

## A POLICYMAKER'S GUIDE TO WELFARISM

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In response to Matthew D. Adler & Chris William Sanchirico, *Inequality and Uncertainty: Theory and Legal Applications*, 155 U. PA. L. REV. 279 (2006).

Welfarism is widely employed and debated not only among philosophers, political scientists, and economists, but also increasingly among legal scholars. However, not all legal scholars fully appreciate this approach to social choice. For example, welfarism is commonly, but wrongly, equated with utilitarianism. Recent contributions by legal scholars—in particular, Kaplow and Shavell—considerably advanced the understanding of welfarism.<sup>1</sup> Professors Adler and Sanchirico (hereinafter “the Authors”) make another important contribution.<sup>2</sup> They present the welfarist approach and its mechanisms in simple terms, accompanied by illuminating examples. They clarify the relationship between equity and welfarism, especially contrasted with utilitarianism. Even without considering the Authors’ innovative arguments, their Article is undoubtedly valuable reading material for welfarist and nonwelfarist legal scholars.

The Authors’ key contribution is their discussion of ex ante versus ex post assessment of social welfare. The starting point is that any equity-regarding social welfare function may rank policy options differently depending on the welfarist methodology selected: ex ante or ex post.<sup>3</sup> An ex ante methodology would aggregate the expected

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<sup>†</sup> I am grateful to Adi Ayal and Gideon Parchomovsky for their helpful comments and discussions.

<sup>1</sup> LOUIS KAPLOW & STEVEN SHAVELL, *FAIRNESS VERSUS WELFARE* (2002). See also Matthew D. Adler & Chris William Sanchirico, *Inequality and Uncertainty: Theory and Legal Applications*, 155 U. PA. L. REV. 279, 283 n3 (2006).

<sup>2</sup> See Adler & Sanchirico, *supra* note 1.

<sup>3</sup> Discussions of the ex ante and ex post methodologies can be found in Elchanan Ben-Porath et al., *On the Measurement of Inequality under Uncertainty*, 75 J. ECON. THEORY 194, 194-96 (1997); John Broome, *Uncertainty and Fairness*, 94 ECON. J. 624, 624 (1984); Peter A. Diamond, *Cardinal Welfare, Individualistic Ethics, and Interpersonal Comparison of Utility: Comment*, 75 J. POL. ECON. 765-66 (1967); Thibault Gajdos & Eric Maurin,

utilities of individuals. An ex post approach, on the other hand, would aggregate the actual utilities of individuals in the various (ex post) states of the world, and then take an expectancy of the aggregations. These two approaches to welfarism necessarily coincide under utilitarianism, which is not an equity-regarding method of social ranking. Under any equity-regarding welfarist method, these approaches may rank various social choices differently.

The Authors argue that the ex post approach to social welfare is preferable.<sup>4</sup> That is, if welfarism is adopted and equity (in the Pigou-Dalton sense) is subscribed to, the ex post perspective is socially superior. They conclude, then, that policymakers should evaluate public policies according to the ex post approach, even though this might require rejecting policies that would make everyone better off from an ex ante perspective.

This Response adopts the Authors' axioms: (1) welfarism, and (2) equity-regarding aggregation of utilities. It also adopts the Authors' standpoint—i.e., it favors the ex post perspective of welfarism.<sup>5</sup> However, it supports the opposite case as guidance to policymakers. That is, although the ex post valuation of welfare is assumed to be superior, *most* public policies should, in general, be guided by an ex ante perspective. Moreover, this Response presents utilitarianism as a feasible welfarist option for *most* public policy analyses, even under a general ex post equity-regarding approach to social welfare.

The case is built by focusing on the compensation option, following the Authors.<sup>6</sup> "Compensation" describes redistribution of individuals' utilities. Compensation can be applied ex post to "repair" or "rearrange" socially inappropriate distributions of utilities. Assuming a proper compensation apparatus can be applied ex post costlessly, the dilemma is solved: ex ante policy evaluation is permissible, *even under the ex post approach*, since its ex post unwanted ramifications can be fixed costlessly when the (ex post) time comes. Costless compensation makes us socially indifferent to the two welfarist perspectives of policymaking. Yet, compensation schemes,

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*Unequal Uncertainties and Uncertain Inequalities: An Axiomatic Approach*, 116 J. ECON. THEORY 93, 94 (2004); Peter J. Hammond, *Ex-Ante and Ex-Post Welfare Optimality under Uncertainty*, 48 ECONOMICA 235 (1981); Alon Harel et al., *Ex-Post Egalitarianism and Legal Justice*, 21 J. L. ECON. & ORG. 57, 69 (2005).

