

AMERICAN UNIVERSITY OF BEIRUT

ASSESSING LIBERTARIAN PATERNALISM THROUGH
JOHN NEVILLE KEYNES' TRIPARTITE CATEGORIZATION
OF ECONOMICS

by
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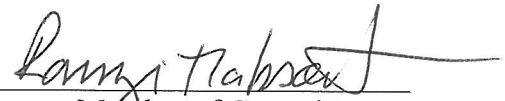
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AN ABSTRACT OF THE THESIS OF

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Libertarian paternalism has been recently advocated by behavioral economist Richard Thaler and legal scholar Cass Sunstein as a form of paternalism distinguished by its libertarian nature. Libertarian paternalism draws on the findings of new behavioral economics in order to justify choice architecture and nudge theory. However, paternalism has been criticized over time on the ground that it obstructs the promotion of welfare through value substitution, hinders freedom of choice, and violates the dignity of autonomous beings. Therefore, the question of whether libertarian paternalism is a modified or a reinvented form of paternalism has recently arisen.

This thesis adopts the tripartite categorization of economics advocated by John Neville Keynes in the late 19th century in order to assess libertarian paternalism. Neville Keynes identifies three aspects of economics namely the positive aspect, the normative aspect and the art of economics. As such, new behavioral economics qualifies as the positive part of libertarian paternalism, paternalism as the normative part, and the application of libertarian paternalism to public policy as the art of economics. Evaluating libertarian paternalism through Neville Keynes' tripartite categorization shows that libertarian paternalism is not a complete theory yet.

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CHAPTER I

INTRODUCTION

The rational utility-maximizing agent assumed to exist in orthodox economic models has been empirically challenged. Instead, a complex and logically fallible human inhabits the world. However, humans are bombarded with millions of decisions to make. In addition, as the number and variety of choices increase, the decision making process becomes more complex. If humans were able to make the correct decisions every time, then problems such as poverty, obesity, unemployment, pollution, divorce and the like would be less prevalent. However, the ubiquity of these ills signals that much of human decisions could be based on flawed reasoning.

Economists dissatisfied with the assumptions of orthodox economics sought to challenge its underlying principles of unbounded rationality, unbounded self-control, and unbounded willpower. Thus, behavioral economics was founded. Behavioral economics incorporates psychological and cognitive findings that explain decision making processes. Behavioral economics establishes that humans are susceptible to cognitive biases and heuristics such as default rules, framing effects, and starting points. As such, their decisions are not always optimal.

Drawing on the findings of behavioral economics, economist Richard Thaler and legal scholar Cass Sunstein have advocated the need for choice architecture in order to direct people toward what is best for them while incurring minimum costs and preserving freedom of choice. This architecture will, allegedly, aid people in vast ways

including following a healthy lifestyle, saving more for their old age, making profitable investments, decreasing energy consumption etc... Their theory of libertarian paternalism may be considered the most recent manifestation of paternalism. However, paternalism has been heavily criticized over time on the ground that it violates the freedom and dignity of autonomous beings and hinders the promotion of welfare through value substitution which involves substituting people's interests and ends with those of the policymaker. In light of the implications of paternalism, does libertarian paternalism emerge as a modified form of paternalism that can respond to its critics?

This thesis offers a positive and normative evaluation of libertarian paternalism. It follows the tripartite distinction between positive economics, normative economics, and the art of economics as advanced by John Neville Keynes in 1891. Positive economics is concerned with studying facts; normative economics is concerned with studying norms, rules, and ideals; whereas the art of economics explores policy applications (Hands, 2001). Applied to the realm of this work, behavioral economics falls under positive economics; paternalism falls under normative economics; whereas applying behavioral findings to paternalism generates a new theory, libertarian paternalism, which combines positive and normative aspects and is thus necessary for policy recommendations.

This thesis has five parts. The first part, "Behavioral Economics: An Overview", provides a historical background of the link between psychology and economics which led to the emergence of behavioral economics. The second part, "Paternalism and Libertarian Paternalism", explains the different interpretations of paternalism over time

until its most recent version, libertarian paternalism. The third part, "A Positive Critique", questions the libertarian paternalistic choice of resorting to new behavioral findings and dismissing old behavioral findings. The fourth part, "A Normative Critique", offers a critical scrutiny of paternalism and libertarian paternalism on the grounds of welfare, freedom, and dignity of autonomous beings. The final part, "Libertarian Paternalism and Policy Making", situates libertarian paternalism in the field of public policy and investigates whether its proponents can respond to three critiques pertaining to its public policy implications.

CHAPTER II

BEHAVIORAL ECONOMICS: AN OVERVIEW

Orthodox economics is defined on the assumption of a rational world inhabited by calculating, unemotional, and maximizing beings known as rational economic man or Homo Economicus (Thaler & Mullainathan, 2008). There is a connection that will not be explored in this paper between the rational economic man of orthodox economics and libertarian philosophy (Burgin, 2013; Harcourt, 2011; Jones, 2012). This subject requires a study that would take us beyond the scope of this paper. Our focus here is on how, over the years, orthodox economics has overlooked and resisted integrating the findings of cognitive and social psychology. Orthodox economics assumes that consumer choices are independent of defaults, frames, and price anchors. In orthodox economics, furthermore, economic agents base their decisions on cost-benefit studies and pre-existing preferences. Thus, in this sense, decisions will always be optimal (Barden et al., 2014). The rational agent portrayed in orthodox economics had backers that believed that the model was descriptively correct but the majority defended the model because it implied an easy and pragmatic method to formalize the findings of orthodox economics. However, when behavioral economics emerged it was critical of both, those who supported the model on the rationale that it is descriptively correct and those who supported the model on the rationale that it is practical (Thaler & Mullainathan, 2008). In the 1970's behavioral economics emerged and this chapter will

outline its historical development as well as its bond with psychology. Therefore, this chapter deals with the positive foundation of libertarian paternalism namely, behavioral economics.

A. The Historical Context of Behavioral Economics

Behavioral economics has emerged as the hybrid offspring between two disciplines namely economics and psychology. Behavioral economics draws insights from cognitive and social psychology in order to study the human decision making process. As such, it is important to examine the historical connections between these two disciplines.

Before psychology was established as an independent field of research, numerous economists delved into psychological study. One example is Adam Smith (1723-1790) who established the psychological foundations of individual behavior in his book "The Theory of Moral Sentiments". Smith's views on human psychology have paved the way for recent developments in behavioral economics (Camerer & Lowenstein, 2002). Smith's statement that "we suffer more... when we fall from a better to a worse situation, than we ever enjoy when we rise from a worse to a better" refers to the modern behavioral finding of loss aversion (Smith, 1759, p. 214). Another example is Jeremy Bentham (1748-1832) who prolifically researched the underlying psychological disciplines of utility. Also, Francis Edgeworth (1845-1926) presented his prominent box or diagram through his Theory of Mathematical Psychics. His diagram conveys yet another finding of behavioral economics since the two persons negotiating outcomes

have utilities that are influenced by the other's payoff (Camerer & Lowenstein, 2002). Therefore, psychology has been prevalent among economic works.

Economics as a field of study therefore enjoys an older history than psychology. In the eighteenth century, psychology was considered only complementary to moral philosophy. However, in the nineteenth century, the discipline of physiology which regarded the whole body to be a machine prospered. This helped psychology, which held the mind to be a machine, to flourish. As such, psychology had a mechanistic view towards humans (Sent, 2004). As a result, economists including Francis Ysidro Edgeworth, Richard Jennings, and William Stanley Jevons integrated the psychological findings on sensation, response, and stimulus into economics. However, the mechanistic view of the human mind advocated by early psychologists was criticized with the growth of Freudianism and its underlying foundations in repressed memories and the unconscious, which economists rejected. As a result, economists expunged psychology from economics (Sent, 2004).

In the first part of the 20th century, the extent of psychology that existed in economics was limited (Sent, 2004). Economists including Irving Fisher and Vilfredo Pareto published works which encompassed assumptions about how decision makers think and feel about economic choices. Lionel Robbins in 1938 criticized interpersonal comparisons of welfare. He argued that since utility can only be accessed via introspection it is not measurable and it is unscientific to compare utility levels among different individuals (Hands, 2012). In addition, Paul Samuelson's 1938 paper "A Note on the Pure Theory of Consumer's Behavior" states that even though the ordinal

revolution led by Hicks and Allen (1934), Pareto (1927), and Slutsky (1934) had succeeded in distancing economics from hedonistic and cardinal notions of utility, their revolution was not yet complete. Samuelson states that: "... despite the fact that the notion of utility has been repudiated or ignored by modern theory, it is clear that much of even the most modern analysis shows vestigial traces of the utility concept ... I propose, therefore, that we start anew in direct attack upon the problem, dropping off the last vestiges of the utility analysis" (Samuelson, 1938, p.62). He accordingly called for the utter eradication of the concepts of utility and preference from the theory of consumer choice. However, in 1953, Milton Friedman successfully sought to protect the underlying assumption that human beings are rational decision makers from any criticism. Friedman argued that economic theories should not be judged based on psychological assumptions but rather on the accurate predictions they generate through their wide applications. As such, psychological discussions mostly disappeared from economic works (Sent, 2004).

