‘Econogenic Harm’: On the Nature of and Responsibility for the Harm Economists Do as they Try to Do Good

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Abstract: Economists have long recognized that virtually all economic policy interventions that they advocate entail foreseeable and/or unforeseeable harm to some economic actors, even while promising benefits for others. And yet, there is no tradition in economics that explores carefully the harm that economists cause as they try to do good.

“Iatrogenic harm” (from the Greek, “doctor-originating”) refers to the harm that results from medical practice. The essay proposes the term “econogenic harm” to name the harm that results from economic practice. Despite the ubiquity of econogenic harm, economists have failed to give a good account of the complex nature of economic harm or to wrestle with its ethical entailments. Instead, economists have relied too eagerly on the Kaldor-Hicks compensation test, often operationalized through cost-benefit analysis, as a sufficient ethical guide for their own conduct in policy formation. But Kaldor-Hicks cannot serve the ethical purposes to which it has been put.

Keywords: Econogenic harm; economic harm; Kaldor-Hicks compensation test; compensable vs. non-compensable harm; reparable vs. irreparable harm; rights violations; normative vs. positive economics

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> "If it were known to be true, as a question of fact, that measures that cause misery and death to tens of millions today *would* result in saving from greater misery or death hundreds of millions in the future, and if this were the only way in which it could be done, then it *would* be right to cause these necessary atrocities."
>
> --J.J.C. Smart 1973 (emphasis in original)

> *Words matter!*
>
> --Deirdre McCloskey

<1>I. Introduction

Professional practice often entails a potential for harm to those professionals seek to serve, and to third parties. This is true in clinical medicine and public health, of course, but also in social work, engineering, law, and many if not most other professions. Partly in recognition of this fact some professions have established bodies of professional ethics in hopes of promoting responsible behavior by their members—behavior that minimizes the avoidable harms and that helps them manage appropriately the unavoidable harms that may arise in the context of their practice. The medical profession is exemplary in this regard. In medical ethics we find the term "iatrogenesis" or "iatrogenic harm" (from the Greek, "doctor-originating"), which refers to the adverse effects or complications associated with medical treatment. The concept of iatrogenic harm captures physician- or clinic-induced harms ranging from those that are associated with malpractice to the unpreventable consequences of well intentioned and expertly delivered medical interventions.

Economists, on the other hand, generally do not give sufficient attention to the nature of economic harm or to the ways that their own practice induces harm.[1] In fact, we have no language to discuss economist-induced harm. There is no parallel in economics to the concept of medical malpractice, of course; economists are not held legally liable for their mistakes, no matter how severe the effects. More broadly, there is no economic analogue to the concept of iatrogenesis. There should be. We need a concept, and a

[1] This claim will strike many economists as incorrect, if not absurd. The economist's toolkit includes cost-benefit analysis and the Kaldor-Hicks compensation test—both of which involve explicit recognition of the harms associated with economic interventions. I face a burden in what follows, then, to sustain the claim that these methods generally entail a grossly simplistic account of harm—one that fails to recognize its internal heterogeneity and complexity.

corresponding term, to name what is as-of-yet unnamed. Let us refer to the harm economists cause with the term "econogenesis," or "econogenic harm."

The term iatrogenesis is used most often to refer to physical and psychological harm—or to the *medical* harms associated with medical practice. But the concept is also used to capture other harmful effects of medical interventions. For instance, Meessen et al. (2003, 581) describe the impoverishment that accompanies "catastrophic health care expenditure" in the developing world as "iatrogenic poverty." Following their lead, we can distinguish between economic and non-economic forms of econogenic harms. For instance, while adverse health effects of economic interventions—such as the rising alcoholism and dramatic declines in life expectancy that followed rapid privatization in Russia in the 1990s (Stuckler, King, and McKee 2009)—have economic consequences, they are not in the first instance economic. We can therefore speak of "econogenic morbidity" or "econogenic mortality" in cases where economist-advocated interventions undermine public health.

Why do we economists fail to examine sufficiently economic harm in general, and econogenic harm in particular? Several reasons come to mind. First, economists recognize that harm is a regular and, likely, ineradicable feature of economic practice. Any policy intervention that affects relative prices—which is to say, all interventions[2]—"benefits those on one side of the market, and damages those on the other" (Hicks 1939, 706). It needs to be said plainly: *economists are in the harm business*. Almost always we cause harm as we try to do good. Hence, the Hippocratic directive "first, do no harm," if taken as an inviolable mandate or a decision rule, has no relevance in economics since it

[2] While the arguments that appear here apply with particular force to economic policy, many also apply to other economic interventions that economists design and advocate. These include, for instance, the design of government regulations, market structures, financial investment or corporate strategies, etc.

would imply that economists can do nothing at all.[3] Second, for over a century the economics profession has remained stubbornly uninterested in ethical matters (Sen 1987). The allergy to ethics manifests in part as a mistaken presumption that one can easily bifurcate economics into its positive and normative components, and that the economist should privilege positive science over normative speculations. But by its nature, and as we will see, harm does not permit such a bifurcation. Third, in comparison with many other professions that enjoy substantial influence over the life chances of others economics has been particularly dismissive of the idea of *professional* ethics, and especially of professional economic ethics.[4] It is noteworthy in this regard that the large majority of economists in the U.S. work outside of academia where they engage in applied work that bears on policy formation, regulation and other government interventions; affects the outcome of legal disputes; entails consulting to private actors; influences financial market developments; etc. (Lowenstein 2000; DeMartino 2011). Yet, we have no professional economic ethicists, or any texts, journals, newsletters, curriculum, regular conferences, or other forums that explore systematically what it means to be an ethical economist, or what it means for economics to be an ethical profession.[5] Unfortunately, the absence of professional economic ethics deprives us of a tradition of careful inquiry into the nature of econogenic harm.

[3] If we take the Hippocratic directive as an absolute (which, it bears emphasis, neither physicians nor medical ethicists do), it would prohibit economic adjustments that promote extraordinary aggregate gains, or even substantial gains to those most in need. It would dictate that we do nothing at all, even when doing nothing prolongs avoidable misery.

[4] Only in 2011, in the wake of the unwelcome attention to the apparent misbehavior of leading economists that was exposed in the film *Inside Job*, did leading economic associations begin to explore the need for rules to govern conflict of interest disclosure among their members. This is a welcome development—but so far the new initiatives have failed to look beyond conflict of interest to other ethical issues, such as econogenic harm, that arise in the context of economic practice.

[5] The non-binding code of the National Association of Forensic Economics (NAFE) and the interest of that organization's members in professional ethical issues stand as a notable exception (see NAFE undated).

The neglect of economic harm in general and econogenic harm in particular allows economists to undertake their research, teaching, and applied work without sufficient worry about their impact on others. It allows economists to sleep too well at night—a happy circumstance for economists, to be sure, but far too dangerous for those the profession purports to serve.

Three issues concerning harm deserve more careful attention than economists tend to give them. They are 1) the complexity of the concept of harm; 2) the causes and prevalence of econogenic harm; and 3) the inadequacies in the predominant way that economists theorize harm. The following explores each of these matters in turn.

