PERSONALLY SPEAKING

Number 33 April 2007

JUSTICE, LAWYERS, AND ECONOMIC EXCHANGE

Edward J. O'Boyle, Ph. D.
Mayo Research Institute

In addressing the decision-making process regarding economic affairs, mainstream economics draws attention to the cost -- known as opportunity cost -- of whatever the economic agent cannot do or cannot have when he/she makes a decision even in those cases where the agent is not explicitly aware of this cost. To illustrate, the opportunity cost when a producer decides to use barley to produce coffee is that the same barley cannot be used to produce whiskey.

Without dismissing the importance of opportunity cost, personalist economics is more inclined to look at the decision-making process in terms of its ethical dimensions. There are many instances, for sure, when the choices made are ethically neutral. For example, the decision to paint the exterior of one's house with white paint versus some other color has no ethical content. That is, one color is not morally right and another morally wrong. However, the decision as to what you should pay a person to work for you very likely has an ethical dimension. Thus, deliberately withholding the pay until the work has been completed and paying the worker less than what was agreed to is unethical even though the work was done to your exact specifications.

Are decisions regarding ethical issues in economic affairs entirely arbitrary, depending completely on the whims, fancies, feelings, opinions, attitudes, and values of the persons making those decisions? Or, are there objective standards that apply in economic affairs rendering ethical decision-making reasoned, defensible, and alike from one person to the next except in extenuating circumstances? Overwhelmingly mainstream economics argues that ethical standards are essentially relative, that they differ from one person to the next, and therefore are outside the limits of legitimate inquiry for economic science. Moreover, the market system sorts out all conflicts between economic agents including ethical disputes and for that reason there is no need to concern ourselves with ethics and ethical issues.

Our view is that there are certain objective ethical standards to be applied in economic affairs, and that those standards originate ultimately in the human experience. Thus, shoplifting is destructive of retail trade because clearly it is unreasonable to expect a shopkeeper to operate his/her store when customers are entirely free to take whatever they want from the shelves and exit the store without paying. Indeed, not punishing the shoplifter assures that few if anyone would be so foolish as to become a merchant and expect to earn a living. To teach and reinforce the ban on shoplifting, it is necessary to have laws and enforcement officers to assure that shoplifting is punished.

To address the lawyer's role in economic exchange which includes finding remedies for failures or breakdowns in exchange due to human imperfection,[1] it is best to begin by defining justice. **Justice is the**

---

[1] Failure or breakdown in exchange can lead to a tort. The cost of the tort system in the United States in 2005 was estimated at $261 billion or 2.1 percent of GDP. See Tillinghast's *2006 Update on U.S. Tort Cost Trends.*

virtue of rendering to another that which is owed. More specifically, in economic affairs justice is expressed in terms of three principles: equivalence, distributive justice, and contributive justice. There are just three principles of economic justice because there are only three modes of human interaction in economic affairs: person to person, superior to subordinate, and member to group. Equivalence sets forth the duty of buyer to seller in the marketplace and worker and employer in the workplace. Distributive justice defines the duties of the superior to his/her subordinates whether that interaction takes place in the marketplace or workplace. Contributive justice sets down the duties of the member to the group in interactions occurring in the workplace or marketplace.

Economic Gain: Profits, Consumer Surplus, and Economic Rent. Before moving on to the principle of equivalence, it is instructive to address first what happens in a market exchange. Every exchange involving economic agents who are well-informed and free to act entails gain for the parties involved: what is gotten in the exchange is more highly valued than what is given up. To illustrate, a person shopping for shoes finds a pair priced at $118. In deciding to purchase the shoes that person asks ‘Are they worth $118 to me?’ If the answer is affirmative, he/she buys the shoes. If the answer is negative, he/she turns away. If that person is not sure, he/she turns away but may return later to buy the shoes provided they are worth the $118 that must be given up to acquire them. In a complicated transaction such as the purchase or sale of property in which mineral rights are involved the buyer or seller might consult with a lawyer to assure that he/she is well-informed as to precisely what is gotten and what is given up.

As with mainstream economics, personalist economics differentiates between exchange value and use value. Exchange value is what is given up for the good or service acquired through exchange. Use value is what is gotten, that is the usefulness of the good or service to the person who acquires it.

