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Focus on Fairness, Efficiency, and the Law: Response. An Integration of Equity and Efficiency

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AN INTEGRATION OF EQUITY AND EFFICIENCY

Richard O. Zerbe Jr.*

Policy analysts have long recognized that both efficiency and equity are relevant for decisions. Because both are seen as components of justice, judges and policymakers are presumed to take both efficiency and equity into account in their decisions. The aim of integrating efficiency and equity is thus not generally at issue. The question is how to do it in a useful way.

Swygert and Yanes, in an article in this issue of the *Washington Law Review*, suggest a means to achieve this integration.¹ In this Article, I first discuss the shortcomings of the approach suggested by Swygert and Yanes. Next, I suggest a more practical approach for integrating efficiency and equity that relies on benefit cost analysis. Finally, I consider some of the cases to which Swygert and Yanes apply their analysis. The fundamental shortcoming of the Swygert and Yanes approach is that it offers little for deciding practical cases. The authors combine two abstract and heuristic proposals and quite naturally end up with an abstract approach that is uncertain in its application.

In this response, I show that benefit cost analysis, a well-established technique for determining whether a decision is efficient, is also applicable to equity considerations. Indeed, I show that the distinction between efficiency and equity is artificial. The expanded efficiency approach I suggest remedies the defects in the Swygert and Yanes approach and offers a more practical alternative for integrating efficiency and equity.

I. A CRITIQUE OF THE SWYGERT AND YANES APPROACH

Swygert and Yanes invoke the Coase Theorem, with its world of zero transaction costs, along with Rawlsian ideas of justice, particularly the concept of the initial position, as rhetorical devices to aid in thinking

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1. Michael I. Swygert & Katherine Earle Yanes, *A Unified Theory of Justice: The Integration of Fairness into Efficiency*, 73 Wash. L. Rev. 249 (1998).

about actions that satisfy both efficiency and equity. Although these rhetorical devices are useful in thinking about efficiency and equity, the concepts of a zero-transaction-cost world and a world of an initial position are too abstract to allow much of an improvement to existing thinking about equity and efficiency.

Consider first the Coase Theorem as a device for deciding efficiency.² The Coase Theorem applies to the world of zero transaction costs and perfect knowledge.³ Such a world guarantees economic efficiency as long as rights are well specified. With zero transaction costs, all profitable trades will be made.⁴

In the real world where transaction costs do exist, the Coase Theorem has limited applicability.⁵ The rule that results in economic efficiency when transaction costs are very low is not necessarily the rule that results in efficiency when transaction costs are high. For example, when transaction costs are low, the efficient rule may be one that promotes bargaining. When transaction costs are high, the efficient rule is more likely to put the burden of action on the party that can make efficient adjustments more cheaply. In focusing on the Coase Theorem, Swygert and Yanes lose sight of what efficiency is. Not surprisingly, then, the authors are unclear about whether they refer to Pareto efficiency or the Kaldor-Hicks (KH) efficiency (also called wealth maximization).⁶

Similar difficulties arise when Swygert and Yanes introduce Rawls's theories of justice as the vehicle to consider equity issues. The authors invoke Rawls's approach because they believe it generates constructive empathy by the assumption of risk aversion in an initial position.⁷ The initial position, originally defined by Harsanyi and not by Rawls, is one in which individuals make decisions about fundamental rules of society

2. For an extended discussion of the Coase Theorem, see Steven Medema & Richard Zerbe, *The Coase Theorem*, in *The Encyclopedia of Law and Economics* (Boudewijn Bouckaert & Gerrit DeGeest eds., forthcoming 1998).

3. *Id.* The Coase Theorem does not define economic efficiency nor does it suggest what actions are efficient.

4. Initial rights determine a wealth floor in the Coase Theorem world because no one would agree to a bargain that makes him or her worse off. With zero transaction costs, everyone is part of every bargain.

5. Coase's purpose was to draw attention to the role of transaction costs, not to develop an economic theory based on zero transaction costs. See Medema & Zerbe, *supra* note 2.