<1>**II. The Complex Nature of (Economic) Harm**

Harm is an exceedingly complex concept.[6] First, harm is internally heterogeneous: a person (or group) can be harmed in many distinct ways (see Table 1). Harm can take the form of dismemberment or the loss of physical and mental faculties; psychological or emotional suffering; loss of income or wealth, or loss of access to valued goods; impairment in the pursuit of one's life plans; loss of creativity, or of inventiveness, or of playfulness (Nussbaum 1992); loss of respect, of meaningful connections with others, of community, or of a valued way of life (Marglin 2008); loss of political efficacy (Sen 1992); etc. Moreover, harm comprises objective and subjective components, and the two may not always align in the ways we might expect. Indeed, harm may occur without inducing any anguish or unhappiness. An example that is relevant in the economic context is given by the case of "adaptive preference formation" in which the oppressed

[6] And yet, sophisticated treatments of the concept of harm are surprisingly rare. But see Feinberg (1984), Sharpe and Faden (1998), and Linklater (2011). The discussion here does not begin to do justice to the complexity of the concept that is revealed in these texts.

Table 1: An Incomplete Taxonomy of Harm

Physical:

- Pain
- Injury or dismemberment
- Loss of physical or mental capacities
- Loss of life
- Degradation of the physical environment

Psychological:

- Emotional or psychological suffering; depression
- Becoming fearful, insecure, or anxious
- Shame
- Loss of hope
- Adaptive preference formation
- Erosion of self-respect
- Loss of capacity for creativity, playfulness, inventiveness, or fraternal feelings

Economic:

- Loss of income, wealth, or social welfare/utility
- Loss of access to valued goods
- Loss of genuine choice over valued goods
- Loss of economic security
- Loss of economic opportunities (to do, be, or become)
- Loss of economic capacities (e.g., to earn a living)

Loss of control over one's economic activities and practices

Alienation from one's labor, output, or nature

Subjection to exploitation, discrimination, or deprivation

Social:

Loss of community

Loss of place in community (status, influence, or role as contributor)

Loss of respect, recognition, or honor

Loss of political efficacy

Loss of fraternity, or meaningful connections with others

Erosion of social capital

Moral:

Erosion, inversion and/or collapse of important values or ethical virtues, sensibilities and norms

Autonomy:

Impairment in the pursuit of one's life plans

Treatment as mere means and not also as an end

Destruction of a valued way of life

Constriction of one's capabilities or feasibility set

Exacerbation of personal or systemic threats, risk, or instability

Assault on negative or positive rights/freedoms (coercion)

Denial of opportunity to participate in vitally important social, economic, or cultural processes

come to believe that they do not value the important goods that are denied to them (Elster1982). The possibility of hidden harm complicates greatly judgments about the incidence and extent of harm and raises the thorny question, who should be authorized to ascertain when, how and how badly an agent has in fact been harmed—the agent, her close associates, or some detached "harm expert"? Making matters worse, a harmful event might induce diverse, compound harms to individuals, families, and communities. For instance, an economic crisis causes various economic harms, of course, but also many of what I've listed here as psychological and social harms, along with harms to personal autonomy and freedom. The example of economic crisis also points us to the fact that while harm often manifests immediately upon the heels of the event that induces it, it can also linger well into the future (and even compound over time), affecting those not yet born at the time of the event. A Greek family in 2014 whose economic security is undermined as a consequence of the severe austerity measures now in place, which many economists endorse in response to the country's fiscal imbalance, may very well transmit substantially diminished health prospects (Stuckler and Basu 2013) and economic capacities to future generations. Finally for present purposes, we need to acknowledge the analytical problem that what is harmful to one person may prove to be benign or even beneficial to another owing to differences between the two (in their age and other physical attributes, familial obligations, degree of optimism and initiative, extent of integration into the community, and other salient characteristics).[7] For instance, becoming unemployed may severely damage one agent who for whatever reason lacks the capacity to respond productively to the change in circumstances but

[7] I am grateful to Robert Lepenies for suggesting this line of argument.

provide the impetus for another to attain new skills, start his own business, relocate to a more vibrant region, or otherwise change his life for the better. This complicates the matter of assessing the occurrence and causes of harm, the causal significance of any harm-inducing event, the severity of the consequent harm, the responsibility for the harms suffered (and harm avoidance and amelioration); and much else besides.

Second, the concept of harm relates in complex ways to central features of human nature and social existence. Agents suffer harm when their welfare, agency, freedoms, liberties or valued relationships are undermined. An adequate account of harm, then, presumes an adequate engagement with these salient features. For instance, a comprehensive account of harm almost certainly requires a good account of human needs, flourishing, subjectivity (and subjectivity formation), and of human connections with others and with their natural and social environment, let alone an adequate conception of human rights (civil and political, and economic, social and cultural), freedoms, liberties, and responsibilities.

Third, once we have specified what does and what does not count as harm, we then have to explore carefully which harms are morally indictable and which are altogether acceptable. If one participant beats another in a fair contest voluntarily and fairly played and judged—be it a sporting event, a political election, the pursuit of a coveted honor, award, good, life partner, or some form of economic competition—the victor may have harmed the vanquished by denying him the goal he sought.[8] The

[8] By fair contest I refer to a contractarian judgment that society's members would choose to live in a world that permits the contest and the stakes associated with winning and losing. Though I cannot explore the matter here (but see DeMartino 2011), economists too readily presume consent (or dismiss the need for

unsuccessful participant may feel the pain of loss acutely; he may even be devastated and ashamed, with detrimental effects on the course of his life. But while such harm may earn for the unsuccessful contestant sympathy or concern for his welfare, it does not entitle him to our indignation, or to redress. In short, not all victims of harm are rightly aggrieved by their hardship; and not all individuals or institutions that cause harm deserve opprobrium.

Fourth and finally, all of these antecedent matters are contested. Different philosophical and economic frameworks will and do disagree about just what events cause harm, and what effects register as harm, and as indictable harm. The concept of harm, then, must also be invariably contested. A libertarian and a utilitarian would be apt to disagree sharply about the causes and nature of harm, which harms are substantive and which are *de minimis*, and which forms of harm are ethically worrisome.[9]

The foregoing discussion carries what is, for the economist, an inconvenient implication. *Positive* analyses of the concept of harm, such as assessing when harm has occurred and measuring its extent, is thoroughly infused with *normative* judgments. We need to make normatively charged decisions about what counts as harm before we can begin to explore the supposedly positive questions whether a policy has or has not induced harm, and what is its magnitude. We then have to follow up the discovery of harm with normatively laden decisions about which of the harms we recognize are to be taken as ethically indictable or otherwise troubling, and which are not. All of this implies

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consent) to policy regimes that entail substantial risks to those who populate the economy—where the stakes for winning and losing are very high.