Under competitive market conditions, exchange value should not vary from one person to the next. The price paid for the same dog food in a supermarket is the same for everyone buying that brand of dog food there. However, use value is not the same for everyone who buys that dog food because some persons are more deeply attached to their dogs and derive greater pleasure from feeding and caring for them than do others. While exchange value is determined by market conditions at the time and place of the exchange, use value is determined by the value systems of the uniquely different persons involved in the exchange. Exchange value is an objective piece of information. Use value, on the other hand, is a subjective human experience. For every one of the persons involved, use value (what is gotten) must be greater than exchange value (what is given up).

Without that gain, the exchange cannot be carried out. However, without a limit to that gain and its origins, some persons are able to take more than their due while others are left with less. Mainstream economics brushes aside the problem of exploitation and victimization with the invisible hand argument: every economic agent in the pursuit of his/her own self-interest serves the good of all through the invisible hand of the market. Introducing justice is unnecessary and threatens the value-free nature of mainstream economics. Personalist economics rejects the invisible hand on grounds that its appeal to magic and rhetoric is no substitute for a call to reason and substance. Personalist economics accepts a value-laden economics as the price for aligning economics more closely with economic reality.

In the workplace, for example, when the baker hires a sales clerk to tend to his/her customers, there is gain for both parties. The baker gets the clerk’s labor services that are more useful to him/her than the wages that must be paid, thereby adding to the baker’s profits. Without that gain, the baker could not afford to hire the sales clerk. At the same time, the clerk contributes his/her labor services because the wages paid are more useful than the time and effort involved in working. Without that gain (known among economists as economic rent) the clerk would not accept the job.

The gain to the worker or the owner of natural resources that are used in the production process may be enhanced further by the generous employer/producer who pays more (adds more to economic rent) than is absolutely required perhaps in the expectation that his/her generosity will be repaid by more diligent workers and more careful suppliers, thereby adding to the employer's profits. The model employee or supplier is one who contributes more to profits than is normally expected.

In the marketplace, the baker produces more loaves of bread than can be used for his/her own personal consumption, and sells them provided what is gotten (the price paid by the customer) is greater than what is given up (the bread itself, specifically the cost to produce the bread), thereby adding to the baker's profits. Without that gain, there is no incentive for the baker to produce and sell bread. At the same time, the baker's customer who does not bake bread, or does not make it as well or as inexpensively, buys from the baker because the bread that is gotten is more useful than the money given up. The gain achieved by the consumer (consumer surplus) can be saved or applied to buying other things that the customer wants or needs. A bargain is an exchange in which the consumer's gain is greater than initially expected.

Thus, profits flow from two sources because the producer engages in exchange in two markets each yielding its own gain. There is (1) the gain that comes from the producer's buying inputs in the resource market for use in the production process, and (2) the gain that derives from selling the finished goods in the product market. Thus the producer's profits are enhanced in two fundamental ways: by reducing the cost of production and by selling finished products at a higher price.

However, regarding economic rent and consumer surplus, the gain originates in exchange that takes place in a single market. For the worker and the owner of natural resources, economic rent originates in exchange in the resource market. For the consumer, it is exchange in the product market that gives rise to consumer surplus. Though the language used in mainstream economics for these gains -- profits, economic rent, and consumer surplus -- suggests that they are incidental to the exchange process, the hard reality is that all three are necessary to that process. In their absence, exchange tends to break down.

Nevertheless, there must be limits to profits, consumer surplus, and economic rent in order to prevent one party from taking advantage of another and to assure that market exchange serves all economic agents fairly and effectively and not just those with the power and will to turn gain into excess. Later on we will see more specifically that those limits are grounded in the duties that economic agents owe one another under the three principles of economic justice. Whenever agents fail in those duties remedies are available through litigation. The faithful practice of justice, in other words, prevents the ill-gotten gain. Litigation, on the other hand, compensates for ill-gotten gain. In a perfect world, litigation would not be necessary. The extensive use of litigation bears witness that the invisible hand does not sort out all conflicts because economic agents are not perfect human beings.