<sup>4</sup> See Adler & Sanichirico, *supra* note 1, at Part V.

<sup>5</sup> I do not necessarily subscribe to this position, though I do believe it merits attention. See Jacob Nussim, *Redistribution Mechanisms*, REV. L. & ECON. (forthcoming).

<sup>6</sup> See Adler & Sanichirico, *supra* note 1, at Part III.

the Authors rightfully claim, are socially costly (e.g., administrative and compliance costs).

The conclusion the Authors draw from this fact is not entirely clear. Notwithstanding a few nonconclusive statements, the general thrust of the the Authors argument is that the *indirect* route to the ex post equity-regarding choice—i.e., ex ante valuation supplemented by costly ex post compensation—is unwarranted. For example, the Authors do not try to assess the costs of redistributing utilities, or to counter them with any other opposing force; it would seem that even the slightest cost of compensation would suffice for rejection of the compensation route. This Response builds a case for the indirect route to social welfare via “compensation.” It proceeds in four parts. Part I reveals the costs of the ex post approach and contrasts them with those of the compensation option. Part II argues that a weaker condition is required to establish the compensation option, and hence it incurs even lower costs. Part III is built entirely on separate work by David Weisbach and myself, and attempts to enrich the analysis by adding another dimension to it. It shows how the institutional structure of social policies militates against the ex post approach, and emphasizes the benefits of the compensation scheme. Part IV adds other considerations supporting the indirect route to the ex post approach via compensation.

## I. THE RELATIVE COSTS OF COMPENSATION

The argument in this Part is constructed in two stages: first, I argue that the (relative) size of compensation costs is important for the Authors’ argument to hold. If these costs are low enough, an ex ante approach to social welfare, coupled with ex post compensation is superior to direct choice of the ex post option. Second, there are good reasons to believe that compensation costs are relatively low, and hence the indirect route is preferable.

The starting point is to realize that the ex post approach itself is inherently costly. If the social choice changes as a result of going from ex ante to ex post evaluation of social welfare (i.e., due to divergence), then *in terms of ex ante analysis*, the ex post approach is costly. This is straightforward according to the Authors’ article. If the planner’s ex post social choice is different from that based on the ex ante approach, then the former must be inferior under ex ante analysis. In Part IV, the Authors state this explicitly: an ex post social choice is ex ante Pareto inferior. That is, the *ex ante level* of welfare under an optimal ex post social choice is lower than its level under an

optimal ex ante social choice. This must be true since these two choices diverge. The difference between these welfare levels represents the social costs of an ex post approach, in terms of an ex ante evaluation. Accordingly, from the viewpoint of ex ante analysis, a divergent ex post social choice is costly.

The same explanation can be given for the ex post viewpoint. As the Authors indicate, ex ante Pareto superiority implies that all individuals would prefer the ex ante over the ex post perspective. Assuming individuals' preferences are not equity-regarding, as are those of the social planner, the ex post option is inferior for each and every individual in society. Still, the ex post approach might be socially beneficial due to its distributive effects. The ex post social choice diverges from the Pareto superior ex ante option when the social distributive benefit (i.e., equity) outweighs the aggregate welfare loss due to decreased expected individual utilities. This potentially outweighed loss is the cost of the ex post option, from the viewpoint of the ex post approach.<sup>7</sup> As long as individual choice can be represented by expected utility, the ex post methodology of social welfare is costly in terms of lost utility.

Accordingly, facing uncertainty and equity (or equality) preferences, the Authors argue, the equity benefits of a divergent ex post approach can offset the losses in individual expected utilities. But this cannot be sufficient, since there might be a cheaper way to accomplish the ex post alternative. Given that the ex post choice is preferable, there are a few ways of reaching it, two of which are central: (1) the ex ante social choice accompanied by ex post compensation; and (2) the direct ex post social choice. Both of these routes incur social costs, but of different kinds. Therefore, even an ex post planner cannot discard an ex ante approach—even, say, utilitarianism—without measuring the adjustment costs to the ex post choice (i.e., compensation). These costs may prove lower than the social costs of direct application of an ex post perspective. The mere costs of compensation cannot rule out an ex ante approach.