In 1963, Friedman's claims were criticized most surprisingly by Paul Samuelson himself. However, it was Herbert Simon (1916-2001) who sought to rebuild the tightly knit bond between psychology and economics. As such, Simon's efforts partly assisted in transforming the notion of psychology in the mid-20th century through his input in the cognitive revolution which aimed to reduce the relevance of behaviorism in psychology. The cognitive revolution in psychology resuscitated the notion of the mind and internal psychological processes. As such, the door for renewed links between psychology and economics was opened (Sent, 2004).

In summary, the connection between psychology and economics has not been stable over time. The extent of psychological considerations in economics has been significant in the early 19th century. However, psychology was disregarded from economic research during the late 19th and early 20th century. Nevertheless, the cognitive revolution resurrected the broken connection between the two disciplines in the mid-20th century. As such, many economists embraced psychological findings anew.

B. The Growth of Behavioral Economics

Esther-Mirjam Sent (2004) posits that behavioral economics underwent two stages of development that molded it into its current form. She coins the first stage as "old behavioral economics" and the second as "new behavioral economics". She explains that the former is an early incarnation of the latter. Both stages will be looked at closely below.

1. Old Behavioral Economics

The 1960's witnessed the first signs that psychology was making its way into economics. Thus, explicit references to behavioral economics started to appear. Sent (2004) identifies four major groups who contributed to the development of old behavioral economics. The first and most notable group was comprised of a number of researchers at Carnegie including Richard Cyert, James March, and Herbert Simon. They emphasized the importance of bounded rationality, satisficing, and simulations and focused mainly on analyzing firm behavior. The second group consisted of an

assembly of researchers at Michigan headed by George Katona. They were heavily concerned with consumer behavior and macroeconomic issues. The third group was made up of researchers at Oxford including P.W.S. Andrews, D.M. Lambertson, H. Malmgren, J. Marschak, G.B. Richardson, and G.L.S. Shackle. They focused on case studies, uncertainty and coordination. The final group included Stirling scholars such as Neil Kay, Brian Loasby, Richard Shaw, John Sutton, Andrew Tylecote, and Peter Earl. They concentrated on eclecticism and integration in their works. As such, the contributions of these different clusters shaped old behavioral economics.

Despite the existing diversity between the works of these four schools, their approaches were similar in two ways. First, they shared disappointment with orthodox economics and its concerns with profit, utility maximization, and equilibrium. Second, they expressed their willingness to develop a substitute model based on cognitive and psychological findings (Sent, 2004).

In summary, old behavioral economics was formed through the works of four groups of researchers during the 1960's. Even though variety characterized their publications, they conceded that the orthodox economics model was dissatisfactory and expressed the urge to develop an alternative.

2. New Behavioral Economics

The origins of new behavioral economics emerged in the early 1970's particularly in the works of Amos Tversky and Daniel Kahneman. The two researchers assessed the cognitive character of conformity or divergence from the principles of expected utility

maximization and Bayesian probability judgments (Sent, 2004). As such, Tversky and Kahneman provided a friendly challenge to orthodox economics.

The findings of Tversky and Kahneman can be divided into three major categories namely heuristics and biases, framing effects, and prospect theory (Sent, 2004). Their insights will be discussed below.

a. Biases and Heuristics

The joint work of Tversky and Kahneman, in addition to the collaboration of other researchers, has carved the basic building blocks of behavioral economics. Tversky and Kahneman introduce the notions of heuristics and biases in a 1974 article titled "Judgment under Uncertainty: Biases and Heuristics". They define heuristics as a limited number of principles that people resort to in order to "reduce the complex tasks of assessing probabilities and predicting values to simpler judgmental operations" (p.1124). They further admit that despite the advantages promoted by heuristic principles, they sometimes yield systematic errors called biases. However, Kahneman (2002) admits that the definitions of heuristics and biases proposed in his 1974 article were vague. Later, Kahneman provides a more explicit definition whereby "a judgment is said to be mediated by a heuristic when the individual assesses a specified target attribute of a judgment object by substituting a related heuristic attribute that comes more readily to mind" (p. 707).

A myriad of biases and heuristics were described by Tversky and Kahneman. It is noteworthy to mention that according to White's (2013) interpretation of heuristics and

biases, they are not blunders that average out over time but rather, they represent consistent and anticipated mistakes that are embedded in us due to years of natural selection. Therefore, they can't be easily amended. A few common anomalies noted by Tversky and Kahneman include the endowment effect which occurs when one overvalues an owned good regardless of its market value; optimism bias which implies that one overestimates the probability of positive events and underestimates that of negative events; status quo bias which refers to one's inclination to keep things as they are by fixating on a previously made decision thus dropping all other viable alternatives that may be better; and projection bias which implies that one expects his tastes and preferences to be stable over time, etc... (Barden et al., 2014)

b. Framing Effects

Kahneman and Tversky (1981) define a decision problem as "the acts or options among which one must choose, the possible outcomes or consequences of these acts, and the contingencies or conditional probabilities that relate outcomes to acts" (p. 453). In addition, they describe the decision frame as the "decision-maker's conception of the acts, outcomes, and contingencies associated with a particular choice" (p. 453). They explain that when faced by a choice, a decision maker resorts to a frame that is under the influence of two factors namely the way the problem is constructed and his norms, habits, and personal characteristics. As such, framing a decision problem in various ways yields different choices.

In order to illustrate the framing effect, they introduce their well-known Asian disease problem (1981) in which respondents are told that the United States is preparing for the eruption of a rare Asian plague that is projected to generate 600 casualties and are asked to choose between two alternatives. The choice problem is presented in a different formulation to two groups of students. On the one hand, the first group was faced with the following two alternatives to combat the disease: Program A will save 200 people if implemented and Program B has a one third probability to save 600 people and a two third probability of saving no people. 72% of respondents chose the first option while 28% chose the second. The results show that the majority of respondents acted in a risk-averse manner whereby they chose the certain outcome of saving 200 lives rather than choosing the risky prospect of equal expected value which is a one third chance to save 600 lives.

On the other hand, the second group was given a different set of alternatives: Program C will generate 400 casualties if implemented whereas Program D has a one third probability that no one will die and a two third probability that 600 people will die. 22% of respondents chose Program C and 78% chose Program D. The results indicate that the majority are risk takers whereby they are less attracted to choose the imminent death of 400 people over the two third chances that 600 people will die.

Kahneman and Tversky (1981) explain that the only difference between the two sets of alternatives presented is the way in which the outcomes are framed. The first set is outlined in terms of number of lives saved whereas the second set is defined by number of lives lost. Despite the fact that the outcomes are identical, results show that when

decision makers are faced with a choice involving gains, they are risk-averse whereas when they are faced with a choice involving losses, they are risk-taking. Thus, the variations in results are explained by the framing effect with conflicting attitudes about risks in situations involving gains and losses.

c. Prospect Theory

Kahneman and Tversky (1979) criticize expected utility theory as a descriptive model of decision making under risk and develop an alternative model which they refer to as prospect theory. They reason that when choosing among risky alternatives, individuals are subject to prevalent effects that are incompatible with the principles of utility theory. In specific, the certainty effect whereby people underestimate probable outcomes compared to certain outcomes generates risk-averse behavior in choices involving gains and risk seeking behavior in choices involving losses. Moreover, the isolation effect whereby people discard common components among prospects yields inconsistency in preferences when the decision problem is framed in a different manner. Under prospect theory, value is defined in terms of gains and losses not final assets whereas probabilities are substituted by decision weights. As such, prospect theory diverges from expected utility theory.