Equivalence. The principle of equivalence states that buyer and seller in the marketplace and worker and employer in the workplace have two duties that are binding on both parties: to exchange things of equal value and to impose equal burdens on one another. In many such transactions, personal experience informs us as to what equal value means. By equal burden we mean that the burden of the seller is to give up possession of the good or service in question. For the buyer, the burden is to give up possession of the money necessary to buy and take possession of that good or service. For the worker, the burden is performing the work required by the employer. For the employer, the burden is paying the worker the wage they agreed to.

At first glance, exchanging things of equal value implies that there is no gain involved. On closer examination we see that this is not the case. Exchanging things of equal value means that what is exchanged is of equal **exchange** value, not equal use value. As indicated previously, exchange value refers to (a) the price paid to purchase a good or service and (b) the wage or price paid to hire a worker or natural resource to produce that good or service. Use value is what is gotten, that is the usefulness of the good or service or resource to the person who acquires it. The two taken together result in economic gain under the following condition:

gain is **realized** when use value > exchange value.

Whereas use value cannot be influenced by the other party to an exchange, exchange value at times can be determined directly by the other party. In those cases, restraint may be necessary. However, when a market is reasonably competitive, exchange value normally does not fluctuate markedly from day to day and is the same or nearly the same for all buyers on the same day. Competition in other words reduces the control that any single buyer or seller has over price, keeps the market price close to the cost of production, and allows a reasonable profit margin but not undue profit. Thus there may be little need for personal restraint. Gain under these circumstances can be represented as follows:

gain is **justified** when use value > exchange value **restrained** by competition.

A problem arises, however, when the market does not impose this restraint, and agents are free to act, more or less, without restraint. Action of this type can occur when the producer fixes the price through a cartel or when the buyer is simply ill-informed about the market price and overvalues the product or service offered for sale. In such cases, the gain of the seller is ill-gotten because it is based on taking advantage of the buyer. Unrestrained action may involve a buyer who has an opportunity to enhance his/her gain when the seller is unaware of the true value of the product or service offered for sale. This could happen, for example, in a flea market where the seller offers a book for sale at a low price unaware that the book is a very valuable first edition, or when a widow offers property for sale which she has grossly and innocently undervalued. The principle of equivalence in all such cases informs both parties that the only justifiable gain is one that does not deprive the other party of the gain that is rightfully his/hers.

The following simplification expresses the nature of the gain that is justified under these conditions:

gain is **justified** when use value > exchange value **restrained** by faithful adherence
to the principle of equivalence in a situation where competition alone
does not provide the necessary restraint.

Another example may be instructive in driving home this argument. A market price that is determined entirely by the producer -- in the extreme by a monopolist -- violates the principle of equivalence because the margin of profit inflates the price and effectively manipulates exchange value, yielding ill-gotten gain for the monopolist. In this case, the buyer who needs the monopolist’s product or service has no option other than to buy from the producer who controls the price.

From time to time we may not know precisely the exchange value of a specific item such as a Rolex watch but we very likely know that it does not sell for the same price as a Timex watch. Anyone attempting to sell a watch that is represented as an authentic Rolex for, say, $49 should be suspected of (1) selling a Rolex watch that is stolen, (2) selling a watch that actually is a counterfeit or a “knockoff,” or (3) selling a genuine Rolex but having no real appreciation for its true worth. The principle of equivalence means that selling stolen goods is unjust because the seller has no right to sell what does not belong to him/her and the buyer has no right to buy and take possession of a watch that belongs to someone else. Such practices are not unjust because they are illegal. Rather, they are illegal precisely because they are unjust.

Misrepresenting a "knockoff" as the genuine article is unjust because the seller is deliberately deceiving the buyer. Finally, and with one exception, buying a good at a price well below its current market price is unjust because the buyer has no right to exploit the seller who is unaware of the watch's real value. There is, however, no such exploitation when the seller is fully informed as to the good's real value and freely sells it for less. In that case, the good exchanged is in part a gift.

There are other sources of information about what equal means in a marketplace or workplace exchange. They include information available through family members, friends, co-workers, neighbors, and others including lawyers who consult for a fee. There are published sources of information as well such as **Consumer Reports**, newspaper advertising, and electronic exchanges such as **E-Bay**.