6. Pareto efficiency is achieved when no one is made worse off and at least one person is made better off. See *infra* text accompanying notes 16-17 (defining Kaldor-Hicks efficiency).

7. John Rawls, *A Theory of Justice* 78 (1971).

without knowing their own places in society.⁸ The underlying notion is that rules will be fair if the person making the rules does not know his or her future position.

Rawls offers even less practical help in equity considerations than the Coase Theorem offers in efficiency calculations. The Swygert and Yanes approach begs the question of when the initial position should be invoked in legal decisions. If matters at law are generally decided as if the parties are in an initial position, established rights may be ignored, thereby causing results that are neither fair nor efficient.

Moreover, Swygert and Yanes assume that those in an initial position will be risk averse. This assumption means that any transfers from richer or poorer will be accepted in an initial position. The Swygert and Yanes discussion of risk aversion in a Rawlsian context confuses the matter. They should just recognize the empathy implicit in an initial position and forego the discussion of risk aversion. The initial position simply creates a situation in which risk considerations are relevant because the decisionmaker needs to take into account the fates of all. These risk considerations play the same role as empathy and are unnecessary once empathy is introduced. The initial position does not change the level of risk aversion that people actually have.⁹

Swygert and Yanes also invoke Rawls's min-max notion, according to which an action, to be justified, must increase the well-being of the least well-off person, subject to maintenance of basic rights and liberties. This principle, however, assumes *infinite risk aversion*. This is not the level of risk aversion that people actually exhibit. Nor is this assumption compatible with economic efficiency insofar as it is an incorrect assumption about people's actual preferences—whether or not they are in an initial position. The presumption that individuals behind a veil of

8. John C. Harsanyi, *Cardinal Utility in Welfare Economics and the Theory of Risk Taking*, 61 J. Pol. Econ. 434, 434–35 (1953). In Harsanyi's treatment, the individual recognizes that he or she has an equal chance of being anyone in society. Rawls's concept of the original position is similar but with greater restriction of what one knows in this position (the veil of ignorance). See Rawls, *supra* note 7, at 78.

9. Indeed, Vickrey has shown that (contrary to Swygert and Yanes's assumption) people will maximize expected utility in an original position even assuming risk aversion. William Vickrey, *Measuring Marginal Utility by Reductions in Risks*, 13 *Econometrica* 319, 330 (1945). Expected utility simply includes risk aversion. *Id.*

ignorance will choose equality empirically appears not to be necessarily correct.¹⁰

Suppose, for example, that Bill Gates and the poorest member of society enter into a bargain in which the poorest member will perform yard work for five dollars per hour. After the poorest member has performed 160 hours of work worth \$800, a lawyer for the poorest member sues Gates on the grounds that the bargain between Gates and the poorest member would not have been made if both were in an initial position. Instead the wage would have been at least \$100 per hour, the minimum wage on which the two parties would agree in bargaining from an initial position. Gates thus owes the poorest member at least \$16,000, a result neither efficient nor fair. How would Swygert and Yanes distinguish this case from that of *Walker-Thomas Furniture*,¹¹ which they cite?¹² The alternative that I suggest provides an answer.

Finally, Swygert and Yanes mistakenly rely on the traditional separation of equity and efficiency to support their proposed approach. Economic efficiency has generally been thought to be separate from equity issues such as the distribution of income. Charles Fried's views are representative.¹³ According to Fried, economic analysis of rights uses a concept of efficiency that is removed from distributional questions. Thus, because economic analysis does not consider whether the distribution is fair or just, the fact that a given outcome is efficient does not give it "any privileged claim to our approbation."¹⁴ Similarly, Posner notes, "[T]here is for good or ill nothing in the ethic of wealth maximization which says that society has a duty to help the needy In this regard, wealth maximization is at one with individualist political philosophy, but both are out of phase with powerful currents of contemporary moral feeling"¹⁵

10. Ed Bukszar & Jack L. Knetsch, *Fragile Redistribution's Choices Behind a Veil of Ignorance*, 14 J. Risk & Uncertainty 63, 72 (1997).

