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Libertarian Welfarism

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Abstract: *In a series of publications, Cass Sunstein & Richard Thaler, and Colin Camerer et al., have proposed an approach to legal policy that encourages individuals to pursue actions that will maximize their expected utility while not imposing on those individuals' decisional autonomy. I contend that this policy approach – which has been called "libertarian paternalism" – implies a complementary approach as well, which I call "libertarian welfarism." Libertarian welfarism relies on the same set of policy tools as does libertarian paternalism but with a different goal: to encourage individuals to act in a way that maximizes social welfare. I show that libertarian welfarism leads to different policy prescriptions than does libertarian paternalism, and I argue that the former approach rests on a stronger normative foundation and is less subject to problems of indeterminacy than the latter.*

Neoclassical law and economics analysis, which targets the normative goal of maximizing efficiency, assiduously avoids paternalism as a justification for regulatory policy. Built on the edifice of rational choice theory, law and economics scholars usually assume that most actors are able to maximize the satisfaction of their preferences given the constraints they face.[1]

Evidence gathered by psychologists and economists about human decision making over the last three decades has raised a serious challenge to the rational actor assumption of neoclassical economics. It

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[1] *See* Russell Korobkin & Thomas S. Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics*, 88 CAL. L. REV. 1051, 1060-66 (2000).

turns out that not only infants and the mentally incompetent fail to make optimal decisions. Most people have trouble making optimal decisions (understood as those that maximize the actor's subjective expected utility, or "SEU") in a variety of contexts. The world is too complex for our brains to maximize, so instead we rely on mental heuristics and habits, which allow us to function in the work-a-day world without being paralyzed by information overload. The result is that we stumble through life, remaining on our feet most of the time but often enjoying less utility than is theoretically possible. These findings, imported into normative legal theory as behavioral law and economics, expands the potential space for state intervention on grounds of paternalism.[2]

I say *potential* space because the case for paternalism is subject to two challenges. First, the state functionaries who would presumably intervene in private decision making – legislators, regulators, judges, administrators, at the like – are no less human than the potential subjects of regulation. If I can't figure out whether I would be better off with a car equipped with expensive airbags (which would carry a higher price tag) or a slightly more dangerous (and cheaper) automobile combined with some other goods and services, why should I be confident that a state functionary can do any better?[3]

Second, in nearly all cases of public policy significance, there will be heterogeneity of subjective preferences. Some people would maximize their SEU by purchasing the cheaper car without airbags and spending the money saved on a family vacation in Hawaii, while others with a greater taste for safety and a lesser yearning to travel would maximize their subjective expected utility by paying for the airbags and foregoing the trip. Assuming that it is impractical for even an omniscient government functionary to impose different rules for each individual – that is, a regulation requiring airbags must apply to all car sales or none –

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[2] Christine Jolls, Cass Sunstein, and Richard Thaler described this evidence as supporting "anti-antipateralism–a skepticism about antipaternalism, but not an affirmative defense of paternalism." Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1541 (1998).

[3] *Cf*. Jeffrey J. Rachlinski, *The Uncertain Psychological Case for Paternalism*, 97 NW. U. L. REV. 1165, 1168 (2003) ("The psychological case for paternalism…must rest on a relative assessment of the cognitive costs of improved decision against the costs of supplanting individual choice.").

attempts to operationalize paternalism are bound to harm many, even if they also benefit many.

In response to these objections to using traditional forms of coercive state fiat to address the considerable evidence that individuals are not relentless utility maximizers, a new paradigm of regulation has emerged that calls for the state to help individuals make decisions that the functionaries believe are most likely to make them better off but allow the individuals to decline the assistance if they choose to do so. Colin Camerer, Samuel Issacharoff, George Loewenstein, Ted O'Donoghue, and Matthew Rabin ("Camerer et al.) called this approach "asymmetric paternalism,"[4] in reference to its virtue of creating significant benefits for those who would make suboptimal decisions if left entirely to their own devices while imposing comparatively small costs on those inconvenienced by having to work around the state's "assistance" in order to pursue what they regard to be their own interests.[5] Cass Sunstein and Richard Thaler ("Sunstein & Thaler) proposed a similar approach that they call "libertarian paternalism,"[6] in recognition of its combination of the policy goal of paternalism coupled with the protection of individual freedom of choice.[7] This pair then

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[4] Colin F. Camerer et al., *Regulation for Conservatives: Behavioral Economics and the Case for "Asymmetric Paternalism*," 151 U. PA. L. REV. 1211 (2003).

[5] *Id.* at 1219.

[6] Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism is Not an Oxymoron*, 70 U. CHI. L. REV. 1159 (2003).

[7] There are subtle differences between the policy visions laid out by Camerer et al. and Sunstein & Thaler. The former do not absolutely rule out coercion, as long as the cost of coercion is substantially outweighed by the welfare benefits enjoyed by individuals who are less than fully rational. The latter support only regulations that do not prevent any individuals from pursuing their desired course of action and impose no more than a small amount of inconvenience on those who wish to avoid the intervention. So, for example, Camerer et al. favor medical licensure as an example of asymmetric paternalism because it offers substantial protections to individuals who could not be counted on to optimally assess the quality of physicians while imposing a relatively lesser cost of physicians who must satisfy the licensure requirements. Camerer et al., *supra* note __, at 1237. Sunstein & Thaler presumably would not consider this an example of libertarian paternalism because it not only imposes heavy costs on physicians who must satisfy the requirements, it also coercively prevents patients who wish to contract with an unlicensed physician for medical care from doing so. A

developed the idea in greater depth in their recently-published book entitled "Nudge: Improving Decisions About Health, Wealth and Happiness,"[8] which has garnered significant attention in the popular media as well as in academic circles.[9]

These scholars have made a significant contribution to legal and policy discourse by showing how the state can promote the underlying goal of paternalism – helping people achieve greater subjective expected utility than they would obtain on their own – with lower costs than those associated with regulatory mandates backed up by threats of fines, imprisonment, or other punishment. But their paradigm can be expanded, making the tools they promote even more useful. Non-coercive approaches to changing behavior can be used not only to help individuals maximize their SEU, but to encourage them to produce public goods and otherwise improve social welfare, even when doing so is inconsistent with maximizing their own utility. I call the use of "nudges" for this goal "libertarian welfarism."[10]

In this article, I situate the missing category of libertarian welfarism within the existing literature and explain how recognizing this category has two significant virtues for public policy: the concept of libertarian welfarism can help policy makers identify a class of useful "nudges" that might otherwise be overlooked, and it can often provide a

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nonmandatory certification mechanism, however, that allowed a physician who satisfied state requirements to advertise this, would be consistent with libertarian paternalism.