At times, the things exchanged at the very moment the exchange is executed are not of equal value, such as when a house is sold and the buyer makes only partial payment in cash but takes possession of the entire house at the time of closing. To simplify this example, we assume that the buyer does not obtain a mortgage from a third-party lender such as a bank. Rather the seller offers to lend the buyer the unpaid balance by allowing the buyer to make regular payments over time until the balance is paid in full. Notice at closing, the buyer's immediate burden is to make partial payment in cash to the seller. The seller's burden is to surrender the whole house, and accept the buyer's written promise to pay the balance in the future. Under those circumstances, the seller faces the risk that the buyer may not be faithful to his/her promise to make payments in the future until the balance is paid in full. And the seller must wait until payments are made and at closing forgoes the use of that money had he/she insisted instead on payment in full. Consequently, the seller/lender is justified in requiring the buyer/borrower to repay more than the amount of money that was borrowed. Indeed, the seller/lender is justified in charging interest in order to equalize the burdens involved.

The precise amount of interest that equalizes the burden is problematical. However, we know by experience that a rate of interest of 100 percent is excessive because it imposes an undue burden on the buyer/borrower. Similarly, a 50 percent rate of interest is excessively burdensome. However, in 1981 banks across the United States were charging their most credit-worthy customers an average of 21 percent on loans and as much as 35 percent for other higher-risk borrowers. Today, credit card companies commonly charge 18 percent annual interest and, even though some cardholders are not able to pay their credit charges, most cardholders do pay what they owe. We conclude that a rate of interest of roughly 20 percent is reasonable and in general satisfies the requirements of the principle of equivalence.

There are several specific ways in which the principle of equivalence may be violated in the marketplace. Shoplifting is one, and issuing a bad check is another. Loan sharking -- charging excessive interest -- and price gouging that may take place in an emergency such as a hurricane are two more examples. Counterfeiting, whether it involves paper currency or "knockoffs" violates the principle of equivalence as does the bait and switch scheme.

In the workplace there are several ways in which the principle of equivalence may be violated. We enumerate here only two: expense padding and sweatshop. Expense padding means seeking reimbursement from your employer for personal expenses incurred when you have been traveling on official business. Or it may be seeking reimbursement for legitimate business expenses but those expenses have been inflated or padded. A sweatshop is an employer who cheats his/her workers in terms of wages, hours, or working conditions. Paying less than the minimum wage or the wage agreed to, forcing employees to work very long hours without rest or compensation, operating a workplace that violates the local building code or that is generally unsafe are ways in which an employer "sweats" his employees in order to reduce labor costs and add to profits.

At times, buyers are overwhelmed by their indebtedness and simply are unable to pay what they owe under the principle of equivalence. At times, they may have acted foolishly spending beyond their means with credit cards, or they may have been ill-informed regarding a sub-prime mortgage, not realizing that they could not afford the house they agreed to buy. At other times, they may be unable to pay their regular monthly bills because of the death or disability of the family's primary wage-earner or they may be weighed down by huge medical expenses due to a catastrophic illness. The legal system provides some relief from their obligations under the principle of equivalence in the form of bankruptcy. The services of a lawyer, perhaps even a specialist in bankruptcy law, very likely would be required to sort through the options available to the person who is unable to handle the financial burdens he/she has taken on. In such cases, the virtue of mercy trumps the virtue of justice. This relief, however, is not cost-free. The merchant or provider who holds bad debt does not get all that he/she anticipated when the exchange took place, is deprived of the gain he/she is legally entitled to, and may compensate for that loss by raising his/her prices or fees, forcing others who are entirely innocent in the matter to pay the true cost of bankruptcy relief.

Distributive Justice. The second principle of justice -- distributive justice -- defines the duties of the superior to his/her subordinates. Specifically, distributive justice requires the superior to distribute the benefits and burdens of the members of the group under his/her supervision in some generally equal fashion. This does not mean strictly equal because there likely are significant differences among subordinates and it is entirely appropriate to take those differences into account. For example, handicapped employees appropriately may require different parking and restroom accommodations than able-bodied employees. Single parents in general shoulder heavier child care responsibilities than married parents. Distributive justice demands that the superior differentiate among subordinates only when the differences among them are real and substantial and require different arrangements. For example, a superior may allow a single parent to rush home to tend to a sick child when the same permission might not be given to a married worker with a spouse who routinely stays at home to look after the children.