[9] And so would feminist, Marxist, Keynesian, social and neoclassical economists. Their respective judgments regarding harm would be driven in part by their competing conceptions about human and physical nature, and about what makes for a good economic outcome (see DeMartino 2000; thanks to Robert Lepenies for emphasizing this point in correspondence).

that as regards the matter of harm, if not everywhere else in economics, *the positive and the normative are inescapably linked.* Talk of harm is, necessarily, at once positive and normative. And it may be that the deeply normative character of the concept of harm helps to explain what is otherwise mysterious: why the economics profession has more often repressed rather than welcomed serous consideration of economic harm in general, and econogenic harm in particular.

<1>**III. The Tragedy of Economics**

The duty to engage economic harm is imposed upon us by the problematic nature of economic science and practice. Harm to those whom economists purport to serve results most obviously from error in economic judgment—such as when an economist fails to anticipate the unintended adverse consequences of a proposed economic intervention. The position taken by US Federal Reserve Chair Alan Greenspan on the need for financial regulation during the late 1990s and early 2000s qualifies, as indicated by his stunning admission before Congress in the fall of 2008 of his own naïveté in believing that liberalized financial markets would police themselves sufficiently so as to prevent irresponsible and destabilizing behavior. As the most severe economic crisis in the U.S. since the 1930s unfolded, Greenspan testified that “I made a mistake in presuming that the self-interest of organizations, specifically banks and others, was such that they were best capable of protecting their own shareholders.” Speaking of a “once in a century credit tsunami,” he continued, “[t]hose of us who have looked to the self-interest of lending institutions to protect shareholders’ equity, myself especially, are in a state of shocked disbelief” (Andrews 2008).

But Greenspan is by no means exceptional among economists in making a consequential mistake. His failure reflects a deep and likely ineradicable knowledge problem in economics. Economists operate in a world of *epistemic insufficiency*, where they largely cannot be certain of the effects of the interventions they advocate (DeMartino 2013; see also Colander 2005).[10] The effects of economic policy interventions can be extraordinarily complex and dispersed, and can extend indefinitely into the future. In this regard, economics is closer to the field of environmental science than clinical medicine or other fields that operate on smaller canvases, treating one client at a time, where the effects of an intervention are relatively localized. Environmentalists Bill Vitek and Wes Jackson (2008: 1) argue that humanity will always be "billions of times more ignorant than knowledgeable" about the physical world we inhabit. Their warning is just as apt in regard to economic phenomena. Epistemic insufficiency implies that even well-meaning and highly-skilled economists risk imposing econogenic harm when they try to promote good economic outcomes.[11]

The condition of epistemic insufficiency under which economists act entails an additional problem: economists cannot control the world in which they operate. There can be and often is substantial slippage between policy recommendation and policy effects owing to unforeseeable vagaries in policy making and implementation, and in the

[10] Nor can they be certain the effects of policies that were implemented in the past. The conclusion that a certain economic intervention generated a particular effect requires counterfactual analysis indicating what would have happened had the intervention not occurred. Presumably there are cases that involve discrete policy interventions of limited scale where the counterfactual may be fairly easy to discern. Most economic policy interventions, however, involve extensive and complex interactions—and in these cases deducing the counterfactual may be fairly impossible. This fact complicates all economic policy assessment, including the task of tracing harms back to their causes.

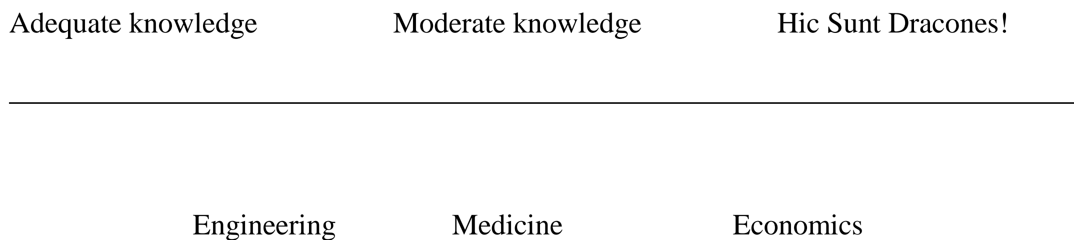
[11] Economists are by no means alone in confronting epistemic insufficiency. Philip Tetlock's study of expertise across the professions provides remarkable evidence of consistent failure. In his words, "When we pit experts against minimalist performance algorithms—dilettantes, dart-throwing chimps, and assorted extrapolation algorithms—we find few signs that expertise translates into greater ability to make either "well-calibrated" or "discriminating" forecasts" (Tetlock 2005, 20).

responses of economic agents to any policy intervention. Even in the unusual instances in which economists occupy the role of social engineer—such as arguably in the economic restructuring projects of the 1990s in countries that were transitioning away from socialism, when leading economists at the international financial institutions, government agencies, and think-tanks were able to engage in institutional design on a vast scale—economists enjoy *influence without control*. Economists sometimes wield just enough influence to be dangerous—call it the Jeffrey Sachs in Russia Problem (DeMartino 2013). Not least, the policies that economists advocate can be and often are hijacked by special interests for their own ends or are otherwise undermined in execution by unforeseen contingencies, or by the unpredictable response of the private actors populating the economy (cf. Friedman 1972). In the policy arena politics and not economic science is typically in charge. Moreover, the effects of any intervention will depend on innumerable factors about which the economist's knowledge is at best quite limited, as Hayek (1978), McCloskey (1990), and others have rightly argued. All of this implies that economic practice is fraught with uncertainty and with the risk of perhaps substantial unintended and unforeseeable harm. The image we should keep in mind when we think about the position of the economic social engineer is a ten-year old boy behind the wheel of a Hummer, careening down Main Street. Does the child have influence over what's about to happen? Absolutely. But does he enjoy control over those events? Don't bet on it—not your own livelihood, and especially not anyone else's (cf. Taleb 2012).

Harm resulting from error—or more broadly, from the imperative facing the professional to act under conditions of epistemic insufficiency, in a world that defies dependable prediction or control—is undoubtedly a universal problem in the professions.

Its salience in economics represents a difference in degree rather than in kind (see Figure 1). If we theorize a continuum from the professional fields in which ignorance is manageable and domesticable, to those where it is unmanageable and consequential, we might place basic civil engineering near the benign pole and medical practice at a middling point. In contrast, economics resides in the perilous zone, where ignorance is vast and dangerous.

Figure 1: Severity of Epistemic Insufficiency



Economists also cause harm in ways that may be (relatively) *sui generis*, at least in comparison with those professions that serve individual clients. Economic interventions generally entail disparate effects across society's members, as the Hicks quotation above indicates. It is in the nature of complex economic systems that even well-designed economic interventions almost invariably cause harm to some economic actors. Think of the standard textbook advocacy of the removal of trade barriers or price supports. In this case, which is representative of economic policy in general, some in society benefit from market liberalization while others necessarily suffer economic harm.