[8] Richard H. Thaler & Cass R. Sunstein, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS (2008)

[9] *See, e.g.*, Benjamin M. Friedman, *Guiding Forces*, N.Y. TIMES, August 24, 2008, at BR13, Elizabeth Kolbert, *What Was I Thinking?*, THE NEW YORKER (http://www.newyorker.com/arts/critics/books/2008/02/25/080225crbo_books_ kolbert?currentPage=all); Stephen Gandel, *Behavioral Economics Can Help You Save Money*, CNN MONEY, Jul. 24, 2008, (http://money.cnn.com/ 2008/07/24/magazines/ moneymag/105711588.moneymag/); Barbara Kiviat, *Lured Toward the Right Choice*, TIME, (http://www.time.com/time/magazine/article/0,9171,1727729,00.html).

[10] In the article version of their idea, Sunstein and Thaler recognize in passing the possibility that libertarian paternalism could be complemented by an approach that considers vulnerable third parties rather than the targeted actors themselves, but they neither flesh out the contours of this category nor compare its merits to those of libertarian paternalism. Sunstein & Thaler, *supra* note __, at 1162. The notion of a fourth category is entirely absent in the book version of their idea.

normative justification for nudges that is missing from libertarian paternalism. Libertarian welfarism can help us to both understand and justify a broad range of state actions – from requiring restaurants to post the calorie content of their meals, to publicizing greenhouse gas emissions of new cars, to providing recycling bins to homeowners, to automatically enrolling individuals in 401(k) and cadaveric organ donation programs unless they opt out – far better than can libertarian paternalism.

II. LIBERTARIAN PATERNALISM

The objective of a paternalist state is to increase the subjective expected utility of the citizens subject to a legal regulation.[11] The objective of the libertarian paternalist state is to accomplish, or at least make progress toward, this goal without resorting to coercion, as understood – roughly – as enacting regulations that mandate behavior on threat of some negative material consequence.[12] A policy fits within the libertarian paternalist paradigm if it "nudges" individuals to act in accordance with their best interests but allows them to ignore the nudge at minimal or no cost.[13]

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[11] Thaler and Sunstein put the point this way: "In our understanding, a policy is 'paternalistic' if it tries to influence choices in a way that will make choosers better off, as judged by themselves." Thaler & Sunstein, supra note __, at 5 (emphasis in original). For some common examples of paternalistic policies enacted into law, see CAL. VEH. CODE § 27803 (West 2007) (requiring drivers and passengers of motorcycles to wear a safety helmet); CAL. EDUC. CODE § 48201 (West 2007) (requiring persons age 6 to 18 to enroll in and attend a full-time school); CAL. EDUC. CODE § 48293 (West 2007) (establishing monetary penalties against parents or guardians who do not comply with compulsory education requirements); CAL. BUS. & PROF. CODE § 19921 (West 2007) (preventing individuals under the age of 21 years from entering gambling establishments).

[12] Thaler & Sunstein, *supra* note __, at 6.

[13] *Id.* ("the intervention must be easy and cheap to avoid"). Some critics have criticized the concept of libertarian paternalism on the grounds that it is inconsistent with some particular understanding of *libertarian* philosophy. This criticism misses the point of Sunstein and Thaler, whose argument is that the non-coercive nature of their paradigm should cause it to appeal to people who consider themselves libertarians.

A. The Empirical Basis

Research on human decision making conducted over the last four decades has catalogued of plethora of ways in which individuals violate the implicit assumptions of rational choice theory, which forms the behavioral model of neoclassical law-and-economics analysis. This research, known alternatively as "judgment and decision making," "behavioral decision making," or "behavioral economics," has been sufficiently reported and discussed in legal scholarship over the last decade that it is well-known to many legal scholars, at least in its broad contours, and providing a detailed treatise of its findings here would be redundant.[14] It is important, however, for understanding what is both innovative and potentially problematic about both libertarian paternalism to recognize that the relevant findings of judgment and decision making research can be loosely divided into two categories: (1) ways in which individuals systematically err in their assessment of factual information, and (2) ways in which preferences, as they are revealed by behavior, are at least partially constructed and dependent on contextual cues rather than fixed and invariant to context.

1. Judgment Biases

In order to maximize subjective expected utility, it is necessary for an actor to have a realistic assessment of the probabilities of the potential outcomes associated with various courses of action. To decide rationally whether to invest in the stock market or in a legal education, one needs to assess the potential financial and non-financial returns from each and evaluate the relative likelihood of the various possibilities. To decide rationally whether to rob a bank, one needs to consider the likelihood of being caught and convicted, the potential jail time associated with that outcome, and the likely disutility associated with imprisonment.

One thread of research in judgment and decision making details ways in which such factual assessments tend to systematically deviate

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[14] *See, e.g.*, Korobkin & Ulen, *supra* note __; Jolls et al., *supra* note __; Donald C. Langevoort, *Behavioral Theories of Judgment and Decision Making in Legal Scholarship: A Literature Review*, 51 VAND. L. REV. 1499 (1998).

from objective reality. The general finding is that people tend to overestimate the likelihood of salient or readily "available" events (such as homicides and airplane crashes) while underestimating the likelihood of events that are less mentally prominent (such as suicides and automobile accidents).[15] Memorable events are sometimes more common than events that seem more mundane but, of course, they aren't always.

Events are also judged to be more likely if they seem typical of a class of events. In the most famous experiment to demonstrate this "representativeness" heuristic, subjects were more likely to believe that the protagonist, "Linda," who was described as being active in liberal political causes, was a feminist bank teller than merely a bank teller (a logical impossibility).[16] When deriving numerical estimates, people tend to insufficiently adjust from "anchor" values that are salient but known to be only partially (if at all) diagnostic.[17] Judgments about current facts and probabilities of future events are likely to reveal an egocentric bias[18] that results from paying disproportionate attention to facts consistent with preexisting belief structures[19] and overestimating one's agency in the world.[20] Both of these effects are consistent with the fact that exemplars of our beliefs and our agency tend to be more salient than contradictory events.