Discrimination occurs when the superior differentiates among subordinates for reasons that are insubstantial. In this regard, false stereotyping may be the device used to rationalize the difference in treatment among subordinates. For example, older workers may be treated differently because they simply have "less upside potential" than younger workers. Women may be treated differently because for them work is of secondary importance in their lives. Favoritism is simply the other side of the coin of discrimination: treating some better than others for reasons that are superficial or based on the false stereotyping of others.

The Civil Rights Act of 1964 accorded special legal protection against discriminatory practices to women, African Americans, native Americans, Jews among others. In 1968 persons 40 years of age or older were included in the "protected class"; 22 years later persons with disabilities were included. Even so, false stereotyping is the means by which discrimination persists and flourishes today in the United States. By assigning negative characteristics to a person based on what is taken to be common characteristics of the minority group to which that person belongs, false stereotyping essentially blames the victim for certain character defects and thereby rationalizes treating that person differently. Thus a specific minority person is branded as shiftless, boisterous, drunken, or is labeled as practicing odd religious rituals and the like. For those reasons and others, it becomes much easier to treat that minority person differently than others. Our language itself conveys and reinforces such false stereotypes, notably by the "n" word and the "b" word. Unless and until it is exposed false stereotyping attributes the discrimination to the victim rather than the perpetrator, justifying the discrimination on the basis of an alleged defect in the character of the victim.

Discrimination and the government intervention required to address it are evidence that the market system in which each economic agent in the pursuit of his/her own self interest also serves the common good through the invisible hand is not always sufficient to resolve important conflicts in economic affairs.

Two especially noteworthy violations of distributive justice are kickbacks and harassment. A kickback is the ethical equivalent of a bribe. A bribe is a payment to a superior in the expectation of special treatment. The payment **precedes** the special treatment. A kickback is a payment for special treatment wherein the payment **follows** the special treatment. A contractor bribing a state highway official in order to influence that official's decision as to which contractor is to be awarded a construction contract makes payment beforehand. A contractor kicking back to a highway official promises beforehand to make payment after the deal has been closed. Either way the public servant is rewarded for putting personal gain before the common good. Harassment is the practice of a superior exacting special sexual favors from a subordinate, or touching or addressing him/her in ways that are disrespectful in exchange for a favorable performance evaluation, a raise, a promotion, job assignment, or the like.

The principle of distributive justice has application in the marketplace too, but here the issues are not as serious as in the workplace. In the marketplace, it is the merchant or shopkeeper who is the superior because he/she is the one who must treat his/her customers with fairness. There are several ways in which this is done. We examine one. A merchant who makes rain checks available is saying in effect that when an item is put on sale at a very favorable price, he/she will treat all customers alike even those who come to the store after the supply of that item has been exhausted. Under those circumstances, the merchant re-orders the item in such quantities to satisfy all customers who have been issued a rain check.

The key to understanding how the merchant meets his/her obligations under the principle of distributive justice is that while the specific terms of sale differ across different promotional practices -- limit 3 to a customer, rain check available, sale price effective as long as supplies last -- once a specific practice is put in place there is no difference in the way those terms are applied to any customer. Further, though some customers may not be able to take advantage of the favorable opportunities afforded by the merchant, due perhaps to their lack of transportation, their infirmities or disabilities, their being away from home on business, the merchant's duties under distributive justice extend only to those who actually enter the store, provided the merchant has made an effort to properly inform his/her customers of the opportunities and to maintain the usual store operating hours.

As we observed already with the principle of equivalence, an ill-gotten gain can be had when the superior fails in his/her obligations under the principle of distributive justice. For example, discrimination in the workplace can yield an ill-gotten gain to the employer who resorts to paying some workers less than others for work of the same kind and quality. Favoritism in the marketplace in which the offending purchasing agent is rewarded with a kickback represents a similar ill-gotten gain. Here, too, the law offers a remedy for market failure though a powerless plaintiff may find that legal representation is expensive, the litigation process tedious and drawn-out, and the outcome problematical. Because economic agents including lawyers, judges, and juries are imperfect human beings, even this remedy may fall short of what is needed to completely right the wrong.