11. *Williams v. Walker-Thomas Furniture Co.*, 198 A.2d 914 (D.C. 1964).

12. In both cases, Swygert and Yanes assume risk aversion, which is what drives their result.

13. Charles Fried, *Right and Wrong* 93 (1978).

14. *Id.* at 94.

15. See Richard A. Posner, *Wealth Maximization Revisited*, 2 Notre Dame J.L. Ethics & Pub. Pol'y 85, 101 (1985) [hereinafter Posner, *Wealth Maximization Revisited*]. Posner's inconsistency in defining economic efficiency and his use of it on occasion in a utilitarian manner has led one commentator to refer to Posner's approach to law and economics as "quasi-scientific mysticism." Robin Paul Malloy, *Letters from the Longhouse: Law, Economics and Native American Values*, 1992 Wis. L. Rev. 1569, 1621. Elsewhere Posner has noted that wealth maximization is the same thing as KH efficiency. Richard A. Posner, *Wealth Maximization and Judicial Decision Making*,

These assumptions are profoundly wrong because they ignore both the nature of a good in economic analysis and what I call “the regard we have for others” that is an integral part of economic efficiency. Because these assumptions are common throughout much of the legal and economic literature, one can understand why Swygert and Yanes rely on them. Nevertheless, these assumptions fail to consider carefully the nature of economic efficiency.

Economic efficiency for policy purposes is Kaldor-Hicks (KH) efficiency. KH efficiency says (approximately) that a change is efficient when the winners from the change could, in principle, compensate the losers.¹⁶ No actual compensation need take place to ensure that a change satisfies the KH test. The gains to winners are measured by their willingness to pay (WTP) for them. Losses are to be measured by the losers’ willingness to accept (WTA) payment as compensation for the loss. Thus, a change is efficient when the sum of the WTPs for the change exceed the sum of the WTAs for the change across all people who care about the change.¹⁷

A “good” in economic analysis is defined by what people care about. They care about equity. People care about the fairness and efficiency of rules, for example, so that these attributes of decisions are also economic “goods.” They will often care not just about the cost of a project but also

4 Int’l Rev. L. & Econ. 131, 135 (1984); see also Richard A. Posner, *Economic Analysis of Law* 13 (4th ed. 1992).

16. See Richard O. Zerbe Jr. & Dwight D. Dively, *Benefit Cost Analysis in Theory and Practice* 96–98 (1994).

17. The concept of KH efficiency is well captured in the following example:

You are asked to compare two worlds. The first is the status quo: the world the way it is now. The second is identical with the status quo except for the change brought about by the project. In the comparison, you take into account the ramifications of the project, differences in income to you and others, differences in habitat, and so on; but except for the changes brought on by the project, the two worlds are the same.

Suppose that you value the first world more highly than the second Then you are asked what is the minimum you need to be compensated so that you would value the change (with the compensation) just as much as the status quo. If you value the world with the project more than the status quo, then you are asked how big a payment you could make in the changed world (with the project) so that you would just value equally the status quo The economic criterion says that if the sum of all the compensations (to those who would lose by the project) is less than the sum of the equilibrating payments (from the gainers from the project), then the change from the status quo is worth making.

Talbot Page, *Environmental Existentialism*, in *Ecosystem Health: New Goals for Environmental Management* 97, 102 (Robert Costanza et al. eds., 1992). See generally W.A.S. Hewins, *Economics*, in 7 *Encyclopædia Britannica* 899, 900 (11th ed. 1911).

who pays for the project, and whether the beneficiaries are deserving. They will care about the income distribution. For these reasons, equity is a logical part of economic efficiency. For any good that people care about, we can in principle determine an aggregate WTP to obtain that good and an aggregate WTP to give up the good. Since people care about equity and fairness,¹⁸ there will be a KH test that can be applied to fairness, to equity, and to the income distribution. Thus, the concept of economic efficiency applies to considerations of fairness and to equity.¹⁹