Less well-known in the legal literature, but of potential use for legal policy, are several similar findings about the effect of salience on

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[15] See Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, 185 SCIENCE 1124, 1128 (1974).

[16] *Id.*

[17] *Id.* at 1128-30.

[18] David A. Armour & Shelley E. Taylor, *When Predictions Fail: The Dilemma of Unrealistic Optimism, in* HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT 334 (Thomas Gilovich et al. eds, 2002).

[19] *See, e.g.*, Charles G. Lord et al., *Biased Assimilation and Attitude Polarization: The Effects of Prior Theories on Subsequently Considered Evidence,* 37 J. PERSONALITY & SOC. PSYCHOL. 2098 (1979).

[20] *See, e.g.*, David Dunning et al., *Ambiguity and Self-Evaluation: The Role of Idiosyncratic Trait Definitions in Self-Serving Assessments of Ability, in* HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT 324 (Thomas Gilovich et al. eds, 2002).

probability judgments known as "support theory."[21] This body of research shows that the assessment of an event's probability will generally be higher if the event is described with greater specifically, or if each of the ways it might come about are enumerated compared to if it is described more vaguely and broadly.[22]

Generally, this body of research demonstrates that, when making probability judgments, individuals are unlikely to behave in an optimal, Bayesian fashion.[23] There is too much information available in our world for us to analyze consider all of it, much less process it in accordance with anything like statistically valid methods. People often rely on intuitions driven by attention to highly salient information rather than careful, reflective analysis, emotions rather than reason, and other heuristics that lead to boundedly-rational[24] rather than fully rational decisions.

These types of systematic tendencies can demonstrably lead to incorrect assessments of facts about the world, which in turn can lead individuals to make suboptimal decisions about how to act. It is, therefore, proper to refer to these tendencies as "biases." It is likely that the underlying heuristics have evolved over human history because they are generally useful (or, at least, were in the evolutionary environment) in helping us survive in an information-rich environment.[25] Nonetheless,

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[21] *See* Amos Tversky & Derek J. Koehler, *Support theory: A nonextensional representation of subjective probability*, 101 PSYCH. REV. 547 (1994); Craig R. Fox & Richard Birke, *Forecasting Trial Outcomes: Lawyers Assign Higher Probability to Possibilities that are Described in Greater Detail*, 26 L. & HUM. BEHAVIOR 159 (2002).

[22] *Id.*

[23] On the mathematics of rationally updating prior probability assessments when new information becomes available in accordance with "Bayes's Law," see, e.g., Robert V. Hogg & Allen T. Craig, INTRODUCTION TO MATHEMATICAL STATISTICS 208-09 (1970).

[24] The term "bounded rationality" is usually attributed to Herbert Simon. See Herbert A. Simon, *A Behavioral Model of Rational Choice*, 69 Q. J. ECON. 99 (1955); Herbert A. Simon, *Rational Choice and the Structure of the Environment*, *in* MODELS OF MAN: SOCIAL AND RATIONAL 261 (1957).

[25] *See, e.g.*, Colin Camerer et al., *Neuroeconomics: How Neuroscience Can Inform Economics*, 43 J. ECON. LIT. 9, 11, 26 (2005); Michael Waldman, *Systematic Errors and the Theory of Natural Selection*, 84 AM. ECON. REV. 482, 483 (1994).

they clearly can lead to errors of judgment in particular circumstances that cause individuals to deviate from the assumed goal of maximizing subjective expected utility. Some traditional economists might object that it is logically impossible for an individual's actions to be a suboptimal expression of subjective expected utility because the concept of "utility" has traditionally been defined solely by reference to choice, but common sense and common experience suggests that misestimation of probabilities or misunderstanding of facts can cause an individual to make a choice that makes him worse off, given his particular preference structure, than he might otherwise have been.[26] Daniel Kahneman has described this as the difference between "decision utility," which is the decision weight assigned to a particular course of action, and "experienced utility," which is a measure of the hedonic experience associated with that course of action.[27] For policy makers, the latter represents the appropriate understanding of SEU.

The problem is that, precisely because individuals are boundedly rational and almost always incapable of considering all information that might be relevant, it is difficult for the state to respond to these biases in neutral ways unlikely to introduce new biases. If the state provides information, or, more likely, enacts regulations requiring other actors to provide certain relevant information, this information is likely to become salient. But if this new information becomes salient, it is likely to crowd out other information that also might be relevant for maximizing subjective expected utility.

2. Context-Dependent Preferences

A very different thread of research in the field of judgment and decision making demonstrates that preferences are not fixed and invariant to context, as rational choice theorists usually assume. Rather,

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[26] *Cf.* Colin F. Camerer, *Wanting, Liking, and Learning: Neuroscience and Paternalism*, 73 U. CHI. L. REV. 87, 90-92 (2006) (criticizing the familiar "revealed preferences view [that] basically equates welfare (experienced utility) with choice (decision utility), as a matter of the *definition* of welfare") (emphasis in original).

[27] Daniel Kahneman, *New Challenges to the Rationality Assumption*, 150 J. INSTITUTIONAL & THEORETICAL ECON. 18 (1994),

preferences often are constructed at the point of decision making and based, at least in part, on contextual cues.[28]

One extremely important contextual cue, demonstrated by research on prospect theory, is the reference point from which a decision maker evaluates changes from the status quo as "gains" or "losses."[29] People typically care less about achieving a “gain” than they do about suffering a “loss.” As result, all other things being equal, people tend to shy away from risky choices when they perceive the upside to be a gain but embrace similar risks when they perceive their upside as avoiding a loss. This tendency is called the “framing effect.”[30] An even more important implication is that, all other things being equal, most people will favor what they perceive to be the status quo state of the world to an alternative state of the world (the “status quo bias”[31]) and, relatedly, place a higher value on what they own than what they don’t own (the “endowment effect”[32]).

The universe of potential or salient alternatives is another contextual feature that can affect preference construction. Given a series of choices that span a spectrum, people are more likely to select an intermediate choice (the "compromise effect"),and people are more likely to select an option if it is contrasted with a similar but inferior option than if it is dissimilar to all the other choices (the "contrast effect").[33] For example, people are more likely to prefer a mid-sized rental car over a compact model if they are also given the option of a

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[28] Sarah Lichtenstein & Paul Slovic, *The Construction of Preference: An Overview, in* THE CONSTRUCTION OF PREFERENCE 1 (Lichtenstein & Slovic, eds., 2006).

