate the causes of poverty from the effects, there is no doubt that poverty is associated with various economic and social ills.

Suppose that you were a policymaker in the government, and your goal was to reduce the number of people living in poverty. How would you achieve this goal? Here we examine some of the policy options that you might consider. Each of these options helps some people escape poverty, but none of them is perfect, and deciding upon the best combination to use is not easy.