Contributive Justice. The third and last principle of economic justice is contributive justice that lays down the obligation of the member to the group to which that person belongs. Insofar as a person receives benefits from the group, that person has a duty to maintain and support the group. Paying dues -- a duty -- is the usual requirement for the persons joining and remaining active in a membership organization. Failure to pay membership dues typically reduces a person to inactive membership status enjoying fewer benefits of membership as compared to those in good standing.

There are several powerful examples as to how contributive justice is violated in the marketplace and the workplace. We mention only two. In the workplace, industrial spying and sabotage violate contributive justice because the person who appears to be a loyal and productive member of one business establishment actually is faithful to a rival organization and seeks to undermine the effectiveness of the first establishment by stealing secrets and disrupting its work. Is it a violation to hire a person from a rival establishment and then pick his/her brain for whatever information he/she might be able to share with the new employer? It does, if that person surrenders proprietary information, that is information to which that the former employer can claim a clear property right such as a secret formula for making a product.

In the marketplace, insurance fraud violates contributive justice because if a fraudulent claim is not detected by the insurance company, payment is made to the insured party that drives up the cost of the insurer who may pass those additional costs on to all policy holders in the form of higher premiums. The Coalition Against Insurance Fraud estimates that insurance fraud costs Americans about $80 billion every year or $950 per family (see www.insurancefraud.org). Here, as well, the law provides some relief by defending propriety rights and prosecuting insurance fraud, but for reasons cited previously the harm done may not always be fully undone.

To repeat, limits on the amount of gain in the form of profits, consumer surplus, and economic rent are necessary to prevent one party from taking advantage of another and to assure that market exchange serves everyone fairly and effectively. Those limits derive from the duties that economic agents owe one another under the principles of equivalence, distributive justice, and contributive justice. Specifically, the principle of equivalence limits ill-gotten or excessive gain because what is gotten and what is given up in the exchange are what were freely and openly agreed to before the exchange took place. For example, the ill-gotten gain for the employer who operates a sweatshop is the added profits from denying his/her workers what is due them. The ill-gotten gain for the employee who embezzles is money that rightfully belongs to the employer. The principle of distributive justice limits ill-gotten gain because the superior assures that what is gotten and what is given up are the same for everyone in the same or similar circumstances. To illustrate, the ill-gotten gain for the employer who pays some workers less than others for the same work is the added profits gotten through discrimination. The ill-gotten gain for the public official who has been bribed to award a contract for a clearly substandard proposal is the money which that official has gotten dishonestly. The principle of contributive justice limits excessive gain because each member gives up (contributes) what is necessary to maintain the group provided what is gotten by that member is the same or similar to what is gotten by the other members of the group. The ill-gotten gain for the inside trader comes at the expense of persons who sell shares that the inside trader knows are undervalued or who buy shares that the insider knows are overvalued. The ill-gotten gain in industrial spying is the property that rightfully belongs to someone else.

In closing, in a perfect world in which all economic agents are fully-informed, free to act, and faithful in practicing the three principles of economic justice, the market system alone would be sufficient to assure the economic gain of each party in every exchange, that what is gotten is more highly valued than what is given up. Economic agents, however, are imperfect human beings and at times are able to grab hold of gains that are not rightfully theirs. The business of the lawyer is to try to remove the imperfections that produce the ill-gotten gains or find some remedy that compensates the victims for their losses.

Edward J. O'Boyle is Senior Research Associate with Mayo Research Institute located in West Monroe, Louisiana. Since he completed his doctorate in economics from Saint Louis University more than 30 years ago, Dr. O'Boyle has been specializing in economic research and analysis increasingly from the perspective of the human person engaged in everyday activities both as a unique individual and as a community member. In 2004 the Association for Social Economics conferred on Dr. O'Boyle its prestigious Thomas Divine Award for lifetime contributions to social economics and the social economy.