Economics is unlike many other professions in two relevant senses: the degree to which harm is inherent in its practice; and in the distribution of the harms it induces. In clinical medicine, for instance, serious harm typically arises from medical error or from the limits to medical knowledge of physiological and psychological processes. In economics, in contrast, harm is an inherent feature of even successful economic interventions; it can and generally does occur even when the economist gets it right. Moreover, medical harm typically afflicts only the agent whose welfare the doctor seeks to improve, and perhaps those others who are closely related to the agent and who value his welfare. No longer is it deemed acceptable in medicine to harm some for the benefit of others.[12]

In contrast economists are, inescapably, in the harm business: econogenic harm is a routine feature of economic policy implementation, even in the absence of error. Harm arises whenever a policy that may very well promote aggregate economic interests also worsens the absolute situation of some members of the economy. And if Sen (1992) is correct in arguing that severe inequality can diminish levels of welfare or agency among the poor, then we should recognize that an agent can be harmed even in the absence of a diminution in his absolute income if his relative standing declines. The relatively poor in a wealthy society might lack self-respect, social capital or political voice. While politicians often claim that their preferred economic policies benefit all of society's members, economists know better. In all but the simplest economies virtually all

[12] Though there are instances of third-party harm and harm to some for the benefit of others in the context of public health, where medical decisions affect large groups of people rather than individual patients one at a time, and where effects of interventions across the relevant population can be disparate. In part for this reason public health ethics may offer a better guide in the formation of economic ethics than does (clinical) medical ethics.

economic interventions have disparate impact, and many may induce significant harm. Helping some routinely requires hurting others—this is the tragedy of economic practice.

Taken together, the extent of epistemic insufficiency in economics and the harm-inducing nature of economic practice imply that economics faces a more urgent duty to engage the matter of harm than do other professions in which harm is not as salient a feature of professional practice. So does the fact that econogenic harms, though substantial, are often indirect, postponed, and otherwise obscured. Unlike many other professionals, economists typically don't have to confront the people who are harmed by their practice; nor are they generally aware of the extent of or held accountable for the harm (see Angner 2006; Ravallion 2009). The ethical burden associated with harm lies heavier on the shoulders of economists, then, than engineers, accountants, and even physicians.

And yet, to repeat, we find no tradition of serious inquiry within the profession into the complex nature of economic harm. What we find in the history of economic thought are fits and starts—periods such as the 1930s during which leading economists attempted to theorize carefully the ethical entailments of economic harm in the context of policy formation, and periods such as the present in which economists have "a love-hate relationship" with the predominant procedures for assessing policy that generates harm (Kanbur 2003). In general, economics treats harm too casually, perhaps out of an inchoate awareness that facing up to econogenic harm in a serious and rigorous way, attending carefully to the claims of those who will be adversely affected by economic interventions, would complicate economic practice to such a degree as to render it untenable.

<1>**IV. The Kaldor-Hicks Compensation Test**

The predominant approach to harm assessment and mitigation in economics reflects the utilitarian framework from which economics draws its normative foundations. Standard neoclassical economics carries forward the consequentialism and welfarism of classical utilitarianism. These features entail the evaluation of states of affairs by exclusive reference to the levels of welfare of the agents affected by such states.[13] Welfarism can and has been defined in neoclassical theory as levels of utility or, more frequently in recent history, the extent of preference satisfaction (where existing preferences are generally taken as valid) (Sen 1987). Unlike classical utilitarianism, however, the welfarist consequentialism of neoclassical thought does not permit cardinal measurements of utility; hence, it disallows inter-personal utility comparisons or the summation of utility levels across distinct individuals. Contemporary welfarist social assessment depends instead on the Pareto criterion or, when the conditions for Pareto comparisons are not met, on the Kaldor-Hicks potential compensation principle. Put simply, the principle states that some policy A is preferred to an alternative policy B if the winners under A can fully compensate the losers under A and still retain net benefit.

The legitimacy of Kaldor-Hicks depends on the legitimacy of a web of empirical, theoretical, and normative claims about what humans do and should value, and about the nature of the harm they suffer as a consequence of economic policies. The textbook approach to normative assessment depends on the level of each agent's welfare (defined

[13] The term "neoclassical" is used here simply to refer to the standard textbook approach to economics and, in particular, to applied economics. The term is problematic since it is imprecise in what it includes and excludes, and since economics today appears to be breaking with some of the central assumptions that guided economics through much of the 20th century. In what follows I discuss those aspects of neoclassical economic theory that are germane to the matter of how economists theorize harm.

on an ordinal scale); and tends to include as arguments in each individual's utility function only her own level of consumption of private and public goods or the satisfaction of self-regarding preferences (Sen 1987). Consider workers who are displaced by a shift in economic policy, such as the removal of tariff protection for an industry in which they work and for which the country does not enjoy a comparative advantage. In the standard textbook treatment of the problem only the loss of workers' income registers in the harm accounting. In broader formulations other harms that are associated with unemployment can be figured in, of course.[14] These might include the increased incidence of physical ailments and psychological damage among the affected workers, increased rates of suicide and crime, and declining asset values (such as housing prices) that are consequent to the policy shift. But in keeping with the utilitarian tradition such damages are treated as reducible to impacts on workers' welfare. Moreover, the diverse contributors to workers' levels of welfare are taken to be *comparable* and fungible. The assumption of substitutability among arguments is nearly universal within standard utility functions (and within models of preference satisfaction). Such features of neoclassical thought imply that the damages are taken to be fully *commensurable* with each other and with a sum of money, which in turn permits the conclusion that the damages are fully *compensable* through monetary transfers. Indeed, under the predominant welfarist approach any welfare loss may be fully offset through monetary compensation. Full compensation simply requires finding the appropriate magnitude of

[14] This is the norm in cost-benefit analysis, where various effects of alternative policy interventions can be and are factored into policy assessment, such as through the use of contingent valuation, but typically only as determinants of individuals' levels of welfare. For the purposes of this essay it suffices to treat cost-benefit analysis as a means to operationalize the Kaldor-Hicks decision rule, and so I do not explore cost-benefit analysis separately here. A fuller treatment would need to examine carefully their salient practical, technical and normative differences (see Boadway 1974; Adler and Posner 2006).

monetary transfer that will restore the displaced worker to his previous level of welfare. If full compensation is made, then the worker is taken to suffer no harm from the loss of employment—indeed, she is theorized as indifferent between her pre- and post-unemployment situations since full compensation implies that she has been made whole following the loss of her job.

Unlike the Pareto criterion, the usefulness of which in economic application is limited owing to conflicting preferences across people concerning possible social states, Kaldor-Hicks is taken to provide a tractable framework for reaching unequivocal judgments on economic policy decisions that entail harm. In Hicks' words, there is

> a perfectly *objective* test which enables us to discriminate between those reorganisations which improve productive efficiency and those which do not. If *A* is made so much better off by the change that he could compensate *B* for his loss, and still have something left over, then the reorganisation is an unequivocal improvement. (Hicks 1941, 111, emphasis added)

The Kaldor-Hicks potential compensation test appears to provide economists with a wonderfully elegant decision rule. The policy is preferred that is Kaldor-Hicks efficient.[15] Kaldor-Hicks seems to imply an appropriate standard that is only minimally normative for the applied economist. The economist should advocate policy interventions that pass the Kaldor-Hicks compensation test, and refrain from advocating policies that

[15] But see Scitovsky (1941), which demonstrates that Kaldor-Hicks assessments of policy options can yield indeterminate results. See also Little (1957, 93), who argues that Kaldor-Hicks is not a criterion or test of alternative social states at all, but is rather a value-laden definition of "increased general economic welfare."

fail it. On this basis, for instance, economists typically preach the desirability of free trade. In Hicks' own view, "this criterion is more useful than any other as a basis on which to establish maxims of sound economic policy" (ibid, 111). With Hicks, many economists believe themselves to be warranted in advocating policies that induce even substantial harm to some in order to augment aggregate welfare (cf. Kanbur 2003). Indeed, they do it every day.