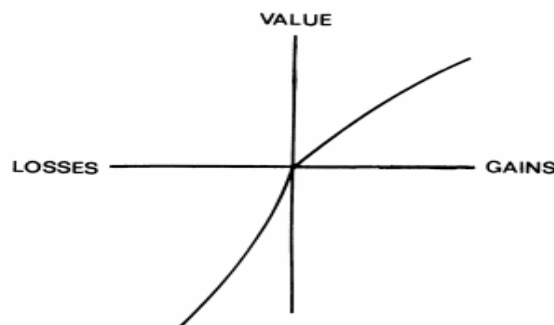
Under prospect theory, people make decisions grounded in choices that are defined in terms of prospects. Kahneman and Tversky (1979) define a prospect (x_i, p_i) as a contract that generates outcome x_i associated with probability p_i where the sum of p_i is 1. They further explain that prospect theory is comprised of two stages that characterize

the choice process namely editing and evaluation. The former involves a preliminary analysis of the prospects under representation and thus generates a simple representation of prospects. The latter consists of evaluating the edited prospects and selecting that with the highest value. The overall value of an edited prospect, represented by V , is expressed via two scales namely π and v . The first scale π attributes to each probability p a decision weight $\pi(p)$ which shows the relative importance of p on the total value of the prospect. The second scale v assigns to each outcome x a number $v(x)$ which reveals the subjective value of that outcome. Given that outcomes are measured relative to a reference point, v is thus a measure of deviations from the reference point. In other words, v measures gains and losses.

Thus, Kahneman and Tversky (1979) explain that an outcome is assessed according to the following value function:

$$V(x, p; y, q) = \pi(p)v(x) + \pi(q)v(y)$$

Furthermore, they represented a hypothetical value function by the following graph:



They explain that the value function is normally concave for gains, commonly convex for losses, and is usually steeper for losses than for gains. Decision weights are

generally lower than the corresponding probabilities, except in the range of low probabilities.

In conclusion, this chapter has reviewed the historical bond that has existed between psychology and economics. The irregularity of this connection has caused economics to adopt psychological findings at some times and abandon them at other times. However, the cognitive revolution in psychology has fixed this bond paving the path for the field of behavioral economics to develop. As such, behavioral economics challenged the foundations of orthodox economics and suggested that human choice is not always optimal. Therefore, the need to correct the deviation of human decisions from what is optimal arises. This explains the renewed interest in paternalism in the early 21st century.

CHAPTER III

PATERNALISM AND LIBERTARIAN PATERNALISM

Following the tripartite categorization Neville Keynes developed in the late 19th century, paternalism here is the normative aspect of libertarian paternalism. In its broadest sense, paternalism is defined as the "interfering with a person's freedom for his or her own good" (Andre & Velasquez, 1991). It has not yet been established whether paternalism counts as a movement, theory, revolution, or simply an idea. However, paternalism arises in a variety of domains, in the private and public sphere and encompasses a wide range of applicability. For example, the government may require people to contribute to compulsory retirement savings plans. The civil law may prohibit the enforcement of contracts that serve gambling debts. Doctors may conceal the truth from the family of a car accident victim by telling them that he died instantly instead of confessing that he suffered horrifically. A husband may hide sleeping pills from his depressed wife (Dworkin, 2014). This chapter will highlight the various interpretations of paternalism over time reaching its most recent manifestation as libertarian paternalism.

A. Political and Philosophical Background

The political origins of the term paternalism stem from the thought that the structure of the state ought to reflect that of the family. As such, the king or ruler governs his

subjects just as a father rules over his family. Hence, the underlying assumption is that the state would act to promote the greatest advantage of its citizens as a father would do to stimulate the best interests of his household. Paternalistic acts are thus achieved regardless of the consent of the citizens or the family given that the state or father is endowed with greater wisdom than the subjects (New World Encyclopedia, 2015).

Philosophers have molded and developed the notion of paternalism over time preserving some of its characteristics and amending others. Paternalism dates back to Classical Greece where Plato (428/427 BC-348/347 BC) in "The Republic" (380 BC) endorses the notion of paternalism in his understanding of the state. He depicts a philosopher king who has outright authority and wisdom as an expert in philosophy to govern his flock. Moreover, the king described by Plato ought to be a benevolent dictator concerned with the good of his subjects. In addition, Plato believed that individuals must be shielded from each other as well as from themselves physically, psychologically, and morally because immoral conduct, regardless of its effects on others, disorganizes one's soul, thus triggering detrimental effects to society. Therefore, the state according to Plato has the responsibility of producing righteous citizens just like a father has the duty of molding his children (New World Encyclopedia, 2015). Therefore, Plato's interpretation of paternalism is consistent with its political roots.

The notion of paternalism was further developed by Aristotle (384 BC-322 BC) who was a student of Plato. Despite Aristotle's doubt of the absolute power granted to Plato's philosopher king, he concurred that the government has the duty of safeguarding its citizens against physical and moral harm and promoting virtuosity since it is

fundamental for happiness. However, Aristotle calls for a paternal society grounded in the belief that a natural hierarchy subsists. As such, Aristotle believes that individuals should be subject to a government just as plants are subordinate to nature, animals to humans, women to men, slaves to citizens, kids to adults, and the body to the mind (New World Encyclopedia, 2015). Therefore, Aristotle's view of paternalism diverges from that of Plato in that it serves to promote inferiority and inequality between the binaries in each set mentioned above.

The post Platonic-Socratic era was characterized by a widespread acceptance and endorsement of the idea of benevolent and paternal rule among Europe's monarchies. These monarchs took the idea of paternalism a step further and highlighted their wisdom and right to govern by claiming that they were chosen by God (New World Encyclopedia, 2015). As a result, western political philosophical thought was shaped on the basis of this paternal Christian rule where the ruler is depicting God.

Around 1500 years later, Aristotle's ideas on paternalism were still popular and influential among thinkers. For example, Saint Thomas Aquinas (1225-1274) advanced Aristotle's perspectives on paternalism namely that the state is endowed with the privilege and the obligation to treat its subjects paternalistically. Just as Aristotle purported that the state should advance virtuosity as a means to achieve happiness, Aquinas added that the state should mold virtuous citizens in order to serve God and thus prompt happiness (New World Encyclopedia, 2015). Therefore, Aquinas was influenced by Aristotle's thoughts.

Half a century later, philosophers including Thomas Hobbes (1588-1679), John Locke (1632-1704), and Jean Jacques Rousseau (1712-1778) established the notion of paternalism as a social contract whereby individuals engage in a trade-off between giving up some of their rights to the state in return for social order and protection. However, this social contract is legitimate only with the assent of citizens (New World Encyclopedia, 2015). As such, social contract theorists were greatly affected by Aristotle's views in the sense that the ruler should advance the greatest advantage of his subjects. However, they introduced the concept of consent whereby the subjects are apt to revolt if the ruler violates their approval, just as a slave or a child were likely to flee if their master or father abused them.

In summary, despite the rich and diverse political and philosophical history of paternalism, no unanimous and clear-cut definition has been advanced in order to explain the term and its applications. However, the concept of paternalism has embarked on a long journey starting from Classical Greece where Plato and Aristotle deemed paternalism as a crucial component of the state, continuing to Europe's monarchies where paternalism was defended on the grounds that rulers were chosen by God and were endowed with the right to act paternalistically, reaching its understanding as a social contract by social contract theorists. Nonetheless, the development of the notion of paternalism has been stable in that thinkers agree on the responsibility of the state as the legitimate power to protect its citizens.

B. Paternalism in the Modern State

Different times have highlighted different aspects of paternalism. In modern times, philosophers, legal scholars, and economists have defined paternalism in terms of freedom of choice, autonomy, and consent.

Consistent with the political and philosophical background of paternalism, the philosopher Peter Suber explains that the term paternalism originates from the Latin pater that means "to act like a father or to treat another person as a child" (Suber, 1999). However, Suber clarifies that in modern philosophy and jurisprudence, paternalism is "to act for the good of another person without that person's consent, as parents do for children" (Suber, 1999). According to Suber (1999), paternalists ground their beliefs in the assumption that they are able to make better decisions than those they aim to help either because they are wiser or because the others are foolish.

In a similar vein, the philosopher Gerard Dworkin's definition of paternalism as "the interference of a state or an individual with another person, against their will, and defended or motivated by a claim that the person interfered with will be better off or protected from harm" emphasizes two dominant features of paternalism namely its means and its end (Dworkin, 2014). Therefore, according to Dworkin, paternalism resorts to interfering with people's actions and choices in order to benefit the people interfered with.

Behavioral economist Richard Thaler and legal scholar Cass Sunstein summed up the previous views on paternalism and inferred that a policy is paternalistic if it "attempts to influence the choices of affected parties in a way that will make choices better off"

(Thaler & Sunstein, 2003, p.1162). Moreover, Sunstein (2013) admits that despite the various forms that paternalism can take, paternalistic approaches are similar in that the government considers that people's choices are not welfare promoting and thus acts to influence people's choices in order to advance their welfare.

C. Libertarian Paternalism

The notion of libertarian paternalism was coined by behavioral economist Richard Thaler and legal scholar Cass Sunstein in 2003 in an article titled "Libertarian Paternalism". They later developed this conception further in another article titled "Libertarian Paternalism is not an Oxymoron". Their work was popularized in their book "Nudge: Improving Decisions about Health, Wealth, and Happiness" published in 2008. Arguably, the authors' notion of paternalism marks the middle ground on a continuum with paternalism occupying one extreme and libertarianism inhabiting the other and with libertarianism being defined as a "political philosophy that affirms the rights of individuals to liberty, to acquire, keep, and exchange their holdings, and considers the protection of individual rights the primary role for the state" (Standard Encyclopedia of Philosophy, 2002).