[29] Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 ECONOMETRICA 263 (1970).

[30] Daniel Kahneman, *Reference Points, Anchors, Norms, and Mixed Feelings*, 51 ORG. BEHAV. & HUM. DECISION PROCESSES 296, 298 (1992).

[31] William Samuelson & Richard Zeckhauser, *The Status Quo Bias in Decision Making*, 1 J. RISK & UNCERTAINTY 7 (1988).

[32] This term was coined by Thaler. Richard H. Thaler, *Toward a Positive Theory of Consumer Choice*, 1 J. ECON. BEHAV. & ORG. 39, 44 (1980); *see also* Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227 (2003).

[33] Mark Kelman et al., *Context-Dependence in Legal Decision Making*, 25 J. LEGAL STUD. 287, 288-89 (1996).

full-sized car than if only the first two options are available, and they are more likely to choose a large ice cream cone over a large cookie if a small ice cream cone is a third option.[34] Given the ability to divide their choice among options, people often diversify equally amongst available choices, even if some are substantially similar.[35]

Another example of how preferences can be highly context-dependent is the power of social pressure. According to the well-documented principle of social proof, people are be more likely to favor a particular choice if they believe most of their peers are making that choice than if they believe most of their peers are making a different one.[36] In different situations, the effect could be due to faith in the wisdom of others or desire for conformity. For example, if I were to learn that 90 percent of law professors drink Pepsi rather than Coke, I might switch my beverage choice from Coke to Pepsi. If the reason for my switch is that I have no inherent preference for the taste of either – or only a slight preference – but I gain satisfaction from feeling affiliation with a certain social group, my new knowledge can be said to have a preference-shaping effect. A related regularity is that preferences are often shaped by a desire to conform with social norms. Separate from what my colleagues actually drink, my preference for Coke or Pepsi might be affected by which of the beverages I believe it is good to drink, or which of the beverages I think will generate more esteem in eyes of my colleagues.[37]

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[34] For a clear discussion of these contextual effects, see Dan Ariely, PREDICTABLY IRRATIONAL 1-21 (2008). On Amir & Orly Lobel provide an interesting discussion of how the compromise and contrast effects might result from very different mental processes. On Amir & Orly Lobel, *Stumble, Predict, Nudge: How Behavioral Economics Informs Law and Policy*, 108 COLUM. L. REV. 2110-12 (2008).

[35] Daniel Reed et al., *Mixing Virtue and Vice: Combining Immediacy Effect and the Diversification Heuristic*, 12 J. BEHAVIORAL DECISION MAKING 257 (1999); Shlomo Benartzi & Richard H. Thaler, *Naïve Diversification Strategies in Defined Contribution Savings Plans*, 91 AM. ECON. REV. 79 (2001).

[36] Robert B. Cialdini, INFLUENCE: SCIENCE AND PRACTICE 100 (4th ed. 2001).

[37] Different theories of the power of social norms suggest slightly different motivational bases. Robert Cooter theorizes the power of norms comes from their internalization. Robert Cooter, *Normative Failure Theory of Law*, 82 CORNELL L. REV. 947 (1997). Richard McAdams argues that people comply with norms to earn the esteem of others. Richard H. McAdams, *The Origin, Development and Regulation of Norms*, 96 MICH. L.

Unlike the findings above that I have called judgment biases, it is difficult to say that, even in theory, the demonstrated effect of contextual cues in preference formation lead to decision making errors or mistakes. Assume that Anthony would not trade the apple in his lunch for Betsy's orange, but if he had the orange and Betsy had the apple, he would still not trade. Informed of the counterfactual, it is not clear that Anthony would feel compelled to alter his behavior. Or assume that Anthony would trade his apple for Betsy's orange if Betsy also had a tangerine but not if she also had a plum. Or assume that Anthony would not trade his apple for an orange if he knew that Carl and Donna like apples better than oranges, but he would if he knew Carl and Donna preferred oranges to apples. In all of these examples, Anthony seems to exhibit inconsistent preferences, but it is not clear that any of them constitute mistakes under the circumstances, because there is no reason that a fully rational person cannot have different preferences in different contexts. That is, once we realize that preferences do not always preexist opportunities to make choices but are often constructed in real time, apparently inconsistent choices might each be utility maximizing given different background conditions.

Another well-documented phenomenon that might be viewed as an example of the context-dependence of preferences is hyperbolic discounting.[38] When faced with the choice between two goods deliverable at different time periods, individuals will often display a much lower discount rate if both time periods are far into the future than if they are closer. For example, many people would choose $100 today over $110 tomorrow while also choosing to receive $110 in 31 days rather than $100 in 30 days.[39] Some decision making researchers believe this is a consequence of the conjecture that our minds work as dual-system processors, sometimes evaluating an option based on "hot" emotion, or affect, and sometimes based on "cold" analysis. When two

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REV. 338 (1997). Eric Posner believes that norms have power because conformance with them generally signals a cooperative nature and responsibility, which is valued by others. Eric Posner, LAW AND SOCIAL NORMS (2000).

[38] *See* Shane Frederick et al, *Time Discounting and Time Preference: A Critical Review,* 40 J. ECON. LIT. 351, 360-63 (2002).

[39] *Id.* at 361.

options are distant, the analytical mode is used to compare them. When at least one option is immediate, the temptation is more likely to provoke an affective response.

Described this way, it might seem that when a decision based on hot emotion is inconsistent with a decision that would have been resulted from cold analysis, the emotion-laden decision should be considered a mistake. And in some cases, this position seems quite defensible, especially when our visceral drives such hunger, thirst, sleep, sexual desire, or other cravings tempt us to take immediate actions that would have promoted survival in the evolutionary era but are suboptimal in modern society.[40] If you have made a considered decision to diet, it would probably increase your overall SEU if you were required to choose whether or not to order the chocolate cake a week in advance, thereby providing you with the opportunity to make a commitment to avoid the temptation, rather than when it is wheeled before you on the dessert cart and the wafting scent drains your will power. The primal urge humans have for sweet food, while once key to survival,[41] is no longer helpful, and five minutes of pleasure enjoyed while eating the cake probably will be followed by more than a compensating amount of regret.