<1>**V. Inadequacies of Kaldor-Hicks**

Kaldor-Hicks raises several issues that pertain to harm, some of which have been long debated among economists.[16] One well-worn controversy concerns whether *potential* compensation is sufficient to warrant a policy intervention—or whether, as a condition for the economist's support, the losers under a Kaldor-Hicks efficient policy intervention must *actually receive* full compensation for their losses.[17] Hicks and Kaldor thought that potential compensation was generally sufficient; most economists follow their lead. In contrast, Amartya Sen (1987) ridicules the idea that potential compensation provides adequate justification, especially for a policy that benefits the rich but harms the poor. The eminent free trader, Jagdish Bhagwati, concurs:

> Sometimes I wonder whether the younger economists today are taught what Ian Little taught us—that it is not enough that there be potential compensation;

[16] Several controversies surround the use of Kaldor-Hicks that I will not examine here. Marxian, Austrian and other heterodox traditions largely reject the Kaldor-Hicks test—in part owing to their appreciation of the endogeneity of preference (and subjectivity) formation. See, for instance, Stringham (2001) for an Austrian critique of the use of Kaldor-Hicks in the judicial setting. See also Scitovsky (1941) and Sen (1979) for critiques that have emerged within the tradition of welfare economics.

[17] We postpone for just a moment the questions whether all harms are in fact compensable.

compensation must actually be made. Otherwise, imagine a situation where the rich can compensate the poor while still getting richer, yet they do not. Surely, no people in their right minds, or certainly in their true hearts, would approve of the policy change, in that event" (1994, 21).[18]

In fact, full compensation rarely occurs, as Hicks understood (1939, 711). Absent actual compensation, Kaldor-Hicks policy adjustments generate anticipated harm (in comparison with the *ex ante* state of affairs) where the harm is in principle avoidable by foregoing the adjustment.[19] And yet economists tend not to think through carefully what might be their obligations to those who populate the economy when their practice routinely induces foreseeable, avoidable harm.

A second matter ought to be equally controversial, though economists to date have not given it the attention it is due. Are economists warranted in advocating all policy options that pass the Kaldor-Hicks test, irrespective of the matter of compensation, or are there deontological (or other) limits on the policies that they should support? And if there are such limits, what are they?

A comparison with the field of medical practice might help to elucidate what is so disconcerting about the economist's reflexive embrace of the Kaldor-Hicks test when

[18] Bhagwati notes, however, that in practice compensating each victim of every policy change is infeasible. He advocates instead for a general safety net as a means to ensure compensation. See also Kanbur (2003, 32), who calls for automatic redistribution mechanisms and safety nets "to complement project-specific compensation."

[19] It can plausibly be argued, of course, that *not* implementing Kaldor-Hicks efficient policy also causes harm to those who would benefit from the state of affairs that the policy would yield. Hence Kaldor-Hicks policy assessment requires a careful engagement with the ethical standing of competing claims—of those who would suffer relative to their current situation were the policy to be implemented; and those who would suffer relative to their potential situation were the status quo to be preserved when an alternative state of affairs that benefits them is available.

adjudicating policy that causes harm. Is a physician warranted in causing harm to some to benefit others? For instance, is a physician warranted in corralling together, in an isolation unit, those who have been exposed to a dangerous pathogen during an epidemic, but who are as of yet asymptomatic, so as to reduce the risk of infection to the general public? Doing so might be taken to violate important rights (to mobility; to protecting and caring for oneself as one sees fit), and may also place the isolated individuals at greater risk of illness and even death than if they were free to migrate away from the diseased site. Is it ethically appropriate for the medical profession to impose quarantines, then? Many of us—and certainly most economists—would answer in the affirmative. In this case we tend to think it right (though surely regrettable) to impose potentially severe harms on some for the greater benefit of the broader population.

But now consider an alternative case: is it ethically appropriate for a physician to snatch a healthy individual off the street in order to harvest organs from him, killing him in the process, in order to improve or perhaps even save the lives of many others? Less dramatically, is the physician warranted in merely extracting a kidney from the unwilling donor—a procedure that the donor will likely survive, and that is certain to save the life of another? Most of us would reject the legitimacy of organ snatching, whether or not compensation is paid, viewing the practice as an egregious violation of personal autonomy. We should take note, however, that harvesting body parts against the will of the donor is consistent with the utilitarian logic underlying J.J.C. Smart's claim that appears as the epigraph to this essay; and under standard economic assumptions it is likely to meet the conditions set forth in the Kaldor-Hicks compensation test. Does that fact make it a commendable policy?

The side-by-side consideration of the two similar cases suggests the difficult question: just what is the ethically salient difference between them? *Is there one*? Both cases involve harming some severely and against their will to benefit others—potentially many others. Yet, we intuit some sort of compelling ethical difference.[20] Asking the question, just what is the difference, requires us to pause and think. And that moment of hesitation, in which we reflect carefully about which harms physicians can and can't impose on some for the benefit of others, gives us reason for hope for ethical medical practice.

In contrast, economists do not tend to hesitate. We are trained to apply Kaldor-Hicks instinctively whenever we face policy disputes even when substantial harms will follow from the policy option that meets the test. In so doing we fail to inquire whether the imposition of harms is appropriate. In possession of Kaldor-Hicks economists do not typically ask themselves whether the cases they confront are the economic analogues to medical quarantines, or to involuntary organ snatching. Instead, we make the error of reducing complex ethical judgment to what Radest (1997) calls "moral geometry," imposing a simplistic, mechanical formula where nothing less than deep, nuanced and careful consideration will do. In possession of the convenient decision rule that Kaldor-

[20] One is that those who have been exposed to a pathogen during an epidemic represent "innocent threats" to others, while unwilling organ donors do not. This consideration weighs in favor of coercion in the case of epidemics but not in the case of organ transfers. Analogizing to economic cases, those harmed by an economic policy shift (such as trade liberalization) do not generally represent a threat to others (in the common sense of the term "threat"): they occupy the position of unwilling organ donors rather than potential transmitters of disease. Hence, the innocent threat rationale cannot be used to sustain the harm that is imposed on them. See Nozick (1974) for a provocative though ultimately incomplete discussion of the ethics surrounding the treatment of innocent threats.

A possible response appears in the previous footnote, of course. It can be argued that the beneficiaries of trade restrictions do pose a threat to the welfare of those who stand to benefit from trade liberalization. But then the reverse is also true: the beneficiaries of trade liberalization pose a threat to the welfare of those who benefit from trade restrictions.