What is required is a reliable evaluation technique for these two kinds of costs. On the compensation side, redistribution of utilities generally involve redistributing resources (both across individuals and across states), commonly via taxes and transfers. Redistribution of utilities probably cannot be *fully* accomplished through taxes and

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<sup>7</sup> See also Harel et al., *supra* note 3, at 62 (arguing that reducing variation in utility distribution costs in average utility).

transfers, and additional redistribution might potentially be accomplished through public policies, but the former are the central means of utilities' redistribution.

Although it is hard to make any general statements about the relative costs of an ex post perspective,<sup>8</sup> it is generally contended that the efficiency costs of redistributing via taxation are lower.<sup>9</sup> Additionally, there are complexity (i.e., administrative and compliance) costs. The complexity costs of redistribution are probably rather low under the tax-transfer system. As long as the tax and transfer system exists in any case—for revenue and equity purposes—its marginal use for compensation is most likely quite trivial. The additional burden on administration and the public incurred by the extra redistribution, which is required due to public policies, is apparently not significant. It may involve increased or decreased tax rates, adding or eliminating deductions and exemptions, changing the level of progressivity, etc. In particular, no major modification of the tax and transfer system is required. Although it is difficult to assess the general complexity costs of redistribution by public policies, it should be noted that equity-regarding policies tend to be more interventionist. This, in turn, typically induces higher levels of administrative and compliance efforts.

Additionally, redistribution through the tax-transfer system exhibits two additional complexity advantages. The tax-transfer system is likely to be better specialized than other public entities in redistributing utilities in society. Specialization can be translated into lower complexity costs.<sup>10</sup> Redistributing utilities ex post through the tax-transfer system also enjoys economies of scale. That is, it must be cheaper (in complexity terms) to redistribute utilities once, through

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<sup>8</sup> In particular, the efficiency costs of the ex post policy evaluation crucially depend on the policy content—e.g., the policy's means of equating utilities across individuals and states. These means are supposedly different, for example, under environmental protection and public education policies.

<sup>9</sup> See, e.g., RICHARD ZECKHAUSER, USING THE WRONG TOOL: THE PURSUIT OF REDISTRIBUTION THROUGH REGULATION (1981) (arguing that distributional objectives are optimally achieved through the tax system alone); Aanund Hylland & Richard Zeckhauser, *Distributional Objectives Should Affect Taxes But Not Program Choice or Design*, 81 SCANDINAVIAN J. ECON. 264 (1979) (same); Louis Kaplow, *On the (Ir)Relevance of Distribution and Labor Supply Distortion to Government Policy*, 18 J. ECON. PERSPECTIVES 159 (2004) (arguing that, in general, distributional concerns should play no role in evaluating public policies).

<sup>10</sup> For a similar argument in a different legal setting, see Jacob Nussim and David Weisbach, *The Integration of Tax and Spending Programs*, 113 YALE L.J. 955, 992-97 (2004).

one procedure and a single mechanism, than via a multiplicity of public policies and public agencies. These two complexity advantages will become clearer later when we discuss the organization of governmental decision making.<sup>11</sup>

Thus, there are good reasons to believe that the relative costs of compensation are generally lower. If this is the case, what would be our conclusion? Certainly, no rejection of the ex post methodology; but, then, no recommendation of this methodology to social planners either. On the contrary, if the ex post approach is appropriate for social welfare, then it is better realized through an ex ante approach accompanied by an ex post compensation (i.e., redistribution of utilities). If the relative costs of compensation are low enough,<sup>12</sup> this indirect route to ex post policy evaluation is superior in social welfare terms. Furthermore, the selected ex ante approach need not be equity-regarding since in any case its ex post consequences would be mitigated through compensation. In particular, utilitarianism is not a bad choice for nontax policy evaluation, even under an ex post approach.

## II. A SUFFICIENT CONDITION FOR CONVERGENCE

According to the Authors, compensation requires redistribution (i.e., transferability) of utilities along two dimensions: across individuals in each potential state of the world, and across states of the world for each individual. These are sufficient (though probably not necessary) conditions for the re-convergence of the ex ante and ex post approaches to social welfare.<sup>13</sup> This Response proposes, however, that cross-individual transferability of utility is superfluous. That is, if each kind of transferability condition is costly, the social costs of convergence are exaggerated by requiring too much.