Even though the two concepts of libertarianism and paternalism seem to be at odds with the former purporting freedom of choice and the latter denying it, Thaler and Sunstein reconcile the rival ideas through introducing a kind of paternalism characterized by a libertarian nature that is likely to be endorsed by protagonists of freedom of choice on the basis of either autonomy or welfare (Thaler & Sunstein,

2008). The authors further explain that the libertarian facet of libertarian paternalism is guaranteed by the explicit insistence that people enjoy the right to choose to opt out of any arrangement and thus they do not endorse policies that hinder individual choices. The paternal trait of their approach is preserved through the power granted to public and private institutions to steer people's decisions in welfare-promoting ways instead of tracking people's anticipated choices. As such, libertarian paternalism qualifies as a weak and non-intrusive form of paternalism given that choices are not eliminated (Thaler & Sunstein, 2008). Therefore, they allege that the kind of paternalism they promote supports freedom of choice.

Thaler and Sunstein explain and popularize two means that libertarian paternalism resorts to in order to affect choices namely nudge and choice architecture. They define a nudge as "any aspect of the choice architecture that alters people's behavior in a predictable way without forbidding any options or significantly changing their economic incentives" (Thaler & Sunstein, 2008, p. 6). Moreover, an intervention is classified as a nudge if it meets two conditions namely if it is easy to be evaded and costless or nearly costless to be dodged (Thaler & Sunstein, 2008). The low costs associated with nudges render their effects harmless or nearly harmless if they fail to meet their purpose (Sunstein, 2013). Applied in the most thoughtful way, libertarian paternalism imposes insignificant material or psychological costs on those who wish to diverge from the planner's proposed choice (Thaler & Sunstein, 2003). Therefore, libertarian paternalists claim that their interventions qualify as nudges.

In order to illustrate choice architecture, Thaler and Sunstein (2008) introduce an imaginary director of food services who works for a large city school system. She has decided to conduct experiments in her cafeterias in order to investigate if there is a relationship between the display and arrangement of food and kids' choices while holding the menu constant. Through a simple rearrangement of the cafeteria, the director was able to tamper with the consumption of food items. Endowed with the power to influence kids' choices, she now has to decide how to display the items offered. According to Thaler and Sunstein, the director faces five options namely:

- 1- Arrange the food to make the students best off, all things considered.
- 2- Choose the food order at random.
- 3- Try to arrange the food to get the kids to pick the same foods they would choose on their own.
- 4- Maximize the sales of the items from the suppliers that are willing to offer the largest bribes.
- 5- Maximize profits.

The director of the cafeteria embodies what Thaler and Sunstein refer to as a choice architect. A choice architect is delegated with the responsibility of organizing the environment in which people make decisions given that small and insignificant details have the potential of influencing choices. Sunstein claims that "choice architecture is always inevitably all around us and influencing our behavior in countless ways of which we're unaware" (As cited in Burkeman, 2015). As such, choice architecture has become a factor embedded in everyday life.

The authors then investigate the implications of the director's choices in order to show that the libertarian paternalistic choice embodied in the first option is the best selection. They classify the first option as paternalistic yet attractive because the alternatives provided are all inferior. Option 2 will create nutritional discrepancies between schools and therefore is dropped. Option 3 attempts to mimic the market as a way to avoid interference in kids' choices. However, the true preferences of the kids are not explicit but are a function of the way the food is arranged, rendering option 3 problematic to apply. Option 4 is dismissed because the director is honest and honorable. Option 5 is realized by encouraging the consumption of foods with the highest profit margin and as such encompasses the possibility that the profits earned might be at the expense of inferior nutritional choices. Therefore, by selecting the first option, the director is acting in a libertarian paternalistic manner as she attempts to nudge kids towards the welfare-promoting diet choice (Thaler & Sunstein, 2008).

The authors base their views on findings of new behavioral economics and cognitive psychology. They explain that since people do not exhibit clear, stable, or well-ordered preferences, their choices are susceptible to default rules, framing effects, and starting point effects. As such, the decisions people make are highly influenced by the design features of legal and organizational rules. In summary, Thaler and Sunstein (2003) claim that the findings of new behavioral economics and cognitive psychology prove that people sometimes make inferior decisions. In other words, had they been endowed with complete information, unlimited cognitive abilities, and complete control over will power, they would have made different decisions. Therefore, they argue that a form of

paternalism is inevitable given people's vulnerability to default rules, framing effects, and starting points.

To sum up, Thaler and Sunstein have promoted the latest manifestation of paternalism namely libertarian paternalism which they claim is distinguished from other forms of paternalism by its libertarian nature. The authors refer to the findings of new behavioral economics and cognitive psychology to show that people sometimes make inferior decisions because they are susceptible to default rules, framing effects, and starting point effects. Thus, Thaler and Sunstein resort to the concepts of choice architecture and nudge in order to steer people towards the welfare-promoting choices.

In conclusion, this chapter has followed the history of the political and philosophical development of paternalism and its various interpretations by different thinkers reaching its most recent manifestation as libertarian paternalism. Despite the significant support attributed to paternalism in its several forms, from the time it originated until now, it has been an issue of great concern for those who endorse autonomy and freedom of choice.

CHAPTER IV

A POSITIVE CRITIQUE

Thaler and Sunstein have relied on only one form of behavioral economics, namely new behavioral economics, in developing libertarian paternalism. An inherent weakness in their work is that they have not justified the reason they use new behavioral economics instead of old behavioral economics to be the positive foundation of their analysis. This chapter will investigate the different approaches followed by old and new behavioral economics and the subsequent distinct policy implications they generate. For the purpose of this section, we will rely on the work of evolutionary psychologists in particular Gerd Gigerenzer and the ABC research group even though old behavioral economics was shaped by the efforts of four different groups of researchers. This section's focus on Gigerenzer and the ABC research group is due to the fact that they are not just critical of Kahneman and Tversky but also provide an alternative theory.

A. The Evolutionary Psychology Approach to Decision Making

Even though the interdisciplinary field of evolutionary psychology has not yet reached a consensus regarding its underlying principles, Samuels, Stich, and Bishop (2002) emphasize three core foundations that characterize evolutionary psychology. The first tenet establishes that the mind is composed of many purpose systems referred to as modules or mental organs. These modules are consistently considered to be

computational devices that are domain specific. The second precept maintains that the structure of the mind defined by modules is not limited to input systems that are concerned with perception and language processing and output systems which are responsible for producing actions. However, the structure of the mind also encompasses central capacities including reasoning and belief fixation. It is noteworthy to mention that these two propositions combined yield the Massive Modularity Hypothesis. The third and final thesis of evolutionary psychology is that mental modules are adaptations "invented by natural selection during the species' evolutionary history to produce adaptive ends in the species' natural environment" (Tooby & Cosmides 1995, xiii). As such, evolutionary psychology is defined on the basis of these three propositions.

Given the above three central principles, evolutionary psychologists claim that the modules in charge of reasoning should be expected to perform well when the information provided is presented in a format analogous to that previously offered in the ancestral milieu (Samuels, Stich, & Bishop, 2002). Gigerenzer (1994) and Cosmides and Tooby (1996) claim that our ancestors were subject to probabilistic information in the form of frequencies. Therefore, humans' developed adaptations for reasoning use frequency information as input. Grounded in evolutionary theory, Gigerenzer, Cosmides, and Tooby advocated the Frequentist Hypothesis whereby they proposed that "Some of our inductive reasoning mechanisms do embody aspects of a calculus of probability, but they are designed to take frequency information as input and produce frequencies as output" (Cosmides and Tooby 1996, p.3).

For evolutionary psychologists, framing the Kahneman and Tversky experimental problems in terms of frequencies reveals that humans tend to behave correctly. Two claims characterize their understanding of human rationality. First, evolutionary psychologists contend that in many cognitive problems that involve probability or uncertainty, intuitive decisions tend to lead to correct outcomes. This is particularly evident in decisions problems represented in terms of frequencies. Second, circumstances where intuitive judgments coincide with the correct norms of decision making are explained by the dependence on mental modules which were intended by natural selection to function well given a nature of input that resembles that present in the environment of evolutionary adaptation. Hence, these two thoughts are regarded as the central claims of the evolutionary psychological research on probabilistic reasoning (Samuels, Stich, & Bishop, 2002). The next sub section presents how evolutionary psychology challenges the biases and heuristics tradition advocated by Kahneman and Tversky.