Research suggests, however, that cold analysis will not always outperform hot emotion in its ability to yield utility maximizing decisions. Considerable research suggests that affective responses to decisions often unconsciously take into account a range of data about past experiences that individuals cannot consciously reference or logically explain.[42] Cold analysis, then, can cause individuals to overweight the aspects of a choice that they can describe and quantify in a rationalistic manner, such as price and other objective attributes, a

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[40] *See, e.g.*, George Loewenstein, *Out of Control: Visceral Influences on Behavior*, 65 ORG. BEHAV. & HUM. DECISION PROCESSES 272-73 (intense visceral factors drive a wedge between decisions and self-interest).

[41] *See* Richard Dawkins, THE SELFISH GENE 57 (1989).

[42] *See* Timothy D. Wilson et al., *Introspection About Reasons Can Reduce Post-Choice Satisfaction*, *in* THE CONSTRUCTION OF PREFERENCE 471, 472-73 (Lichtenstein & Slovic, eds. 2006).

regularity that has been called "lay rationalism."[43] In one experiment, researchers found that students who asked to rate how much they liked a series of posters and *provide reasons* before choosing one to take home expressed less satisfaction with their choice one month later than students who were not required to justify their preferences with reasons,[44] notwithstanding the well-known urge to rationalize actions to reduce cognitive dissonance.[45] In another, students asked simply to report their preference for five different jams provided ratings that approximated those of expert taste testers, but varied markedly when the students were required to coldly and rationalistically rate the jams on a variety of attributes.[46] Making decisions based on hot emotion will not lead to improvements in SEU in every circumstance, but it probably will in some.[47]

B. Tools

The principal tools of nudging, or of "choice architecture" as Sunstein & Thaler call it,[48] are the provision of various types of information to choosers and the selection of default rules. Altering

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[43] Christopher K. Hsee et al., *Lay Rationalism and Inconsistency Between Predicted Experience and Decision, in* THE CONSTRUCTION OF PREFERENCE 532, 533 (Lichtenstein & Slovic eds., 2006).

[44] *Id*. at 474-78. The authors conclude their study with the warning that "unbridled claims about the value of introspection need to be tempered." *Id.* at 485.

[45] *See generally* Leon Festinger, A THEORY OF COGNITIVE DISSONANCE (1957).

[46] T. D. Wilson & J.W. Schooler, *Thinking Too Much: Introspection Can Reduce the Quality of Preferences and Decisions*, 60 J. PERS. & SOC. PSYCHOL. 811 (1991).

[47] *Cf.* Ellen Peters, *The Functions of Affect in the Construction of Preferences, in* THE CONSTRUCTION OF PREFERENCE 454, 463 ("[Affect] sometimes may help and other times hurt decision processes….[T]he presence of affect does not guarantee good or bad decisions, only different information processing."); Timothy D. Wilson et al., Introspection About Reasons Can Reduce Post-Choice Satisfaction, 19 J. PERS. & SOC. PSYCHOL. 331, 339 (1993) ("[M]ore work is needed to specify the conditions under which introspecting about reasons will have deleterious consequences….[H]owever,…unbridled claims about the value of introspection need to be tempered.").

[48] Thaler & Sunstein, *supra* note __, at 81.

decision frames and imposing temporary behavioral prohibitions are additional, but less frequently cited, tools.

1. Informational Interventions

The usefulness of providing information is suggested by the broad finding that individuals routinely deviate from Bayesian reasoning when analyzing and evaluating information that is then used in the decision process. What I will call "informational interventions" involve providing information to individual actors about the likely consequences of behaviors. Such interventions can be accomplished by the government directly or through mandatory disclosure or reporting requirements that shifts the information-provision burden to other actors.

One simple example of a direct intervention, offered by Sunstein and Thaler, is the painting of the phrase "look right" in London crosswalks in order to reduce the likelihood that Americans and Europeans, accustomed to looking left for immediately oncoming traffic, will accidentally become road kill.[49] A second example comes from state governments advertising data that shows fewer college students smoke or engage in binge drinking than most college students are likely to predict.[50]

As an example of regulation requiring some actors to provide information to others, Sunstein & Thaler suggest requiring credit card companies to provide customers with annual electronic statements of the different type of charges they have been assessed (interest, annual fees, late fees, etc.) along with the algorithm according to which it assesses such charges.[51] This would allow customers, making use of web sites, to more easily determine which of the many credit card products available in the market place would minimize their annual cost of credit, assuming their spending patterns remained constant. Camerer et al. suggest laws requiring that "rent-to-own" establishments provide customers with the

[49] *Id.* at 90.

[50] *Id.* at 67-68.

[51] Thaler & Sunstein, *supra* note __, at 143. The authors propose similar requirements for mortgage lenders, cell phone service providers, and providers of Medicare prescription drug benefits.

implicit interest rate that they will pay for the goods in the event that they rent for a long enough period of to time to obtain title.[52]

Consistent with the values of libertarian paternalism, the provision of these types of information should help many individuals make decisions -- whether to cross the street, drink excessively, continue to use a particular credit card, or purchase consumer goods on an installment plan -- that are more likely to maximize their subjective expected utility, while leaving individuals who wish to ignore the information free to do so at little cost.

2. Default Rules

As a result of the status quo bias, more people are likely to choose an option if they consider it a constituent part of the status quo than if they view it as inconsistent with the status quo. This insight suggests that the state might be able to alter behavior by changing a default rule of law that apply to individuals who do not make an explicit choice amongst the available options, even if the burdens involved with opting out of the default choice are minimal. One example, used by both Sunstein & Thaler[53] and Camerer et al.,[54] is the decision that most employees face about whether to enroll in a company-sponsored 401(k) retirement plan.

Traditionally, the default rule for employer-sponsored but individually-funded retirement savings plans was "non-enrollment," meaning that an employee had to make an affirmative election to have a portion of her paycheck withheld and diverted into a retirement amount; no affirmative choice, no participation. Contrary to the predictions that follow from rational choice theory, companies that changed the default rule to "enrollment" by requiring employees to opt out if they did not want to participate reported a significant increase in the number of employees taking advantage of the plans.[55] Since the transaction costs of

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[52] Camerer et al., *supra* note __, at 1231.

[53] Thaler & Sunstein, *supra* note __ at 108-09.

[54] Camerer et al., *supra* note __, at 1227.