To demonstrate this, the general construction of the Authors' argument is first reiterated. When policy consequences are certain, ex ante and ex post perspectives, and hence social orderings, are necessarily identical under any kind of social welfare function. Yet, facing uncertainty, both approaches are necessarily equivalent only under a utilitarian welfare function, but can diverge under

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<sup>11</sup> See *infra*, Part III.

<sup>12</sup> As pointed out above, these costs are also sensitive to the ability to redistribute utility through taxes and transfers.

<sup>13</sup> Adler & Sanichirico, *supra* note 1, at Part III.

nonutilitarian social preferences.<sup>14</sup> Since utilitarianism is indifferent to equity, it is inappropriate for social policy analysis. In conclusion, in the face of policy uncertainty, and given equity-regarding social preferences, ex ante and ex post social choices are not necessarily equivalent. Accordingly, two distributional conditions lead to this conclusion: the distribution of utilities across individuals (i.e., equity) and across states (i.e., uncertainty). For example, if both distributions are equalized—i.e., perfect equality exists across individuals and certainty—ex ante and ex post approaches converge, irrespectively of social preferences. Apparently, this is the Authors' intuitive source for the double transferability conditions. That is, if utility can be freely transferred across individuals and across states, both of these distributions can be equalized (or at least controlled ex post).

However, transferability across states of the world alone is enough (i.e., a sufficient condition) for convergence between ex ante and ex post approaches. If utility is freely transferred across states for each individual, uncertainty is eliminated, and no divergence is possible. In the absence of uncertainty, ex ante expected outcomes are identical to ex post actual outcomes. Any equity consideration would be equally relevant under both ex ante and ex post analysis.<sup>15</sup> In logical terms, uncertainty is a necessary condition for divergence, and hence certainty is a sufficient condition for its removal—i.e., convergence.

Therefore, the compensation option demands redistribution of utilities only across states of the world, and not across individuals. That is, the costs of compensation are even lower, and hence the case for the indirect route to ex post policy evaluation is reinforced.

### III. DECENTRALIZED POLICYMAKING

In reality, public policy is not made by a single person in government. Policymaking is decentralized throughout the organization of government. Any recommended methodology of public policy assessment is directed toward multiple entities within the governmental organization, at various levels—e.g., politicians,

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<sup>14</sup> John C. Harsanyi, *Cardinal Welfare, Individualistic Ethics, and Interpersonal Comparisons of Utility*, 63 J. POL. ECON. 309, 316 (1955).

<sup>15</sup> Indeed, free transferability of utilities across individuals may also be sufficient if we agree to adopt utilitarianism as the non-equity-regarding social welfare approach. When utilities are freely transferred across individuals, equity concerns are costlessly removed. Uncertainty concerns are then neutralized, rather than removed, by adopting utilitarian preferences.

committee members, public officials, and bureaucrats. Appreciating the dispersion of policymaking within the public sector crucially affects the choice between the two routes investigated here: the ex post perspective versus the ex ante approach complemented by compensation. This Part draws on ongoing research by David Weisbach and myself, and argues that the latter route is preferable in a decentralized policymaking society.

There are various justifications for decentralized public policymaking, and numerous explanations for the tendency of governmental organizations to decentralize policymaking authority. These issues have been studied by scholars in such diverse disciplines as public administration, sociology, psychology, economics, and political science. This voluminous literature is discussed elsewhere.

In general, this literature indicates a number of reasons for decentralization or delegation of policymaking: in particular, specialization,<sup>16</sup> bounded rationality,<sup>17</sup> and agency problems.<sup>18</sup> The political structures and relationships—House and Senate, committees, subcommittees, agencies, etc.—demonstrate significant decentralization. The tasks of devising, detailing, and implementing public policies are allocated among different entities. Delegation is observed across federal levels—federation, states, cities, counties—and along various public issues—such as environment, welfare, personal safety, etc. Further, within each governmental entity, responsibility is delegated to various individuals. The theory of organizations also indicates that decentralization of tasks and information is limited, inter alia, by coordination difficulties. Synchronizing dispersed actors

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<sup>16</sup> See, e.g., Luther Gulick, *Notes on the Theory of Organization*, in PAPERS ON THE SCIENCE OF ADMINISTRATION 1 (Luther Gulick & L. Urwick eds., 1937) (exemplifying the benefits and effects of specialization within organizations); HERBERT A. SIMON ET AL., PUBLIC ADMINISTRATION 158 (1950) (same).