B. Differences between Evolutionary Psychology and the Biases and Heuristics Tradition

Samuels, Stich, and Bishop (2002) specify three issues over which evolutionary psychologists and proponents of biases and heuristics disagree. The first issue of debate is concerned with the way probability theory should be applied to particular decision problems involving biases and heuristics and with whether or not probability theory offers an exclusive and specific solution to such problems. On the one hand, Gigerenzer

contends that various equally reasonable methods through which probability theory can be applied to decision problems exist and that each method yields a unique yet equally accurate answer. On the other hand, the advocates of the heuristics and biases approach argue that such problems are characterized by one normatively precise answer. Therefore, evolutionary psychology and the heuristics and biases approach diverge in the applications of probability theory.

The second problematic matter deals with whether or not the explanations advocated by the proponents of the heuristics and biases tradition are sufficient to describe cognitive phenomena. Gigerenzer (1996) asserts that the vague nature of heuristics prevents them from qualifying as valid explanations. He believes that the researchers promoting the heuristics and biases tradition have not been successful in identifying accurate and faulty models in explaining the underlying conditions that generate heuristics and in defining the relationship between heuristics. Nevertheless, Kahneman and Tversky (1996) defend their views by insisting that heuristics can be experimentally evaluated and that a theoretical model is not necessary to establish the validity of the prediction that heuristics bias probability judgments (Samuels, Stich, & Bishop, 2002). Hence, the two views disagree as to whether heuristics and biases are adequate to clarify cognitive processes.

The third and final disagreement, according to Samuels, Stich, and Bishop (2002), deals with identifying the correct interpretation of probability theory. Gigerenzer (1993) insists on a frequentist interpretation of probability theory whereby probabilities are presented in terms of relative frequencies of events in one category to events in another.

As such, his interpretation implies that it is futile to allocate probabilities to single events. In contrast with Gigerenzer's understanding of probability theory, Kahneman and Tversky (1996) recommend a subjectivist or Bayesian version of probability theory. Their account of probability thus allows the allocation of probabilities to single events. Therefore, the two approaches disagree as to what constitutes a correct interpretation of probability theory.

In summary, the underlying principles of old behavioral economics differ from those of new behavioral economics. Issues regarding the application and interpretation of probability theory as well as the adequacy of heuristics and biases to explain cognitive phenomena outline the sharp differences between the two behavioral approaches.

C. Gigerenzer's Adaptive Toolbox

Gigerenzer (1999) draws on Simon's ideas on bounded rationality in order to advocate an adaptive toolbox founded on three basic principles. The first premise of Gigerenzer's adaptive toolbox is psychological plausibility. This establishes the mechanics of Gigerenzer's model which is to understand how actual human beings make decisions in contrast to Homo Economicus who enjoys unrestricted time, knowledge, memory, among other resources. The second principle of Gigerenzer's adaptive toolbox is domain specificity. This is evident in the fact that the heuristics represented by the toolbox are domain specific. In addition, the heuristics are made up of cognitive and emotional building blocks that can be part of more than one heuristic and permit the creation of new heuristics. Moreover, these building blocks are

characterized by a more general nature than the heuristics themselves. The third and final tenet of Gigerenzer's adaptive toolbox is ecological rationality. The rationality of the domain specific heuristics does not stem from optimization, omniscience, or consistency. Rather, the success or failure of heuristics is dependent on the extent of their adaptation to the physical and social structure of the environment. Ecological rationality is thus the study of the convergence between heuristics and environmental structure (Gigerenzer & Selten, 2001).

Gigerenzer offers an alternative to the nudge theory of Thaler and Sunstein (which is constructed on the findings of new behavioral economics). Gigerenzer argues that spreading education on how to critically think about statistical probability will increase and enhance people's perception and understanding of risk (Adams, 2014). As such, instead of nudging people towards what policymakers think is best for them, Gigerenzer suggests that equipping people with the right heuristics will educate them on how to make better decisions.

The purpose of this section on the positive critique of libertarian paternalism is to demonstrate that a different view of behavioral economics generates a different set of policy recommendations. Section VI, which analyzes the third component of Neville Keynes' tripartite categorization of economics, namely the art of economics, will further assess the policy implications of libertarian paternalism.

In conclusion, this chapter has offered a positive critique of libertarian paternalism's choice of new rather than old behavioral economics. The chapter traces the underlying principles of evolutionary psychology focusing on Gigerenzer's work and outlines the

distinctions between evolutionary psychology and the heuristics and biases approach.

In the next section, the normative aspect of libertarian paternalism, namely paternalism, will be criticized based on welfare, freedom, and dignity of autonomous beings.

CHAPTER V

A NORMATIVE CRITIQUE

Paternalistic practices have recently become prevalent bringing to light the issue of their underlying ethics and morality. Paternalism encompasses a conflict among two values namely between freedom and wellbeing. In situations where people make a free decision to diverge from the choices that policy makers assume they should make, the issue of whether or not paternalistic interference is allowed emerges. Paternalism is admissible when the subjects of concern suffer from impaired freedom due to coercion, limited cognitive capacities, ignorance, drugs or illnesses such as Alzheimer's (Andre & Velasquez, 1991). Issues of value substitution, liberty, and autonomy associated with paternalism render it a topic of debate and criticism.

A. Paternalism, Welfare, and Value Substitution

Libertarian paternalism and nudges have been critiqued on the basis of welfare and value substitution by Mark White and Till Grune-Yanoff. On the one hand, White has dedicated a chapter of his 2013 book " The Manipulation of Choice: Ethics and Libertarian Paternalism" in order to assess the value substitution implied by libertarian paternalism. On the other hand, Grune-Yanoff has devoted a section of his 2012 article "Old wine in new casks: libertarian paternalism still violates liberal principles" in order

to explain how libertarian paternalism replaces people's interests by those of the policymakers.

White considers that behavioral economists are concerned about the myriad of decisions made by people every day because these choices tend to diverge from the simple interests that people are presumed to promote including health and wealth. In order to correct this deviation in interests, libertarian paternalists maintain that they nudge people into making the choices that people themselves would like to make (White, 2013). This claim is based on the assumption that people's interests are fully disclosed to the libertarian paternalist. In addition, to act in such a way assumes that libertarian paternalists are better judges of people's welfare than the people themselves. However, White believes that interests are internal and subjective and thus can only be revealed through choice or expression (White, 2013). Therefore, a major problem with libertarian paternalism and nudges, according to White, is that an outside observer can never know the real interests behind people's choices. A person's true interests can only be revealed through observing his choices in an environment free from manipulation and nudging.

In addition to the subjectivity of interests, White (2013) argues that libertarian paternalism generates value substitution. Since the only information available to libertarian paternalists regarding people's true interests, where interests are defined as the combination of things, people, and ideals that people care about, is people's actual choice, behavioral economists have to impose some interests in order to judge people's choices. As a result, policymakers overlook people's conception of welfare and replace

it by their own conception of what best promotes the people's welfare. Thus, welfare substitution is generated. As such, this value substitution refutes the libertarian paternalistic claim that people are being nudged in order to promote their own interests and proves that people are being nudged instead towards decisions that advocate the planners' desired choice. In addition, White believes that value substitution entails a "usurpation of judgment about the way individuals structure and run their lives" (p. 74). This is so because when a policymaker substitutes people's true values and interests, he is substituting them not for some neutral values and interests but with his own. Therefore, libertarian paternalism involves replacing people's true interests with those of the policymakers'.

In summary, White (2013) argues that libertarian paternalism yields value substitution. This is because it involves replacing the people's ends with those of the policymakers'. Thus it is ethically problematic.

Grüne-Yanoff (2012) also criticizes paternalism on the basis of value substitution and welfare. He explains that two liberal stances on value exist namely the subjectivist account and the pluralist account. On the one hand, the subjectivist explanation of value posits that a person's values stem from individual experiences. Moreover, an individual's welfare is promoted upon the satisfaction of preferences which are unique to each person. Therefore, a liberal policymaker according to Grüne-Yanoff is one who respects the subjectivity attributed to people's values. On the other hand, the pluralist interpretation offers an objective account of value. It implies that a plurality exists and thus values are sometimes incomparable and at other times incompatible. The

incomparability of values deems the trade-off between them impossible. In addition, the incompatibility of values renders their achievement simultaneously impossible.

Therefore, Grüne-Yanoff believes that the values chosen by an individual depend on personal preference. A liberal policy maker thus can't promote the welfare of a population by adopting a group of uniform and objective values but should rather work to advance the values that are specific to each individual.