II. A MORE PRACTICAL ALTERNATIVE

Benefit cost analysis is a well-established technique for determining the KH efficiency of public projects. If equity can be shown to be a part of efficiency, then a long-standing and practical technique is made available to consider equity aspects of public policy. As a matter of logic, economic efficiency necessarily includes equity considerations.²⁰ This integration I have called "Kaldor-Hicks-Zerbe" (KHZ) efficiency. Because economic efficiency has practical application, so does equity when considered as part of economic efficiency.²¹

Notice that the KH test includes the sentiments of all of those who care about the proposed change(s). Thus, the test includes what I call "the regard of others." People will care about others or about outcomes even when they themselves are not otherwise directly affected. The regard of some for the social welfare of others is well established.²² One expression of the concern for others arises when we are concerned about the appropriate application of principles of justice in situations in which we ourselves are not directly affected. Empathy logically plays an

18. According to Mayr, an eminent evolutionary biologist, people will care about others, even others to whom they are not related. See generally Ernst Mayr, *This Is Biology* (1997).

19. See Richard O. Zerbe Jr., *Is Benefit Cost Legal? Three Rules for Benefit Cost Analysis*, 17 J. Pol'y Analysis & Mgmt. (forthcoming 1998). The major treatment is given in Richard O. Zerbe Jr., *The Foundations of Kaldor-Hicks Efficiency in Law and Economics: On the Kindness of Strangers* (University of Washington Graduate School of Public Affairs & School of Law Working Paper in Public Policy Analysis and Management No. 97-11, 1997) [hereinafter Zerbe, *Foundations*].

20. Zerbe, *Foundations*, *supra* note 19.

21. See *supra* note 19. Posner points out that in economics, wealth is not just money wealth. Posner, *Wealth Maximization Revisited*, *supra* note 15, at 86-87.

22. See generally Fay Lomax Cook & Edith J. Barrett, *Support for the American Welfare State: The Views of Congress and the Public* (1992); Fay Lomax Cook, *Who Should Be Helped: Public Support for Social Services* (1979).

important role in KH efficiency. The separation between efficiency and equity is then convenient but artificial.

As long as the income distribution is valued, it will be one of the goods that must be considered in the choice between the status quo world and the changed world. In terms of KH, a change in income distribution has a value, positive or negative, that can be determined by the WTP or the WTA and in this respect is like any other good. To illustrate, ask yourself if you would pay one dollar to live in a world in which income inequality was less by fifty percent than in the present world, without otherwise affecting your own income or total income. If you answer yes, you have indicated a WTP for the change. You and others will care whether an additional dollar is received by, say, Bill Gates or by the poorest member of society, and KH requires that this regard be counted.

Posner speaks about the problem in which, "if the initial allocation is thought unjust, the change, while increasing the wealth of the society, may actually be carrying it further away from the just allocation."²³ Yet if we care about justice, the change is in fact not KH efficient unless the gain in other forms of wealth is sufficient to offset income distributional consequences of projects as well as social norms generally. Thus, the distributional effects of a policy can be treated like any other good for which there is a WTP or WTA and incorporated into a benefit cost analysis.²⁴

The basis of benefit cost analysis is the KH criteria. Benefit cost analysis incorporates well-developed techniques to determine economic efficiency. By incorporating equity into the traditional calculation of benefits and costs, a practical and established approach that I call "KHZ efficiency" is available to consider equity effects. KH and Pareto efficiency take into account equity and fairness. They take into account the sentiments of others.

The goal is to have decisionmakers act impartially in treating parties instead of considering parties as if they are in an initial position.²⁵ In the

23. Richard A. Posner, *The Justice of Economics*, *Economia Delle Schelte Pubbliche* 15, 23 (1987).

24. Although the KH criteria assume that a dollar is worth the same to all, individuals may consider the different capacities of enjoyment that others have, and this may be incorporated into their WTP or WTA for others. See the commentary of the Biscuit on the relative capacities of the rich T. Patterson Frisby and the poor Biscuit to enjoy income. Pelham G. Wodehouse, *Big Money* 177-78 (Penguin Books 1953) (1931).