<sup>17</sup> See, e.g., HERBERT A. SIMON, ADMINISTRATIVE BEHAVIOR: A STUDY OF DECISION-MAKING PROCESSES IN ADMINISTRATIVE ORGANIZATION (1957) (building his organizational theory on precepts of bounded rationality); Raaj K. Sah & Joseph E. Stiglitz, *The Architecture of Economic Systems: Hierarchies and Polyarchies*, 76 AM. ECON. REV. 716 (1986) (showing how the organizational design affects its output when individuals err).

<sup>18</sup> See, e.g., Anthony Downs, *A Theory of Bureaucracy*, 55 AM. ECON. REV. 439 (1965) (establishing a theory of bureaucratic behavior based in part on self interest); WILLIAM NISKANEN, BUREAUCRACY AND REPRESENTATIVE GOVERNMENT 36-42 (1971) (arguing that bureaucrats seek public reputation, power, salary, large budget); Bengt Holmstrom, *Moral Hazard in Teams*, 13 BELL J. OF ECON. 324 (1982) (showing how competition among agents can be beneficial in revealing information); JONATHAN BENDOR, PARALLEL SYSTEMS: REDUNDANCY IN GOVERNMENT (1985) (arguing that redundancy in public administration can be beneficial).



or decision units is costly, and hence constrains the extent of delegation in organizations. The value of agency multiplicity (e.g., specialization, competition, redundancy) is traded off against its triggered coordination costs. Thus, mis-coordination among governmental agencies, as well as among corporate divisions or workers, is expected; and examples of mis-coordination are abundant.<sup>19</sup>

Thus, the design and implementation of public policy is decentralized through multiple public agencies and officials, which are generally not well coordinated. This means that no single policymaker can see the whole picture—i.e., social welfare function. In particular, uncertainty about any single public policy is only one (arguably minor) part of social welfare uncertainty; and the case is similar for the distribution of utilities generated by a single policy. Clearly, then, it is wrong to speak of a particular policy as being equitable or inequitable.

Consider the following example. Assume three uncertain public policies—I, II and III—which affect the utility of two individuals (U,V) under two possible states of the world—a and b.

	I	II	III
State a	(100, 300)	(300, 100)	(150, 150)
State b	(500, 200)	(200, 500)	(300, 300)

Assume one policymaker is required to choose between policies I and III and the other between II and III. If both policymakers follow an ex post methodology of social welfare assessment, they may both prefer III over I or II. But these decisions are socially wrong in welfare

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<sup>19</sup> See, e.g., NATIONAL COMMISSION ON TERRORIST ATTACKS UPON THE UNITED STATES, THE 9/11 COMMISSION REPORT 263-65 (2004) (describing how a lack of coordination among U.S. governmental agencies contributed to the States' vulnerability to terrorist attack); HAROLD SEIDMAN & ROBERT GILMOUR, POLITICS, POSITION, AND POWER 119-35 (1970) (describing the Reagan administration's transition to an unprecedented centralized decision-making organizational structure); Edward T. Jennings & Dale Krane, *Coordination and Welfare Reform: The Quest for the Philosopher's Stone*, 54 PUB. ADMIN. REV. 341, 396 (1994) (identifying barriers to coordination in the Job Opportunities and Basic Skills program); B. Guy Peters, *Managing Horizontal Government: The Politics of Coordination*, 76 PUB. ADMIN. 295, 303 (1998) (discussing potential failures of coordination by networks); Dominic Stead, *Transport and Land-use Planning Policy: Really Joined Up?*, 55 INT'L SOC. SCI. J. 333, 393 (2003) (finding a lack of integration between land-use planning and transportation policy); Janet A. Weiss, *Pathways to Cooperation Among Public Agencies*, 7 J. POL'Y ANALYSIS & MGMT. 94, 95-98 (1987) (reporting on problems of organizational cooperation with the public school system).

terms. Choosing I and II is superior to choosing III twice under any equity-regarding social welfare function. That is:

	I + II	III + III
State a	(400, 400)	(300, 300)
State b	(700, 700)	(600, 600)

In fact, this example is quite obviously idealized, since the consequences of policies I and II are perfectly and negatively correlated. However, this argument holds, in general, for two or more nonperfectly correlated policies. As long as some public policies are not perfectly correlated, separate and uncoordinated ex post valuation of each may produce an inferior welfare outcome overall (as evaluated by an ex post methodology). This is actually a diversification argument applied to social-policy risks. Like financial portfolios, the value of diversification increases as positive correlation among uncertain choices diminishes.<sup>20</sup> In the social welfare sphere the intuition is similar, however it is the correlation in utilities' distributions which is of interest.