Hicks provides economists are seduced into treating individuals merely as means and not also as ends. Kant would despair at the state of ethical thought in the profession.

<2> *The Contractarian Defense of Potential Compensation*

The most compelling defense of potential as opposed to actual compensation to those harmed by an economic policy initiative warrants close attention. There is a strong contractarian case to be made for potential compensation under Kaldor-Hicks—it is that we all benefit by, and therefore have good reason to support, constitutional arrangements that encourage social innovation that promotes rising incomes even if each of those innovations risk harm to some members of society. This is a claim of the generalized benefits of efficiency: since we are all beneficiaries of a system that generates efficiency-inducing innovations, the harm that befalls any one of us from any particular innovation is ethically benign. Demanding actual, immediate compensation in those particular instances where one is hurt would amount to "double-dipping" since each of us is already compensated in the long run for the risk of harm we bear through the diffused benefits of innovation. The contractarian argument presumes hypothetical approval by all of us (or by our idealized representatives, operating behind a Rawlsian veil of ignorance) of an economic system that will necessarily harm members without compensation—not for the greater good of the greatest number, as a utilitarian would have it, but ultimately for the greater good of each and every one of us. The contractarian defense of potential as opposed to actual contribution is most securely grounded, then, in Pareto rather than Bentham (cf. Adler and Posner 1999; Polinsky 1972).[21]

[21] Polinsky (1972, 409) writes,

Does this argument satisfy as a defense of an economic system that permits non-compensated, Kaldor-Hicks consistent policy adjustments? That would depend in part on the nature of the harms that are associated with successive innovations, and whether they are serially independent and relatively small in comparison with the associated benefits (Kanbur 2003). If, for instance, today's winners are just as likely as today's losers to be tomorrow's losers, and vice versa, and if each of the successive harms is relatively minor (in a qualitative or quantitative sense) so that they are likely to be cancelled out by a series of prior or subsequent benefits, then each of us may be expected to be a winner over time. If these conditions hold, and if the system on balance produces more socially beneficial innovations than alternative systems that entail less risk of harm, then there is a reasonable basis for inferring hypothetical or tacit consent by rational actors to an arrangement that casts each of us occasionally in the role of loser (see Posner 1980; and Coleman 1980).

Several objections have been and can be offered to the contractarian defense of non-compensation for actual harms, however. One is that some economic innovations entail harms to agents from which they may never recover—either because of the qualitative nature of the harm (about which, more below), or its magnitude. This is the case, for instance, in large-scale development projects (like dam construction) that entail

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> By broadening the notion of compensation to include bundles of changes that have some effective randomness in distribution, it thereby becomes possible to leave particular individuals uncompensated and worse off for single changes, yet assure them that they can (mathematically) expect to be better off as a result of the entire bundle (with the probability of actually being made worse off set at a value approaching zero).

McCloskey (2010) points out that the rule utilitarian tradition that runs from Mill and Sidgwick through Harsanyi, Buchanan, Tullock and Rawls establishes a compelling case for the legitimacy of a constitution to govern economic interactions that permits uncompensated harms that yield generalized economic improvement. Also see Hicks (1939, 711-12; emphasis in original) where he summarizes the "hard-boiled attitude" of economists, which is "to reject all compensation on the ground that such risks *ought* to have been allowed for…" If this line of argument is correct, then Kantian concerns evaporate.

the forced relocation of large numbers of people (Kanbur 2003); or social engineering schemes that fundamentally alter a society's basic economic institutions. In cases like this, where the nature, depth and extent of harm is such that the losers will never recover, economists cannot take normative cover in the contractarian defense of Kaldor-Hicks for the proposed policy, absent actual compensation, no matter the size of the aggregate welfare gains. A second objection is that, away from the blackboard and in real economies, the incidence of gains and losses tends to be serially correlated (cf. Adler and Posner 1999). Being a loser today is correlated with having been a loser yesterday, and with being a loser yet again tomorrow. The likelihood of correlation follows from the obvious fact that those with the greatest economic power and political influence are often in position to secure from among the set of available policy options those interventions that reflect their own, particular and immediate interests; and that, even if they refrain from exercising their influence to bias policy, they are typically in much better position than others to insure themselves against the harms that occasionally befall them.[22] This is not to deny that even the losers may secure some benefits from harm-inducing innovations. Workers who lose careers, status, income and wealth owing to the shift to a free trade regime may take advantage of lower consumer prices at Walmart, for instance. It is to claim that a system that concentrates harms among some for the ultimate benefit of others is fundamentally unjust. It cannot be presumed to enjoy the universal tacit consent of rational Rawlsian deliberators, let alone actual economic agents.

[22] A Chicago school economist (but a friend nonetheless) replies: "But you know how I will answer this, in all seriousness and truth: fix the distribution of income and especially wealth directly. Don't use the price system to do the job!" The objection has merit. Perhaps in a world with a fair distribution of income and wealth and where individuals enjoy relatively equal political efficacy, application of Kaldor-Hicks would be far less apt to penalize some routinely and severely for the benefit of others. Perhaps in *that* world, potential as opposed to actual compensation might suffice. Can we agree, then, to postpone reliance on Kaldor-Hicks (or at least refuse to take refuge in the contractarian defense of the decision rule) until that world is realized?

<2> ***Compensable vs. Non-Compensable Harm***

The welfarist approach underlying Kaldor-Hicks tends to overlook conceptual distinctions that figure prominently in serious investigations of harm beyond economics, and that ought to be engaged in analyses of economic harm.[23] One set of relevant issues (discussed above), which has been largely papered over in the consequentialist welfarism of neoclassical thought, is perhaps most important and also most difficult for economists to manage. It concerns the question whether all goods are to be theorized as *commensurable* and *substitutable*, and whether all harms are viewed as *reparable* and, hence, *compensable*. The four concepts are related, but distinct (see Figure 2).

Figure 2: Compensable vs. Non-Compensable Harm

	Reparable Harm	Irreparable Harm
Commensurable, Substitutable Goods	Compensable Harm	Undefined
Incommensurable, Non-Substitutable Goods	Non-Compensable Harm: - Apology, Recognition, Honor	Non-Compensable Harm: - Remedial Measures Unavailable or Inadequate

[23] A fuller treatment than is possible here would require examination of other harm-related conceptual distinctions that are sidestepped under the Kaldor-Hicks compensation test. Relevant distinctions include *inter alia* that between direct and indirect harm (McIntyre 2011); doing and allowing harm (Howard-Snyder 2008); and positive and negative harm (Friedman 1962).

Neoclassical thought encompasses welfare commensurability across all goods—rational agents are able and willing to make welfare comparisons across all commodity bundles that include diverse goods. Moreover, neoclassical theory holds to a notion of complete substitutability across goods. Harm is then defined as a reduction in the level of welfare that follows from the diminution in one or more goods that agents value. Commensurability and substitutability across goods imply that agents who suffer harm from the loss of one good can remain at the same level of well-being—and hence, be rendered whole—through increased consumption of other goods. This claim implies in turn that all harms are reparable through adequate compensation, generally theorized as monetary transfers. In this vision, all harms fall into the upper-left hand cell of Figure 2.