Hence, Grune-Yanoff recommends that libertarian paternalists demonstrate that their notion of welfare adheres to one of the above justifications in order to refute the claim of continuity between libertarian paternalism and other forms of paternalism. However, he contends that libertarian paternalism respects neither the subjectivity nor the plurality of people's values. Rather than attempting to determine people's true preferences, libertarian paternalists resort to reconstructing preferences in a perfect and objective environment through counterfactually reconstructing preferences. Consequently, he concludes that the idea of welfare advanced by libertarian paternalists violates both the subjectivity and the plurality of values.

To sum up, Grune-Yanoff argues that libertarian paternalism has failed to abide by either liberal position on value. He contends that the proponents of libertarian paternalism incorrectly assume people's preferences. As such, libertarian paternalism is in essence similar to other forms of paternalism.

In light of this critique, can libertarian paternalists defend their stance? Thaler and Sunstein (2003) claim that those who object to paternalism base their argument on a false assumption namely that "all people, almost all of the time, make choices that are in

their best interest or at the very least are better, by their own lights, than the choices that would be made by third parties" (p. 1163). They contend that testing this argument proves that it is false. For example, obesity rates in America indicate that 20% of the Americans are obese and that 60% are either obese or overweight (Thaler & Sunstein, 2003). However, information about the detrimental health consequences of obesity is widespread and available to the population. Therefore, they reason that the claim that Americans are making optimal diet options is difficult to corroborate. In addition, they consider that people make better choices in domains in which they have experience and access to information (than in domains in which they lack experience and access to information). For instance, an individual will make a wise decision when choosing an ice cream flavor and a poor decision when choosing between investment options (Thaler & Sunstein, 2003). As such, they advocate libertarian paternalistic interventions that aim to promote individual's welfare whenever their choices diverge from the optimal.

Thaler and Sunstein's response to the first critique is plausible provided that libertarian paternalistic interventions are limited to domains in which people are inexperienced and uninformed. However, even under this condition, libertarian paternalists must make sure that policy makers do not exploit their authority to promote their own welfare through value substitution. As such, libertarian paternalism is able to reply to the welfare critique advanced by White. Nevertheless, libertarian paternalists do not account for the subjectivity or the plurality of values. Even if they restrict interventions to areas where people lack experience and information, their policies will

still assume that people share the same interests. As such, so long as their policies are uniform among people, they cannot reply to Grüne-Yanoff's critique.

B. Paternalism and Liberty/Freedom

A second problem with libertarian paternalism and nudges is that they inhibit freedom. In the eighteenth century, the philosopher Immanuel Kant was the first to provide arguments against paternalism based on liberty. Kant believed that treating people like minors who lack the ability to choose what promotes their interests represents a violation of the concept of liberty. In addition, Kant believed that the duty of the government is confined to protecting freedom and property rights and advocated people's right to seek their own interests provided that they do not impair or intervene with the freedom of others (New World Encyclopedia, 2015). Therefore, Kant deemed freedom to be superior to any form of paternalistic intervention.

Despite the fact that Kant was the first to openly criticize paternalism, it was John Stuart Mill's 1859 "On Liberty" which exerted much influence on the development of the liberal political theory. Mill argues that freedom is superior to protecting people from themselves, is associated with a high cost, is too great a trade-off for welfare and that in the long-run, respecting liberty will generate the highest utility (New World Encyclopedia, 2015). In addition, Mill deemed freedom to be a vital social value. As such, he believed that freedom is central for the development of each person's individuality, attainment of truth, and the advancement of novel and enriching modes of life (Andre & Velasquez, 1991)

In addition, Grune-Yanoff (2012) resorts to freedom to argue that in essence, libertarian paternalism is indistinguishable from other forms of paternalism. He explains that the restriction of freedom imposed by libertarian paternalism is in line with liberalism if it is properly justified through the Fundamental Liberal Principle promoted by Gaus in 1996 which states that: "freedom is normatively basic, and so the onus of justification is on those who would limit freedom, especially through coercive means" (As cited in Grune-Yanoff, 2012, p. 640). This justification is based on Rawls' 1997 principle that "a basic liberty... can be limited only for the sake of liberty itself" (As cited in Grune-Yanoff, 2012, p. 640). Nevertheless, Grune-Yanoff claims that libertarian paternalism cannot adhere to such a justification because the restriction it enforces on liberty does not refer to liberty per se but rather to welfare. Thus he identifies a trade-off between the notion of liberty and that of welfare.

In order to defend libertarian paternalism against this critique, Thaler and Sunstein (2003) simply claim that their approach is liberty-preserving. They argue that freedom of choice is in essence a component of welfare. As such, they believe that freedom of choice is promoted whenever welfare is promoted. However, libertarian paternalists mistake the notion of freedom of choice for availability of options. They believe that providing various options for people to choose among will preserve and promote their freedom of choice. Nevertheless, they do not account that people might choose an option that their policies do not offer. Therefore, the libertarian paternalistic response is very limited in that it fails to explain how libertarian paternalism is consistent with freedom of choice.

In conclusion, libertarian paternalism is advocated by its proponents to be a novel form of paternalism due to its libertarian nature. However, opponents of libertarian paternalism concur that libertarian paternalism is a threat to liberty.

C. Paternalism and the Dignity of Autonomous Beings

A third problem with libertarian paternalism and nudges is their violation of the dignity of autonomous beings. White (2013) defines autonomy as "the right of individuals to govern their own lives, setting their own agendas, goals, and interests, and being free to make choices as they choose (provided those choices don't interfere with anyone else doing the same)" (p. 128) As such, the concept of autonomy revolves around the notion of self-governance.

The philosopher Immanuel Kant calls for respecting the equal "dignity" of all human beings. This regard for human dignity is achieved through respecting people's abilities to think and make their own decisions (Andre & Velasquez, 1991). In other words, respecting people's dignity implies respecting their autonomy. The Kantian perspective holds that autonomous agents are capable of determining their interests and ends in a manner that is unbiased to inclinations, preferences or well-being based on a moral law that every person legislates for himself according to individual judgment (White, 2011). In addition, Kant distinguishes between two forms of autonomy namely outer freedom and inner freedom (White, 2013). On the one hand, outer freedom encompasses expressions of autonomy with regard to external influence and authority such as standing up to your boss. On the other hand, inner freedom includes expressions of

autonomy with respect to one's own desires such as resisting to eat dessert when on a diet. Therefore, a choice is categorized as libertarian if it respects the dignity of autonomous persons.

However, Kant believes that paternalism violates the dignity of autonomous beings. Paternalism in general operates through value substitution. As such, policymakers do not treat individuals as equals who have the ability to control their own decisions. Instead, Kant explains that people are looked upon as merely means to the paternalists' ends and are thus regarded as "immature children unable to distinguish between what is truly useful or harmful to them" (As cited in Andre & Velasquez, 1991). Therefore, paternalism is not in line with the Kantian principle of autonomy.

Furthermore, Kant argues that a person's autonomy can be violated via two means namely coercion and deception which use people as a means to achieve the ends of others. To act in such a way excludes people from the decision-making process and rids them of their right to consent to it (White, 2011).

White (2011) clarifies how coercion and deception fail to respect a person's dignity and autonomy. He explains that an individual subject to deceit or coercion cannot rationally consent to the ends of the paternalist because in the former case he is oblivious of the paternalist's ends and in the latter case he is not given the chance to assent to them. In addition, White (2013) argues that for consent to be desired, it must be actual and not hypothetical. Furthermore, he argues that nudges are coercive in that they operate through the same cognitive biases and heuristics that they use to justify their intervention. Thus, White concludes that choice architecture violates the dignity of

autonomous beings since it fails to give them the chance to express their consent to or dissent from the proposed policies.

Moreover, John Stuart Mill addresses the issue of coercion through his classical argument against paternalism in his 1859 book "On Liberty". In his book, he lays the foundation of the "harm principle" that justifies government coercion only to protect others from harm. Mill argues that ". . . the only purpose for which power can be rightfully exercised over any member of a civilized community, against his will, is to prevent harm to others (Mill, 1859, p.14-15). As such, Mill grounds his argument in the concept of autonomy and advocates the right of individuals to pursue their own ends provided that they don't interfere with others or harm others who are attempting to do the same.

Furthermore, Grune-Yanoff (2012) argues that libertarian paternalistic policies represent an increase in the frequency of actual interference in people's decision making process and therefore create a kind of coercion. He explains that while Thaler and Sunstein (2008) offer a narrow definition of the notion of coercion that encompasses conditional threats or direct force, liberal theorists favor a broader definition such as Berlin (1969) who states that coercion "implies the deliberate interference of other human beings within the area in which I could otherwise act" (As cited in Grune-Yanoff, 2012, p.638). He also contends that many libertarian paternalistic policies are compatible with Berlin's definition; "Save More Tomorrow" nudges people into increasing their savings through reducing their individual valuation of the amount proposed to be saved, requiring that fuel-economy stickers be present on the rear of cars

influences people's assessment of these cars and the like. As such, Grune-Yanoff highlights a wider definition of coercion and shows how it can be applied to libertarian paternalistic policies.