25. Swygert and Yanes create a modification of Rawls's original position that is in fact the same as Harsanyi's initial position. I will therefore refer to the "initial position."

real world, judges make decisions that take into account this expanded concept of efficiency. Judges act according to a norm, a norm that expects them to dispense justice; they use the language of justice. One example from the Irish Land Law of 1881 is illustrative. In *Gilmore v. M'Kelvey*,²⁶ the court uses the language of justice, illustrates the regard for others, and shows concern for the income distribution. The court states:

With respect to the question of value, the court is perfectly unanimous. One can not help having a certain feeling with respect to a gentleman who having in 1878 voluntarily and without coercion taken a couple of fields outside the town from a lady, not very wealthy, at a rent of £30 a year, comes in the year 1882, and seeks to get a perpetuity in that land as against her at a rent of £12 15s. I have no doubt Mr. Gilmore reconciled himself to the transaction, *but there are many people who would not.*²⁷

Consider a hypothetical project to remove a dam on the Elwha river in Washington State. This project will materially enhance fishing possibilities but will result in higher electricity rates for certain rich residents of a nearby city. Many of those who will benefit from the greater fishing possibilities are poor or of middle income level. Table 1 shows hypothetical net gains and losses by income group as measured by the aggregate WTP or WTA (for losses) by group. Table 1 tells us that fifty million dollars is the measure of the gain to those in the bottom one-third of the income distribution. This is measured by the aggregate WTP of those poor people affected by the project. The sum of fifty million dollars is the aggregate value of dam removal for those in the bottom one-third of the income distribution. This project does not pass a traditional efficiency test as shown in the column "total net benefits," which shows negative net benefits of one million dollars.

26. See E.O. MacDevitt, *Land Cases, Being a Collection of Reports of Decisions Under the Irish Land Acts Since the Passing of the Land Law (Ireland) Act 201 (1884)*.

27. *Id.* (emphasis added).

Table 1
Narrow Efficiency
(millions of dollars)

<i>Income Group</i>	poor	middle income	rich	total net benefits
<i>Net Benefits</i>	+50	+29	-80	-1

This test can be expanded to take into account the sentiments of others. Suppose that others care positively about transfers to the poor. The question is how much others are willing to pay for the gain to the poor. Assume that income gains to the poor are valued by others. What value would these gains have to others? What one is willing to pay for a good is always limited to what one must pay for a perfect substitute. In this case, the substitute good is the most efficient purely distributional project that accomplishes the same distributional purpose. Harberger suggests that, at most, the administrative costs of transferring money to the poor by the most efficient method available are twenty percent of the amount of the money transferred.²⁸ A transfer of fifty million dollars to the poor, therefore, would cost ten million. That is, we can say that, at most, the measure of the value of income gains by the poor to others is ten million dollars. Call this the transfer benefit. Table 2 shows the benefit cost calculation including the transfer benefit.

Table 2
Combining Narrow Efficiency and Equity into General Efficiency
(millions of dollars)

<i>Income Group</i>	poor	middle income	rich	transfer benefits	total net benefits
<i>Net Benefits</i>	+50	+29	-80	+10	+9

28. Arnold C. Harberger, *On the Use of Distributional Weights in Social Cost-Benefit Analysis*, 86 J. Pol. Econ. S87-S120 (1978).

By considering the value of the distributional change to others, a project that at first appeared inefficient now proves to be efficient. We have evaluated the improvement of the income distribution on the same basis as other goods. The project is an efficient way to transfer income to the poor.

III. COMPARING THE SWYGERT AND YANES APPROACH WITH THE KALDER-HICKS-ZERBE APPROACH FOR LEGAL DECISIONS

Swygert and Yanes consider a series of legal decisions for which they claim their approach produces superior results. Yet all of these cases can be analyzed more effectively from the standpoint of expanded efficiency. The initial position adds no more information in these cases than already provided by efficiency analysis.