Absent commensurability and complete substitutability, and in the presence of irreparability, the compensation at the heart of Kaldor-Hicks would fail to make a harmed agent whole (lower-right cell). Alternatively, though some harms may prove to be non-compensable in the sense that transfer payments cannot suffice to render the harmed person whole owing to the fact that the lost goods are incommensurable and non-substitutable, the harms might be repaired (wholly or in part) through other, *non-compensatory* acts by individuals or society.[24] Socially sanctioned apology or recognition for one's loss—as sometimes attends the processes of truth-telling commissions in post-conflict situations—may serve to heal the harmed agent in ways that attempted compensation might not. Moreover, harms suffered in the line of duty (e.g., by first responders to crises) or in public service more generally might also warrant the provision

[24] It is perhaps more accurate to distinguish between harms that are largely reparable, and those that are largely irreparable. Apology, recognition and/or honor might be appropriate for all such harms, though the extent to which they ameliorate the harm would vary across cases.

of public honors. Sometimes, of course, transfer payments may occur in the context of apology, recognition, or honor; indeed, apology, recognition or honor might even manifest as a monetary transfer. The "sorry money" that is paid in New Guinea, as exemplified in a story recounted by Jared Diamond (2012), is illustrative. In the wake of a traffic accident that kills a child but where the truck driver is exonerated of any wrongdoing, a relatively wealthy truck company owner gives money to the parents and says to them, "This money is nothing compared to your son's life, but I give it to show how sorry we are." The simple example highlights the necessity of deciphering the social function of monetary transfers in instances of harm. Money transfers can carry diverse meanings that depend on the identities of the giver and receiver, and on the purpose and context. It is an elementary mistake to presume with the economist that all transfers represent monetary compensation that has the capacity to render the harmed agent whole.

In her examination of bourgeois virtues (where she recounts and comments critically on Diamond's analysis of sorry money), McCloskey discusses approvingly an historical trend in the Germanic north of Europe to commercialize disputes over injury or harm that might otherwise generate social conflict and disrupt economic progress. In place of honor-based, eye-for-eye justice, "Germanic law codes of early times encourage *cash* compensation for dishonor" (McCloskey, forthcoming). Payment for wrongs in the form of "wergelt," which became the norm in northern Europe, helped to curtail costly feuds that otherwise might have disrupted commerce. In contrast, in the supposedly more advanced and mercantile south, a more primitive approach to justice survived. "[F]rom Homer to El Cid to *The Godfather*, honor is absolute" and wrongs are righted through

altogether non-bourgeois forms of retribution that could and did disturb economic advancement."

A distinction needs to be drawn, however, between the bourgeois view of compensation that McCloskey recommends and the modern neoclassical view. Commercialization of harms need not presume that all harms are reparable and compensable. The virtue of payment (in coins, cattle and other goods, as was common under Germanic codes) for harms can reside in its *instrumental effects*—keeping the peace, incentivizing and sustaining beneficial commerce, and promoting economic advance. The idea that those who harm must make amends in ways that are consistent with the social interest bears no likeness at all to the naïve, modern economic treatment of all harms as reparable and, indeed, compensable. They are not: just ask the parents who are awarded damages for the wrongful death of a child whether they are indifferent between having their child, and having the money. The economist's mistake, and it is an egregious one, lies in subsuming all instances of transfer under the category of *compensation for reparable harms*—and in believing further that after compensation has been paid, the harm has been fully offset.

Sorry money and non-monetary apology, recognition and honor all reflect an awareness of a truth that economists have long repressed: all harms are not created equal, and all are not compensable.[25] A cursory review of the taxonomy given in Table 1 suggests that it is irresponsible to presume that all harms are reparable. Some rights violations, for instance, are generally viewed as too precious to repair, after the fact, with

[25] It should be said that forensic economists and many in the field of law and economics tend to be far more careful in their judgments about the nature and complexity of harm, perhaps because the concept of irreparable harm is well established (though also contested) in the judicial setting. See, for instance, Keating (2003)

compensation (see below; Rendleman 2002). Alternatively, some harms, such as being dishonored, are not amenable to compensation at all: “Once lost, honor is extraordinarily hard, if not impossible, to regain… the very idea of [pricing honor] seems inconsistent with the concept (McGowan 2010, 589; 591).[26] It is therefore unfortunate that the standard economic assumptions regarding commensurability, substitutability, and reparability facilitate reliance on a convenient but simple-minded decision rule where nothing less than careful, difficult deliberation is required. The strategy of *presuming what should be explicitly investigated* suits the needs of economists in their pursuit of policy influence far more than the interests of those whom economists purport to serve.

Permanent damage to one’s psychological or physical health, social standing, autonomy, and basic freedoms do not lend themselves to full repair—and certainly not by monetary compensation. But then, which harms are reparable and which are not; which reparable harms are compensable and which are not; which compensable harms should be compensated, and which should not; what is to be done when economic interventions potentially threaten or actually do cause irreparable harm; and what authority should the economist have in answering these questions? One looks to the economic tradition in vain for careful investigation of these vexing questions.

<2>***Rights Violations***

[26] Kaldor (1939, 551) recognized that economic policies could induce “losses of a non-pecuniary kind,” such as when “workers derive satisfaction from their particular kind of work, and are obliged to change their employment,” or when “individuals feel that the carrying out of the policy involves an interference with their individual freedom.” But Kaldor did not treat non-pecuniary harms as irreparable or non-compensable. Instead, he concluded simply that in such cases “something more than their previous level of money income will be necessary to secure their previous level of enjoyment.” Unfortunately, the economics profession largely followed Kaldor in trivializing non-pecuniary harms by simply reducing it to a coefficient (greater than one) that is applied to lost income.

There is a fundamentally important and ethically salient distinction to be drawn between those social innovations that occur without violating people's rights, and those that do. The work of Nozick (1974) is illustrative in this regard. Nozick's libertarianism is founded upon a "side-constraint" view of rights that holds that no individual (or institution) may violate the rights of another in order to achieve what one takes to be a higher order social goal (such as economic efficiency). Indeed, the side-constraint approach holds that one may not violate another's rights even when the purpose of so doing is to minimize rights violations in the aggregate. Rights are taken instead to be inviolable constraints on how we act toward each other, and on how the institutions we create (such as corporations and the state) treat each of society's members.