Are social policies perfectly and positively correlated? Apparently not. There is no reason to believe that the distributions of utilities induced by different policies follow a similar pattern in any way. The information gathered by different agencies and its analysis is not usually similar; the preferences of various decisionmakers may differ; the subject matter of social policy (e.g., environmental vs. educational vs. security) is seemingly unrelated; different politicians/policymakers serve various clienteles and hence the benefits of different policies flow to diverse social, geographical, and economic groups; all of the above factors can change over time, possibly creating intertemporal differences in utilities' distributions.<sup>21</sup>

To conclude, a separate ex post analysis of each social policy is inadequate. A comprehensive, all-inclusive ex post analysis is required, but this is not possible in reality. Governments cannot

<sup>20</sup> See, e.g., RICHARD A. BREALEY AND STEWART C. MYERS, PRINCIPLES OF CORPORATE FINANCE 153-80 (6th ed. 2000) (showing that diversification reduces variability and hence portfolio risk).

<sup>21</sup> This naturally raises the question of when is "ex post" realized? The relevant future moment of "ex post" should be determined somehow. Answering this question is important under both ex ante and ex post perspectives.

evaluate all policies in tandem. So what can be done? The resulting all-inclusive distribution can be fixed *ex post* by redistributing utilities—i.e., compensation. Thus, *ex post* compensation can serve to facilitate valuable coordination among policies. But then, if compensation is employed, an *ex ante* approach can be adopted. In particular, utilitarianism cannot be ruled out as a guiding principle for policymakers.<sup>22</sup>

A second conclusion drawn from the theory and practice of organizations is that public policies are allocated to various agencies, each specializing in a particular public issue, generally unrelated to equity (e.g., environment, security, agriculture). But then, equity—i.e., distribution of utilities—is not common knowledge. It requires expertise in equity as well,<sup>23</sup> which by their very nature specialized agencies do not possess. A housing agency does not necessarily have anything to do with equity. It specializes in housing. Specializing in equity issues would be wasteful for these agencies, and for that very reason the government—like other organizations—is structured according to expertise. Specializing in equity would necessarily hurt agencies' expertise in their subject matter, and accordingly impair their nonequity performance.<sup>24</sup>

Therefore, it is conceivable that equity also requires organizational specialization. The tax-transfer system or a “welfare department”, arguably, is, or can be perceived as, an equity-specialized agency. If specialization in equity is indeed valuable enough that a separate agency or a group of policymakers is allocated for it, social equity would be applied separately from other public policies.<sup>25</sup> That is, most policymakers should be guided by a nonequity-regarding welfare function. In particular, utilitarianism cannot be excluded.

#### IV. ACCURACY, POLICY CONSTRAINTS, AND POLITICAL ACCEPTABILITY

There are further arguments in favor of an *ex ante* approach supplemented by compensation. First, it seems that compensation—

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<sup>22</sup> Actually, under certain plausible assumptions, utilitarianism is superior to any *ex ante* equity-regarding welfare function for the same reason. The distribution of the expected utilities of a single policy is meaningless. That is, equity-regarding preferences, in general, are unsuitable for decentralized policymaking, as long as *ex post* compensation is not excessively costly.

<sup>23</sup> Expertise in equity includes, *inter alia*, the collection of relevant information, its measurement, its analysis, and making decisions that fit results.

<sup>24</sup> Yet, though a housing agency is no expert in redistributing utilities, it may enjoy a superior expertise in measuring individuals' utility from housing.

<sup>25</sup> *Cf.* Adler & Sanchirico, *supra* note 1, at 329-30.

i.e., ex post redistribution of utilities—is required anyway under the ex post approach, mainly due to the cost of information. Policies are selected ex ante based on information about the future. Production of information is costly; in particular, information relating to *future* utilities of a country's population is very costly.<sup>26</sup> The other side of the coin is accuracy: cheaper information is less accurate. Accordingly, the choice of policies ex ante can be mistaken due to inaccurate information. Actually, optimality necessarily dictates a certain number of errors in policy choice. Such mistakes—in particular, those relating to distribution of utilities—can be fixed ex post through compensation. The costs of ex post compensation versus the costs of error (or the production of extra information ex ante) have to be weighed: if the former cost is (relatively) small, applying ex post compensation is socially valuable.