One class of cases considered by Swygert and Yanes involves gratuitous promises for benefits previously received. In these cases, a promisor makes an offer to reward a deserving person for having performed a deserving act of value to the promisor. The promise is, however, not enforceable since there is no contract. Swygert and Yanes believe that efficiency is not a sufficient consideration to yield this result because the promisor gains nothing. The act the promisor appreciates is performed in any event.

In an initial position, according to Swygert and Yanes, the promise must be enforceable because either party could foresee being the injured promisee. That is, Swygert and Yanes assume that the compensation is worth more to the promisee than to the promisor. In economic terms there is declining marginal utility of income.

If compensation is, in general, worth more to promisees than to promisors, then it is efficient to require compensation. It is not the initial position that needs to be invoked, just the actual situation that includes further promisors and promisees. Consider a proposed law that would make liable one who avoids harm as a result of an action of a deserving person. The law would make the person liable for damages incurred by the deserving person in performing the harm-reducing action up to the value of the harm avoided. Suppose further that no additional acts of kindness (saving others from harm) will be produced by this law, so that it is not efficient in the sense used by Swygert and Yanes. People will recognize that additional money is worth more to them in the situation of the promisee than the promisor. The WTP for the change in the law will exceed the WTA of those opposed, and the change will be efficient.

Even if the income were worth the same for both parties, people may see a requirement of enforceable promises in this situation as fair. The prevailing sentiment will be in favor if enough people feel strongly enough that payment is fair. Then, again, the proposed change in the law will simply be efficient by definition. That is, the aggregate WTP to make the legal change will exceed the WTA of those against the change. Insofar as individuals regard this proposal as fair, this will be reflected in their WTP for it. Thus, the change may be efficient, but there is no need to invoke the initial position.²⁹ The key assumption is the declining marginal utility of income, not the initial position.³⁰

Use of the initial position in the context of the Coase Theorem may lead to the wrong result. Suppose that most people regard the change as fair, but it turns out that the cost of adjudicating the new law, perhaps because of the difficulty in determining the magnitude of harm avoided, is so great that the change is not efficient and is not desired. An analysis of the legal change according to the Coase Theorem, where the individuals are in an initial position, fails to take into account these administrative costs and wrongly concludes that the change is efficient.³¹

The authors also analyze judicial consideration of non-economic values. In particular they consider the *Peevyhouse* case.³² They fault the court for not considering the value to the landowner of "requiring the restoration of the landowners' property," in short for not demonstrating empathy with the landowners who valued the appearance of the land.³³ The value of restoration, however, is an economic good, notwithstanding that Swygert and Yanes assume this value to be much greater than the

29. Even if the actual position is one in which individuals know beforehand whether they will gain or lose, the initial position adds nothing to the analysis. Again, we cannot say that were these individuals to bargain in an initial position, they would arrive at a solution requiring compensation to the deserving person unless we can assume that individuals regard compensation as fair.

30. KH efficiency assumes away declining marginal utility of income, but the definition of efficiency can be and sometimes is easily expanded to account for the assumption. See Zerbe & Dively, *supra* note 16, at 98.

31. Similarly, in cases of gratuitous promises inducing reliance, there is no need to resort to an initial position to determine fairness; it is efficient to prevent wasteful reliance.

32. *Peevyhouse v. Garland Coal & Mining Co.*, 382 P.2d 109 (Okla. 1962).

33. Swygert and Yanes say the court was unable "to stand in the shoes of both parties." Swygert & Yanes, *supra* note 1, at 323. This is, however, a claim that the court was not impartial, not that bargaining in the initial position was at issue. Indeed the actual bargain called for restoration. *Peevyhouse*, 382 P.2d at 111.

fall in the market price of the land.³⁴ The Swygert and Yanes argument must be, simply, that the result in *Peevyhouse* is inefficient.