From Nozick's perspective actions by the state that promote Kaldor-Hicks efficiency but that entail the violation of rights are ethically indictable despite their beneficial economic consequences for others or even for those agents whose rights are violated (cf. Friedman1962). A notable example is the takings associated with eminent domain—or the forced relocation that attends large development projects—whereby a government appropriates private property (or terminates communal access to common property) for "public" purposes. Harm appears here not just in the form of a loss of income or property, but in the deeper Kantian sense of a rights violation (which may or may not cause a loss of income) that treats some persons merely as means. In libertarian and other rights-based frameworks violations of this sort cannot be offset with potential compensation or with the promise of the higher net income in the long run that results from the action that caused the rights violation.[27] Nor can they be easily justified with a

[27] Nozick's framework demands restitution for those whose rights have been violated, to be sure, and so it might seem that rights violations can be compensated for unproblematically via transfer payments. But in

contractarian claim of potential or tacit acceptance at the constitutional level of a regime that routinely violates rights. From this perspective, there must be an explicit agreement among each of society's members to live under an arrangement that distributes harms and benefits without attention in each case to rights; or, failing that unanimity, each policy innovation must be probed to ensure that it does not violate anyone's rights. Only an *actual* voluntary bargain between an economic actor and the state (where, for instance, the agent willingly agrees to sell property to the state) resolves the normative problem, since in that case there is no rights violation. Short of that kind of explicit bargain, Kaldor-Hicks efficient policy may very well entail substantial harm in the form of a rights transgression that Kaldor-Hicks cannot begin to theorize properly, validate, or compensate. [28]

<2>***On Inequality***[29]

In application, when undertaking Kaldor-Hicks computations only agents' absolute losses and gains typically register in the economist's ledger. Absent here is concern for economic inequality since a policy that increases inequality is just as apt to pass the Kaldor-Hicks compensation test as a policy that has the opposite effect. Indeed,

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the Nozickean framework it is important to keep in view the distinction between the *economic consequences* of the rights violation, which can in principle be rectified, and the rights violation itself. It is not the case that the victim of a rights violation who has secured restitution for his/her economic losses is made whole. Were that the case, Nozick's side constraint approach to rights would evaporate since all transgressions would be permitted provided compensation is paid, after the fact. I thank Eugenia Goh and Patrick Sutherland for conversation that clarified for me this distinction.

[28] Like libertarianism, the rights-focused capabilities approach to equality and development (as freedom) of Sen (1992; 2000), Nussbaum (1992) and others also rejects the presumption that all harms are reparable and compensable. Capabilities scholars argue that the diverse beings and doings (or functionings) that people have reason to value are not necessarily commensurable and substitutable. Harm that takes the form of a diminution in one functionings domain—such as loss of self respect or social standing—cannot be fully offset by increased performance in other domains—such as improved personal welfare. To live in a gilded cage is still to be enslaved, and the trappings of luxury in such a case cannot compensate for the loss of freedom that it entails.

[29] A comprehensive treatment of economic harm would require a careful investigation of the matter of inequality. Here I restrict myself to a few points that relate most directly to Kaldor-Hicks.

the Kaldor-Hicks criterion is agnostic in regards to inequality. Applied economists typically ignore the question whether increasing inequality in itself might harm the losers from a policy shift, beyond the harm suffered by an absolute decline in their incomes. Hence, it is also ignored in calculating full compensation.[30] But economic inequality may induce all manner of harms, as countless theorists from Marx and Veblen to Sen and Stiglitz have by now argued at length.[31]

Kanbur (2003) notes that equality-minded economists can and do incorporate egalitarian considerations into Kaldor-Hicks assessments by weighting the losses and gains to the poor more heavily than losses or gains to the wealthy. On its face, the weighting procedure registers an appropriate concern for fairness by disqualifying some policy initiatives that favor the rich over the poor. But it does not disallow any policies that increase inequality per se, even egregiously, provided the absolute position of the poor does not deteriorate. Moreover, among the set of policies that harm the poor in absolute terms while also worsening inequality, the application of an egalitarian system of weights to gains and losses yields a bias for policies that do the most to worsen income inequality. Consider the two policy options in Figure 3, each of which benefits the rich but harms the poor:

Figure 3: Kaldor-Hicks Test with Egalitarian Weights

Policy 1 ***Policy 2***

[30] Utility functions are generally (though not necessarily) defined in ways that rule out "envious" preferences.

[31] Not all economists share the view that inequality causes harm, of course. Many economists would view the connection between economic inequality and social problems like failed schools, racially-biased incarceration policies and the like as contingent rather than necessary. Moreover, some economists argue that inequality entails important economic and political benefits (see Friedman 1962; Mankiw 2013).

Gains to the Rich:	2	Gains to the Rich:	20
Losses to the Poor:	1	Losses to the Poor:	1

Both policies meet the conditions of Kaldor-Hicks, since the gains to the winners more than offset the losses to the losers. If we impose egalitarian weights in which the losses to the poor are multiplied by a factor of three, then policy 1, which generates just a small increase in inequality, no longer passes muster. In contrast policy 2, which substantially exacerbates inequality, would be deemed acceptable (and indeed, wonderful). The example demonstrates the difficulty of reconciling Kaldor-Hicks with egalitarian concerns, and especially with the view that relative inequality (above some threshold) is itself pernicious.

<1>**VI. Conclusion**

Economists cause harm. Econogenic harm can be predictable, preventable, direct, immediate, and visible; but it can also be unpredictable, unpreventable, indirect, postponed, and largely invisible. The harm can be massive; and it can routinely affect those who can least afford to bear it. And yet, economists strive to do good, in part by theorizing and advocating policies that promise to eradicate suffering, promote prosperity and freedom, and achieve a range of other valued social goods and outcomes.

Recognition of the ubiquity of econogenic harm does not imply that economists should withdraw from the field of public policy. Not acting, too, causes harm—some of which might be substantial, avoidable and irreparable. *Causing harm while answering the call to do good: that is the inescapable tragedy of economic practice.* And yet, the

economics profession has largely failed to wrestle with the complex nature of harm, investigate the pervasiveness and depth of econogenic harm, and explore carefully and openly their duties to those they purport to help, but so often also damage.

The underlying assumptions and welfare consequentialism of neoclassical theory have served as enablers for those looking to repress serious consideration of harm. Not least, neoclassical theory holds an account of the commensurability of all goods based on their respective contributions to welfare; a narrow conception of harm as the diminution in agents' access to goods that they value; and a contentious premise regarding the substitutability among goods that implies the reparability of harm. Commensurability, substitutability and reparability ensure that any harm can be fully offset via monetary compensation. In turn, the Kaldor-Hicks compensation test provides immense service to the economics profession by facilitating economists' influence in the always ethically charged field of policy formation while relieving them of the ethical burdens associated with even severe econogenic harm. Kaldor-Hicks is taken as a technical tool that can solve ethical problems all the while ignoring the fact, as McCloskey (2005) might say, that ethical judgment "does not inhere in a number."

A wide and largely unexplored terrain of inquiry into the nature of harm in general and econogenic harm in particular awaits those economists who are prepared to make even minor departures from neoclassical theory's standard assumption set, welfarist normative framework, and decision rules. The terrain comprises both positive and normative questions, and their necessary interdependence. The prospect of a new field of inquiry in econogenesis, nested as it should be in a broader field of professional economic ethics, is unsettling, to be sure. There is the risk that it could generate

professional paralysis in a world that is badly in need of economists' interventions. But it is imperative, despite the risks. A profession that is in the harm business—routinely generating substantial harm as a necessary byproduct of its efforts to promote the social good—has a deep, inescapable obligation to examine the nature of that harm, and the ethical burdens that attend it.

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