In response to this critique, libertarian paternalists argue that their approach is not coercive in the sense that choices are not "blocked or fenced off" (Thaler & Sunstein, 2003, p.1162). However, libertarian paternalistic policies are not disclosed to people in the sense that people are unaware that they are under the influence of such policies and that their psychological and cognitive weaknesses are being used to allegedly promote their own interests. Therefore, libertarian paternalists cannot address this critique.

In summary, opponents of libertarian paternalism contend that it violates the dignity of autonomous beings. This disrespect of dignity is accomplished via two routes namely coercion and deceit. As such, libertarian paternalism treats people as means to the planners' ends.

As Henry David Thoreau (1854) suggests, if "a man was coming to my house with the conscious design of doing me good, I should run for my life" (As cited in Andre & Velasquez, 1991). Issues of value substitution, freedom, dignity and autonomy emphasized by paternalism carry repercussions for policies in both the private and the public domain. As such, policymakers must realize that a fine line exists between promoting the welfare of others and respecting their freedom and dignity as autonomous beings.

CHAPTER VI

LIBERTARIAN PATERNALISM AND POLICY MAKING

The application of libertarian paternalism to public policy constitutes the art of economics, the third pillar of economics according to Neville Keynes. The form of paternalism promoted by Thaler and Sunstein has been very influential among public officials to the extent that several governments have endorsed and incorporated the concepts of libertarian paternalism and nudge in their policy making procedures. For example, behavioral findings were central to the development of the tax cuts in the 2009 stimulus package, retirement savings policy, the individual mandate in health care reforms and aspects of the Dodd-Frank financial reform bill in the United States (McMahon, 2015). In addition, numerous governments have created and launched behavioral teams with the responsibility of supervising the implementation of behavioral findings in public policy. For instance, Thaler was a consultant on the United Kingdom's Behavioral Insights Team. Moreover, the United States set up a working group in 2013 grounded in the UK model. In addition, countries including Brazil, France, Australia and New Zealand have recognized and integrated behavioral findings in their policy making (McMahon, 2015). Libertarian paternalism therefore, has become a crucial component of public policy in several nations. This chapter will explore three major critiques that address the issue of integrating libertarian paternalism in public

policy and whether the proponents of libertarian paternalism are able to respond to such criticisms.

A. First Critique: Misusing Nudges for Profit

Legally, phishing is categorized as a cyber-crime whereby "a targeted individual is contacted by email or telephone by someone posing as a legitimate institution to lure the individual into providing sensitive information such as banking information, credit card details, and passwords." The alleged qualified institution then gains access to the individual's account and subjects the victim to the potential dangers of identity theft and financial loss ("What is Phishing?", n.d.). As such, phishers exploit the gullibility of individuals in order to attain monetary returns.

However, the notion of phishing has acquired a new dimension through the work of Nobel laureates in economics Robert Shiller and George Akerlof. Their most recent book "Phishing for Phools" widens the scope of phishing to include any kind of deception and manipulation that happens in the marketplace. Moreover, a phool is defined as a person who is unaware that he or she is being phished. As such, Shiller and Akerlof classify any activity, action, or policy that instigates individuals to behave in ways that promote the interests of the phishermen but not those of the target as phishing (Shiller and Akerlof, 2015).

The broadened definition of phishing advocated by Shiller and Akerlof is in line with Adam Smith's teachings. Smith sets the major economic principle that markets work as if through an invisible hand to bring about material welfare. Rather than always acting

in the best interests of their players, markets also have the potentiality of harming their actors. This is evident when Smith writes in *The Wealth of Nations* that “people of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public or in some contrivance to raise prices” (Smith, 1776, p.152) thus indirectly referring to the potential practice of phishing. Akerlof and Shiller (2015) further concur that provided that there exists an opportunity for profit, sellers will take advantage of widespread psychological weaknesses and ignorance through manipulation and deception. Thus, the practice of phishing enjoys an extensive range of applicability in both the private and the public sector such as in the field of advertising and marketing, real estate, car sales, credit cards, financial markets and medicine to name a few. As a result, markets are intrinsically abounding in tricks and ruses and can phish us for phools.

The practice of phishing as presented by Akerlof and Shiller subjects Thaler and Sunstein's nudging to a menacing critique. Superimposing the definitions of phishing and nudging reveals the relationship between them. Both are small and simple design changes that rely on psychological findings and cognitive weaknesses in order to alter behavior. However, the concepts diverge in their means and their ends. While nudging uses ethical means in order to encourage welfare-promoting behavior, phishing resorts to deception and manipulation as a means to alter behavior in order to attain a profit. Nudges therefore require the promotion of welfare whereas phishing practices overlook welfare and focus on profit realization.

An issue of concern thus arises given that both nudging and phishing are tools of choice architecture. Thaler (2015) addresses this matter in his article "The Power of Nudges, for Good and Bad". He defines phishing as evil nudging and admits that it is not unusual for companies and governments to resort to bad nudging in order to achieve profit at the expense of customers and citizens' best interests. Therefore, phishing is problematic to libertarian paternalism since it represents an abuse of nudging which leads to the distortion of its purpose.

Thaler (2015) defends libertarian paternalism against this critique and prevents the possible exploitation of nudges. He clearly states three principles that should govern the practice of nudging, namely, that 1) nudges should be transparent and under no circumstances deceptive, 2) nudges should be easy and costless to opt out of, and 3) nudges should be based on strong evidence that the behavior being endorsed will shift those being nudged in welfare-promoting directions. Therefore, these three conditions are necessary to qualify any tool of choice architecture as a good nudge.

In addition, Thaler admits that abusing nudges is a phenomenon that is prevalent in both the private sector and the public sector. He explains that some believe that the menace of phishing is more pronounced in government than in the private sector. The rationale is that the government is a monopoly that enjoys coercive power whereas the private sector allows for a wide range of choices. Nonetheless, Thaler refutes this argument and considers the division between the private sector and the government to be exaggerated. He reasons that on the one hand, when a government uses bad policies, people can vote it out of office in a democracy. On the other hand however, the private

sector embraces competition which acts to promote rather than repress phishing. As such, even though libertarian paternalists are troubled about misusing nudges in the private and the public sector, their concern is more stressed when it comes to the private sphere.

In summary, Akerlof and Shiller's discussion of phishing emphasizes that choice architecture operates through various tools. Their interpretation of the notion of phishing (2015) draws attention to the possibility of abusing nudges through deception and manipulation in order to attain a profit. However, libertarian paternalists can easily respond to Akerlof and Shiller's analysis. They are strongly against bad nudging and are constantly seeking to spread awareness regarding its hazards. Therefore, despite the impending consequences that phishing practices are likely to generate, libertarian paternalists have displayed their willingness and efforts to suppress the application of faulty versions of nudging.

B. Second Critique: A Libertarian Perspective

In his article "Obama's Behavioral Data Order has Sinister Implications", Logan Albright (2015) explicitly proclaims his libertarian views and expresses his concerns regarding the distressing consequences of libertarian paternalism and nudges in the public sector. His libertarian thoughts are evident through his strong belief that individuals are entitled to freedom of choice and sovereignty to control their lives as they see appropriate without government intervention: "It's not government's place to tell us that we are living our lives wrongly, that we eat too much, that we exercise too

little, or that products we like and want to buy just aren't good enough" (Albright, 2015). His opposition to any form of government intervention is a further assurance of his disapproval of libertarian paternalism and nudges. Therefore, Albright critiques libertarian paternalism from a libertarian point of view.

Albright bases his critique on two major issues. The first premise of his critique relates to the means through which libertarian paternalism operates. Albright believes that resorting to data and psychology in order to impact behavior is a "sinister twist on marketing, with the idea basically being that people must be tricked into making the right decision" (Albright, 2015). The second principle of his critique is concerned with the consequences that he believes libertarian paternalism will generate. Albright postulates that libertarian paternalism will bring about arrogant leaders who expect their public to be "little more than sheep, to be herded" in any direction that those in power consider fit (Albright, 2015). In addition, he claims that libertarian paternalism instigates those in power to central plan the lives of their citizens and thus rid them of their right to freedom of choice and decision making. Furthermore, he deems libertarian paternalism to be an advanced form of an Orwellian state and warns of its impending dangers on the welfare of society. He asserts that the "collection and utilization of behavioral data *en masse* to manipulate the citizenry is one of the most frightening developments of an increasingly Orwellian state" (Albright, 2015). Therefore, Albright's critique reveals two considerations regarding the application of libertarian paternalism in the public sector.