[55] *See, e.g.*, Bridget C. Madrian & Dennis F. Shea, The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior, 116 Q. J. ECON. 1149, 1184 (2001).

opting in or out of a 401(k) plan are relatively small – i.e., filling out a single form that is usually readily available from the employee's human resources department, if not on line – this data suggests that simply changing the default rule can nudge preferences.

Of course, changing the 401(k) decision from opt-in to opt-out will slightly inconvenience employees who, because of significant family wealth, high discount rates, or particularly good prospects for increasing their earnings in future years wish to spend all of today's income today and thus must go to the effort removing themselves from participation in the savings plan. But as long as we take as a given that employees may choose whether to invest in a 401(k) (that is, participation will be neither required nor prohibited), at least one of the two groups – the savers or the spenders – will have to take some action to make their preference known.

3. Frame Alteration

In addition to putting to use the insights of the status quo bias, understanding the related principle of loss aversion can help the state nudge individuals to save more for retirement. Sunstein & Thaler tout the "Save More Tomorrow" program, first suggested by Thaler and colleague Shlomo Benartzi[56] and now implemented by a wide variety of employers. Because people are averse to losses, relatively few sign up to take a current cut in pay in order to shift money into their retirement accounts. On the other hand, it turns out people are much more willing to enroll in a plan that automatically increases the nominal amount of dollars diverted into a retirement account as the employee's paycheck increases over the years.[57] Presumably this option enables employees to increase retirement savings without experiencing what feels like a loss in spendable earnings.[58]

4. Timing of Choice

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[56] Richard H. Thaler & Shlomo Benartzi, *Save More Tomorrow: Using Behavioral Economics to Increase Employee Savings*, 112 J. POL. ECONOMY s164 (2004).

[57] *Id.*

[58] Thaler & Sunstein, *supra* note __, at 112-18.

Another tool of libertarian paternalism is the "cooling off" period, designed with the goal of helping individuals to make choices under "cold," considered conditions, rather than "hot," emotional conditions.[59] Laws that provide a fixed number of days in which consumers can cancel door-to-door sales contracts,[60] waiting periods imposed on gun purchases[61] and divorces[62] are examples of this type of intervention.

III. WEAKNESSES OF LIBERTARIAN PATERNALISM

The paradigm of libertarian paternalism suffers from two principle weaknesses, which substantial limit the breadth of situations to which its tools can be applied in the real world. First, many actions that increase an individual's utility will decrease social welfare, raising the question of whether and how policy makers should nudge individuals when private and social welfare diverge. Second, when the net utility consequences to individuals of a particular choice are uncertain or indeterminate, libertarian paternalism can be defended only as a second-best solution to the resulting policymaking dilemmas. This Part describes these two shortcomings; the following Part explains how libertarian welfarism largely avoids them.

1. The Externality Problem

The most immediately obvious weakness of the libertarian paternalist paradigm is that, at least formally, it ignores negative

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[59] Thaler & Sunstein, *supra* note __, at 250-51; Sunstein & Thaler, *supra* note __, at 1184-85, 1187-88; Camerer et al., 1238-1247.

[60] 16 C.F.R. § 429.1 (requiring door-to-door sales contracts provide a three business-day cancellation period).

[61] *See, e.g.*, CAL. PENAL CODE § 12071(b)(3)(A) (West 2007) (imposing a 10-day waiting period before a firearm can be released to a buyer or transferee). Federal law no longer requires a cooling off period, having a replaced a 5-day waiting period with a required background check that can be processed immediately. See 18 U.S.C. § 922(t).

[62] *See, e.g.*, Conn. Gen. Stat. Ann. § 46.b-67(a) (requiring a 90-day pre-divorce waiting period).

externalities created by the behavior of the regulated individuals. The normative goal of most law and economics scholarship is the maximization of social welfare, which includes the utility of consequences both of actors subject to regulation and third-parties. But libertarian paternalism offers neither a theory as to why it would be appropriate for the government to concern itself only with the utility of the individuals directly affected by regulations, and not those who are indirectly impacted nor, alternatively, how libertarian paternalists ought to go about taking in to account the welfare effects on third parties. One possible explanation for this omission is that the proponents of libertarian paternalism view its tools as useful both to governments and private organizations, and the examples that they offer of how the tools might be employed often switch back and forth between those involving the private sector and government. But the normative justification for private action will necessarily be different than the normative justification for state action. A private company might reasonably choose to nudge its employees to enroll in a 401(k) plan if it believes that participation will increase their SEU, without concern for externalities that might be imposed on non-employees. For the government to demonstrate the same indifference to non-employees, however, demands a justification.

Another possible explanation is that the externalities associated with many, and perhaps even most, of the choices that individuals make every day are so small relative to the utility consequences experienced by the actors themselves lawmakers can safely ignore them. Whether I choose to read a book or watch television after dinner might have a great impact on my utility but very little, if any at all, on that of my neighbors, and the failure of libertarian paternalism to consider the problem of externalities will be inconsequential. The failure of libertarian paternalism to consider externalities also will be inconsequential if the background legal regime is constructed with Pigouvian taxes that fully internalize the costs of all externalities,[63] because in such cases the utility of non-actors will be unaffected by the choices of actors. For example, if a factory's pollution is taxed at the precise level of harm it causes to the environment, the non-actors (in this example, everyone other than the

[63] *See generally* Arthur C. Pigou, THE ECONOMICS OF WELFARE (1920).

factory) will be indifferent as to whether the factory owner chooses to produce an extra quantum of pollution and pay the corresponding fine or chooses not to pollute.

The areas in which the state considers regulating, however, rarely will fit into either of these categories. My wife might nudge me to read rather than watch television if she thinks I would learn more from a book and thus experience greater satisfaction, or she might nudge me to watch television is she thinks I have been working too hard and need to relax. Practically speaking, the government is unlikely to take an interest either way. And it is rare that existing regulation perfectly internalizes externalities. For most activities that create significant externalities, a decision by actors to engage in more or less of the activity will have implications for social welfare. Failing to take this problem seriously substantially weakens the power of the libertarian paternalist paradigm, because its normative basis becomes unclear.

This weakness does not undermine the libertarian paternalism paradigm in all matters of policy making. The state might, and often does, choose to limit its concern to the welfare of a limited group of actors for a reason external to the paradigm, in which case maximizing the welfare of target individuals and ignoring the welfare of everyone else might well be justified. For example, if Congress decides to enact legislation aimed solely at the goal of protecting consumers, it might then reasonably search for techniques in the libertarian paternalism toolkit that will nudge consumers to make purchase decisions that will maximize their SEU, without concern for the externalities that this behavior might create. In the absence of such an independent justification external to libertarian paternalism, however, the paradigm lacks a compelling normative basis.