Swygert and Yanes also find a discrepancy between fairness and efficiency arising where disparity of bargaining power exists. Discrepancies in bargaining power are, however, notoriously difficult to define economically other than as arising in the presence of monopoly or monopsony. Most of the cases that find a bargaining power disparity are not instances of monopoly or monopsony.³⁵ Swygert and Yanes see the need to apply non-efficiency considerations only in non-competitive situations. Competition is, however, neither a necessary nor a sufficient condition to a finding of outcomes that offend the public conscience. For example, in *Williams v. Walker-Thomas Furniture Co.*,³⁶ one of the most noted unconscionability cases, no one, as far as I am aware, has suggested that Walker-Thomas had monopoly power.

The problem with an unconscionability case is how to decide when it is an unconscionability case.³⁷ Swygert and Yanes suggest that the bargain was too one-sided and that the contract gave Walker-Thomas more collateral than it needed.³⁸ This is, however, just an allegation that the contract was inefficient. They suggest that the result would be different if both parties were bargaining in an initial position. Swygert and Yanes thus change the question from one of determining unconscionability to one in which they must ask how to decide when the initial position is the correct analytic viewpoint. It is unclear there is any gain from moving from the first to the second question.

If Walker-Thomas, operating in a competitive industry, had more collateral than necessary in the instance involving Mrs. Williams, there

34. The discrepancy between the cost of restoration and the fall in the value of the land suggests that the landowners had peculiar tastes if restoration was really worth that much to them and not to potential buyers.

35. Talbott has shown that Rawls's approach does not work for certain types of cases thought to contain unconscionable exculpatory clauses. W.J. Talbott, *Cost Spreading and Benefit Spreading in Tort Law*, 11 Res. L. & Econ. 25 (1988).

36. 198 A.2d 914 (D.C. 1964). In this case, a single mother with seven children and limited education purchased many household items from Walker-Thomas Furniture Company over a six-year period under an installment plan. The contract provided that if an account was not paid in full, all items would be forfeited. Walker-Thomas reclaimed all of the items even though the total balance due was \$678. *Id.* at 915-16.

37. Note that if we do not assume declining marginal utility of income then the Swygert and Yanes approach fails to suggest anything wrong with the original contract, absent inefficiency.

38. If Walker-Thomas were claiming too large a collateral, both parties would be served by a change in contract.

may have been other instances of repossession in which collateral was too small to cover the loss, so it is unclear that the contract was inefficient if only the bargaining parties are involved. Nevertheless we may not wish the “Mrs. Williamses” to bear the burden that these contracts impose. We may wish to limit the extent of collateral that may be offered even though some people may be harmed by being unable to secure credit. If our WTP for this change in contract provision is sufficiently large, then it is efficient to offer greater protection to the “Mrs. Williamses.” The regard of others is the way to distinguish *Walker-Thomas* from the earlier example of Bill Gates and the gardener.³⁹

IV. CONCLUSION

Neither Kaldor-Hicks nor Pareto efficiency rises above the sentiments of their times. They rest on the actual sentiments of society. These sentiments recognize existing rights as extant. These concepts of economic efficiency would have judges accept as starting points well-settled rules and rights.⁴⁰ In considering changes in rights at the margin, these sentiments should govern. Truly efficient results accord with the notions of fairness imbedded in culture. The initial position is a device for thinking about fairness when fundamental principles or rights are at stake, that is, in considering constitutional questions. The suggestion that judges should think of parties before the law as being in initial positions may in fact be unfair.

A benefit cost framework that incorporates equity as a good holds more promise for incorporating equity and efficiency in a practical way than does the approach of Swygert and Yanes. It grounds the integration in the actual world and not in the world of zero transaction costs and the initial position. It relies on an established technique, and it frames the questions correctly even where answers are unclear.⁴¹

39. See *supra* p. 352.

40. See Paul Heyne, *The Foundations of Law and Economics: Can the Blind Lead the Blind?*, 11 Res. L. & Econ. 53, 59 (1988). Perhaps Swygert and Yanes contemplate situations in which judges would rise above the sentiment of the times and appeal to more advanced moral ideas. Yet what these more advanced ideas might be remains unclear.

41. I have introduced this method elsewhere. See *supra* note 19 and accompanying text.