In light of this critique, how would a libertarian paternalist respond? On the one hand, the examination of the first foundation of Albright's critique allows a libertarian paternalist to infer that Albright does not distinguish between the tools of choice architecture namely between nudging and phishing. Albright's analysis assumes that the public must be tricked by policymakers in order to make the right decision. However, trickery through the means of deception and manipulation is characteristic of phishing and not nudging. Libertarian paternalists focus on good nudging rather than bad nudging and spread awareness of the possibility of misusing nudges for profit (Thaler, 2015). Therefore, Albright's concern that behavioral economics can be abused to manipulate people's choices is an apprehension he shares with proponents of libertarian paternalism. On the other hand, the scrutiny of the second foundation of Albright's critique reveals that it tackles the macro consequences of phishing. However, up to this point in time, the libertarian paternalistic analysis is still confined to the micro scope and lacks the wider macro implications. Therefore, libertarian paternalists are not capable to determine the damages that could result if nudging is abused and thus can't respond to the second part of Albright's critique. As a result, Albright's article conveys a shared worry with libertarian paternalists and an urge to extend their analysis to the macro sphere.

To sum up, Albright addresses the issue of libertarian paternalism from a libertarian view point. His critique reveals his concern about the abuse and the macro consequences of libertarian paternalism. However, analyzing his critique from a libertarian paternalistic perspective exposes two important findings. The first is his

misconception of nudging whereby he does not differentiate between nudging and phishing. The second is his highlighting the pressing need for libertarian paternalists to broaden their analysis to encompass the macro scale.

C. Third Critique: Value Systems and Incommensurability

In his article "Training for Neoliberalism", John McMahon (2015) focuses his critique on the foundations and implications of new behavioral economics. However, new behavioral economics is the cornerstone on which libertarian paternalism has been built. Therefore, McMahon's critique is pointed towards both new behavioral economics and libertarian paternalism.

McMahon (2015) addresses two significant issues of concern. Firstly, he argues that the new behavioral economics model does not allow economic agents "the possibility of feeling, thinking, acting, deciding, socializing, forming relationships, caring for the self and so on" outside the realm of economic reasoning. Put differently, new behavioral economics discounts various value systems that are important for economic analysis. Secondly, he explains that from the perspective of new behavioral economics, decision making is deemed to be commensurable and all choices are qualitatively similar. In other words, the decision making process operates in the same manner when it comes to both frequent and mundane purchases such as buying clothes and food and infrequent acquisitions for example buying a car, choosing a spouse and selecting an occupation. As such, McMahon's critique tackles the underlying foundations of libertarian paternalism.

In view of this criticism, how would a libertarian paternalist reply? The first problematic matter according to McMahon is that libertarian paternalism disregards primary economic value systems from their analysis. The interdependence between value systems in economic life is discussed by Irene Van Staveren in her 2001 book "The Values of Economics: An Aristotelian Perspective". Staveren (2001) identifies three values that are crucial to the functioning of an economy namely freedom, justice, and care. Freedom operates through exchange, prices, and competition. Justice works via redistribution, solidarity, and rules. Care functions by means of giving. Furthermore, she asserts the intricate liaisons between these values by denying the possibility of commensurability and exchange between them. However, the libertarian paternalistic argument focuses on one value domain namely freedom, while holding all other values constant. Proponents of libertarian paternalism do not utilize notions like care and justice in their work but rather concentrate on the importance of freedom to their analysis. As such, the libertarian paternalistic model captures only one value system while ignoring the need to add other values.

The second issue under consideration, namely commensurability of the decision making process, has been examined by Sunstein in his 1994 article "Incommensurability and Valuation in Law" almost a decade prior to the establishment of libertarian paternalism. Sunstein commits to exploring two claims namely that human values are plural and diverse and that human goods are incommensurable. His views regarding incommensurability are central to exploring the validity of McMahon's critique. Sunstein defines incommensurability as the situation in which "relevant goods

cannot be aligned along a single metric without doing violence to our considered judgments about how these goods are best characterized" (Sunstein, 1994, p.796). He identifies and explains four major components of his definition. First, he clarifies that "our considered judgments" refers to the thorough valuation of the manner by which relationships and events should be understood, evaluated and experienced. Second, a "single metric" denotes a standard of valuation that functions with specificity, rules out all qualitative discrepancies and permits the comparison of distinct goods via a common measurement. Third, "doing violence" shows that resorting to a single metric distorts how people experience or tend to experience goods. Finally, "doing violence to our considered judgments" indicates the disturbance of the reflective assessments regarding the way in which events and relationships should be understood, evaluated and experienced. In addition, Sunstein deems choices among commensurable goods to be investment decisions. Furthermore, he claims that reducing human decisions to investment decisions will lead to misleadingly describing experience. Therefore, Sunstein (1994) offers an exhaustive explanation of his understanding of incommensurability and asserts his conviction that human goods cannot be assessed along the same metric.

However, it is crucial to examine whether the ideas advocated by Sunstein in his 1994 article are consistent with those promoted through libertarian paternalism. Sunstein and Thaler's discussion of libertarian paternalism highlights a possible stark contradiction between Sunstein's previous work and his collaboration with Thaler. In their most recent analysis, the authors assume that decision makers embark upon the

same process when choosing what to eat in a cafeteria and whether to save for retirement (Thaler & Sunstein, 2003). Thus, they adopt a common metric unit upon various decisions. This tension can be solved if libertarian paternalistic analysis is limited to only one value system, namely freedom. In this case, there would exist no tension between Sunstein's thoughts on incommensurability and the libertarian paternalistic position.

In short, McMahon critiques libertarian paternalism in terms of value systems and incommensurability. His analysis is focused on the underlying foundation of libertarian paternalism. Libertarian paternalism focuses on one value system namely freedom while holding all other value systems constant. In addition, it highlights a possible contradiction between Sunstein's 1994 work and his 2003 collaboration with Thaler.

In conclusion, libertarian paternalism has successfully paved its path into public policy. However, the incorporation of libertarian paternalism into public policy has raised various questions and concerns. This chapter has underlined three major critiques that deal with this issue from various perspectives. The first critique was initiated by Shiller and Akerlof and focuses on phishing or misusing nudges. The libertarian paternalistic front was able to respond to this criticism by explaining that choice architecture operates through various tools and that they only endorse those that ethically promote welfare. The second critique was a libertarian critique introduced by Albright who deals with the abuse and macro consequences of nudges. Libertarian paternalists were able to answer the first part of the critique by explaining the difference between phishing and nudging. However, they were unable to address the second part of

the critique because their analysis is limited to the micro sphere. The final critique was instigated by McMahon who emphasizes the founding ideas of libertarian paternalism. Libertarian paternalists were incapable to respond to his critique given their recognition of only one value system while ignoring all others in addition to the tension between Sunstein's previous ideas on commensurability and libertarian paternalists' views on the matter.

CHAPTER VII

CONCLUSION

This thesis has adopted Neville Keynes' tripartite categorization of economics in order to assess libertarian paternalism. The first part, "Behavioral Economics: An Overview", has traced the historical development of behavioral economics reaching the establishment of new behavioral economics, the positive foundation of libertarian paternalism. The second part, "Paternalism and Libertarian Paternalism" has outlined the variations in the concept of paternalism, the normative aspect of libertarian paternalism, over time, until its most recent manifestation as libertarian paternalism. The third part "A Positive Critique" criticizes the libertarian paternalistic choice of new behavioral economics instead of old behavioral economics and highlights that old behavioral economics generates a set of different policy recommendations. The fourth part, "A Normative Critique" has presented three critiques to paternalism and libertarian paternalism based on welfare, freedom, and dignity of autonomous beings and has established that libertarian paternalism violates these three notions. The final part "Libertarian Paternalism and Policy Making" has placed libertarian paternalism in the field of public policy and examined whether or not libertarian paternalism can address three critiques relating to its policy implications.

The development of new behavioral economics has been crucial to the emergence of libertarian paternalism. However, libertarian paternalism is not yet a complete theory due to the following reasons. First, libertarian paternalism still suffers from issues of value substitution, freedom, and dignity of autonomous beings attributed to paternalism.

Second, libertarian paternalists have not yet justified their choice of new behavioral economics instead of old behavioral economics. Third, the designers of choice architecture and nudge are incapable of guaranteeing that their tools won't be abused in pursuit of profit. Fourth, the known implications of libertarian paternalism are still limited to the micro sphere because libertarian paternalistic analysis does not apply to the macro level yet. Fifth, a possible striking contradiction between Sunstein's previous views on incommensurability and the libertarian paternalistic views on commensurability is evident. Finally, libertarian paternalism accounts for only one value system namely freedom while holding other systems constant. As such, libertarian paternalism encompasses a range of loopholes that can be used against it. Therefore, until now, libertarian paternalism is a reinvention of paternalism.

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