B. The Indeterminacy Problem

The second significant problem with the libertarian paternalism paradigm is that in many if not most cases of significant importance, it will often be difficult or impossible to know whether any particular intervention will actually fulfill the goal of paternalism: making people better off as judged by their own utility functions. This problem exists whether the policy intervention attempts to provide information to undermine judgment biases or attempts to alter the context of a choice to

influence preference construction, although the precise nature of the problem is slightly different in these two cases: appropriately labeled a practical problem in the former case and a theoretical problem in the latter.

1. Informational Interventions

Informational interventions satisfy the libertarian condition of libertarian paternalism, in the sense that they do not mandate any behavior on the part of individuals.[64] Those for whom the additional information is either irrelevant or unnecessary are free to ignore it. And, in theory, providing information can help counteract biased judgments that can cause individuals to make suboptimal choices. The problem, however, is that, in practice, it is often difficult to know whether addressing one informational deficiency will crowd out other information relevant to maximizing subjective expected utility.

In the simplest cases, in which one or two factors almost certainly have the most substantial utility consequence in a decisions, informational interventions will be unobjectionable. Take, for example, the example of painting "look right" in London crosswalks.[65] Policymakers can reasonably assume that the desire to avoid being hit by a car is the single most important factor in making this decision, dwarfing the few other relevant factors, such as the desire to get to the other side of the road quickly. Because foreigners might not know, or might have forgotten, that traffic travels on the left side of the road in the United Kingdom, it is a safe bet that pointing out this fact will enable many pedestrians to make a much more accurate calculation of the probability of being hit should they attempt to cross at any particular moment. It is possible that emphasizing this information might cause individuals to pay relatively less attention to other risks, such as tripping on the curb, or to other factors relevant to utility, such as how much of a hurry they are in to get to the other side. But under the circumstances,

[64] Note, however, that such interventions often mandate behavior on the part of the third party who is required to provide or disclose the information, a feature that might in itself be problematic to true libertarians.

[65] Thaler & Sunstein, *supra* note __, at 90.

the benefits to pedestrians of the warning pretty clearly will swamp the costs of unduly focusing their attention on this particular hazard.

In even slightly more complicated cases, however, it quickly becomes less clear whether well-meaning informational interventions will create a net benefit to subjective expected utility. If credit card companies are required to provide customers with electronic information that makes it easy to compare the annual cost of credit, assuming consistent spending patterns, as Sunstein and Thaler recommend,[66] this would, no doubt improve consumers' ability to compare the products along that metric. At the same time, however, it might encourage consumers to pay relatively less attention to other credit card attributes (service, billing flexibility, perks, etc.) or to the validity of the assumptions necessarily embedded in the algorithm (i.e., that the consumer's spending patterns will be consistent from year to year).[67] Moreover, because sellers will have an incentive to exploit the bounded rationality of customers in order to increase profits,[68] one might expect that if a regulation requires credit card companies to provide information that makes the annual cost of credit more salient to consumers, those companies are likely to seek profit by reducing the quality of relatively less salient product attributes.[69] At the end of the day, will the information intervention leave customers better off? Possibly, but it is difficult to know for sure.

2. Preference-Construction Interventions

When the libertarian paternalism toolkit is extended beyond informational interventions to preference-shaping interventions, it not only becomes difficult to know whether the intervention will increase subjective expected utility in practice, it becomes indeterminate in

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[66] *Id.* at __.

[67] *Cf.* Amir & Lobel, *supra* note __, at 2114-15 (observing that requiring merchants to provide clearer information might cause consumers to overemphasize those attributes).

[68] *See generally* Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: The Problem of Market Manipulation*, 74 N.Y.U. L. REV. 630 (1999).

[69] *See generally*, Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1234-35 (2003).

theory. That is, when preferences are constructed in response to context, it is, at least arguably, not possible to say whether an individual will experience more utility in Context A (having made corresponding Choice A) or in Context B (having made corresponding Choice B).

To make the problem less abstract, consider the following specific example: assume a world with five employees, A, B, C, D, and E, each of whom earn identical salaries at Company X. Under a non-enrollment default rule, A and B will opt in to a 401(k) plan, while C, D, and E remain uninvolved. Under an enrollment default, E will opt out, while A, B, C, and D remain enrolled. (Assume the government can predict these outcomes because it first ran a pilot study in which several employee groups were assigned to each default condition.) Assuming that the transaction cost of avoiding the default outcome is trivial -- for example, checking off a box on an employee intake form -- under either rule each of the five employees will reach the end state that is optimal for them given the context in which the choice is made. So how can we determine which default will maximize the expected subjective utility of each of the five employees?

One response might be to say that saving is good for everyone, especially under a tax-favored plan, so the enrollment default maximizes employee expected utility, and the Sunstein/Thaler brand of libertarian paternalists might be fairly understood as implicitly making just this type of assumption.[70] This move, however, undermines the critical premises of libertarian paternalism that preferences are heterogeneous and policymakers are not omniscient. If one size fit all and the government always knew what was best for individuals, there would be no reason to favor libertarian paternalism over coercive paternalism. In such a world, the state might as well mandate participation, an approach that (given these assumptions) would benefit E in addition to A, B, C, and D. In reality, the situations in which there is both complete homogeneity of preferences and near-certainty that the state can know which default will maximize SEU are likely to be few.

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[70] *See* Amir & Lobel, *supra* note __, at 2120 ("Thaler and Sunstein's assumption that, absent irrationalities, every individual would agree that future savings and improved long-term health are better than immediate satisfaction and gratification seems problematic."); Gregory Mitchell, *Libertarian Paternalism Is An Oxymoron*, 99 NW. U. L. REV. 1245, 1268-69 (2005) (criticizing Sunstein & Thaler for assuming that central planners can identify objective welfare measures that will satisfy everyone).