There are good reasons to believe that this is actually the case. The costs of information production are probably quite high, not only because of the difficulties in predicting future consequences, but also due to interdependencies within the government. As explained above, public policy is decentralized throughout the government. The outcomes of any particular public policy may depend, inter alia, on other public policies and choices. Land use policies are interrelated with transportation policies, and both are interconnected with environmental policies. Since policy choices are decentralized and barely coordinated, errors in estimation (of ex post distributions) are difficult (i.e., expensive) to avoid. On the other hand, ex post compensation is, as explained above, relatively cheap. First, this is due to specialization in utilities' distribution. Second, economies of scale indicate that a single unified action of utilities redistribution is probably cheaper than multiple endeavors by separate agencies.

Another possible motivation for ex post compensation is potential constraints on the design and implementation of public policies. Even if all policies are selected according to an equity-regarding ex post welfare function, the resulting distribution of equities might be limited. Public policies are constrained to a larger extent in their spectrum of potential utilities distribution. For example, environmental protection policy can prohibit production by a plant polluting a poor neighborhood, but it may not be able to force it to

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<sup>26</sup> The first difficulty inheres in identifying all possible (or at least, the important) future states of the world, and measuring the effect of a public policy in each. Second, the separate and composite reaction of individuals should then be evaluated, as should its effect on the distribution of utilities.

relocate to a rich area. If the resulting distribution of utilities is limited, additional redistribution *ex post* might be socially beneficial.

If compensation is required anyway, either due to error fixing or constrained policies, and assuming the marginal costs of compensation are not excessive, equity can be dispensed with in policy design. Any non-equity-regarding welfare evaluation—whether under an *ex ante* or *ex post* approach—is appropriate as long as *ex post* compensation is employed. Again, in particular, utilitarianism is also acceptable.

Finally, *ex post* compensation is valuable since it allows for an *ex ante* Pareto superior choice of social welfare. It permits choices of policies that would be unanimously supported.<sup>27</sup> This issue of political acceptability or public choice relates to the discussion of the costs of the *ex post* approach, above. It is actually a similar argument, used for different purposes.

To sum up, the appropriate perspective of social welfare is indeterminate. Uncertainty and equity preferences trigger a social dilemma of *ex ante* versus *ex post* perspectives. Yet, policymakers should not on the whole be concerned with this social choice. As long as compensation—i.e., redistribution of utilities—is a viable and valuable option, policymaking may ignore the dilemma. Compensation is a viable option even though it sustains social costs. There is good reason to believe these costs are relatively low. Furthermore, utilities' redistribution is largely feasible through special redistributive systems—i.e., taxes and transfers.<sup>28</sup> Compensation is valuable for various reasons. It saves on individual utilities. It better coordinates decentralized policymaking. It promotes valuable specialization in social policy production. It allows for economies of scale in achieving equity. It improves accuracy. Therefore, only a very restricted branch of government—i.e., the tax-transfer system—still faces the dilemma presented by the Authors. The rest of the governmental organization is unconstrained by it. However, this does not necessarily mean that any (benevolent) social welfare ordering is proper for policymaking. It implies that nontax policymakers should adopt a Pareto superior welfare ordering, while ignoring equity

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<sup>27</sup> See Adler & Sanchirico, *supra* note 1, at 331-34.

<sup>28</sup> Indeed, to the extent that specific components of utilities are nontransferable through the tax-transfer system and cannot be compensated for (e.g., certain health conditions), and they can be redistributed through other public policies, these policies *may* be guided by an *ex post* perspective after all.

consequences.<sup>29</sup> In particular, utilitarianism is an option, and an acceptable guide for policymakers.

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<sup>29</sup> This result should not be confused with Musgrave's analytical separation of the allocation and distribution branches of government. RICHARD A. MUSGRAVE, *THE THEORY OF PUBLIC FINANCE* 3-22 (1959). Indeed, allocation (i.e., efficiency) and distribution (i.e., equity) are not independent tasks of government. But their *joint* implementation should not be applied by each and every unit of government.