A different response would be to compare the numbers of employees who would opt out of the different possible defaults. Since only one individual (E) will opt out of the enrollment default, whereas two (A & B) will opt out of the nonenrollment default, the enrollment default is preferable. But this logic is flawed. It would be appropriate if the choice of default affected only transaction costs and not preferences, such that, let's say, A, B, and C would opt into enrollment and D, and E would opt out of enrollment. In that circumstance, each employee would end up with the same (personally optimal) end state under either default rule, and the only issue would be which rule would minimize transaction costs. Assuming that the transaction costs of switching in and out of enrollment are the same, and that the switching costs are identical for each employee, the rule that requires fewer employees to opt out would minimize transaction costs and therefore be more efficient.[71] In our example, however, the end state experienced by C & D depends on the default, and even the state that could predict the number of employees that would opt out of either defaults would have no way of determining whether enrollment or nonenrollment would provide more expected subjective utility for the employees who would not opt out of either default.

3. The Response: Compared to What?

Whether the indeterminacy criticism of libertarian paternalism is problematic for the paradigm depends on the point of comparison. Sunstein & Thaler implicitly assume that the alternative to libertarian paternalism is either coercive paternalism, which would be even less likely to improve subjective expected utility than libertarian paternalism because the unhappy cannot opt out, or doing nothing at all.

Concerning the latter option, Sunstein & Thaler argue that, because information and context are ubiquitous, there is no truly neutral way to present information or options.[72] Decisions are never made in a

[71] If these assumptions fail to hold, the analysis becomes slightly more complicated. See generally Ian Ayres, *Making a Difference: The Contractual Contributions of Easterbrook and Fischel*, 59 U. CHI. L. REV. 1391 (1992).

[72] Thaler & Sunstein, *supra* note __, at 10, 237, 243.

vacuum. To make any decision, individuals will have to consider some information, and they can never consider and process in an unbiased way every piece of relevant information. They will always have to make the choice in some context. Given this reality, it is better for the state to nudge individuals in the direction policy makers *think* will make most of them better off – perhaps by imagining what they think most people would choose in a world without context, or hypothesizing which result would likely win the highest ex post satisfaction ratings – than in some other direction?[73] If we think that the annual cost of credit is likely to be the most important attribute of a credit card to most customers but difficult to understand, isn't it better to provide them with that information in a digestible way rather than providing some other information or none at all? If we think most people will lead overall happier lives if they save more for retirement, even if we can't be absolutely sure, isn't a 401(k) enrollment default preferable to nonenrollment default? If we think that people will be happier with their consumer purchases if we encourage cold, cognitive reasoning and discourage hot, emotional intuition by instituting cooling off periods, isn't it better to have cooling off periods than not?

A particularly convincing illustration of this argument offered by Sunstein & Thaler is that research has shown that cafeteria diners are more likely to choose what comes first in the line than what comes last in the line.[74] Since it is physically impossible to place everything at the same place in the line, the cafeteria manager will have to either put fruit in front of cake (favoring fruit) or cake in front of fruit (favoring cake). With neutrality not an option, the authors ask rhetorically, doesn't it make more sense, they ask, for the manager to place fruit first than to put cake first or choose randomly?[75]

Framed in this way, the argument for libertarian paternalism is compelling, but the frame is too narrow. There is another option besides

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[73] *See, e.g.*, Sunstein & Thaler, *supra* note __, at 1200 ("We happily grant that planners are human….Nevertheless, … these human planners are sometimes forced to make choices, and it is surely better to have them trying to improve people's welfare rather than the opposite.")

[74] Thaler & Sunstein, *supra* note __, at 1.

[75] *Id.* at 4-5.

laissez-faire inaction, coercion, and "self-conscious efforts… to steer people choices in directions that will improve their lives."[76] If the policy goal is to maximize the SEU of targeted individuals, the libertarian paternalists are clearly correct that it is preferable to nudge individuals in the direction that policy makers think will be better for the individuals than options they think will be worse for the individuals. But what the indeterminacy problem really suggests is that, at least in many circumstances, it might be more sensible to attempt to implement a different policy goal altogether. The conceptual category of libertarian welfarism provides the needed goal.[77]

IV. LIBERTARIAN WELFARISM

A. A Missing Category

As mentioned above, most law and economics analysis assumes that the proper normative goal of state regulation of private behavior is to increase social welfare.[78] A policy is usually understood to fulfill this criteria if it satisfies the requirement of Kaldor-Hicks efficiency[79] – that is, the beneficiaries of the regulation gain enough such that they could fully compensate those who are burdened – otherwise known as cost-benefit analysis.[80] Even if actors are perfectly capable of maximizing

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[76] *Id.* at 5.

[77] In what he calls a "libertarian approach to choice-framing paternalism," Gregory Mitchell suggests a goal that is different both libertarian paternalism and libertarian welfarism. Mitchell argues that the state should "frame choices in ways that push irrational persons in directions that maximize their liberty or help them retain the greatest degree of future freedom to contract" – such as, for example, by favoring default rules like at-will employment. Mitchell, *supra* note __, at 1262. Because true freedom includes the freedom to commit oneself to future actions, I do not think that maximizing "*future* freedom to contract" is a normatively defensible objective, even if we assume the primacy of personal liberty on the value hierarchy.

[78] *See, e.g.*, A. Mitchell Polinsky, AN INTRODUCTION TO LAW AND ECONOMICS 7-8 (3d. ed., 2003) (defining "efficiency"); Steven Shavell, ECONOMIC ANALYSIS OF Law 1-2 (2004)

[79] *See, e.g.*, Richard A. Posner, ECONOMIC ANALYSIS OF LAW 13 (7th ed. 2007).

[80] *See* Matthew Adler, *Beyond Efficiency and Procedure: A Welfarist Theory of Regulation*, 28 FLA. ST. L. REV. 241, 244-46 (noting that this requirement of what he

their SEU without assistance from the state, in so doing they often impose significant costs, or "negative externalities," on others. The welfarist norm implies that, when private benefits to focal actors are small relative to the negative externalities they impose on others, the state legitimately can coerce behavior to protect those others, or to protect society generally. I refer to this as the "welfarism" justification for regulation.

Coercive regulation based on the welfarism justification is generally considered by law and economics scholars to be appropriate in a far wider set of circumstances than coercion based on the paternalism justification. This is because collective action problems – in which actions that benefit individual actors harm the collective good and actions that benefit the collective good require sacrifice by individual actors – are ubiquitous. In a direct application of the tragedy of the commons,[81] global warming has reached crisis proportions because millions of individual decisions to pollute are in the private interests of the individuals and companies that make those decisions while most of costs are externalized onto the rest of society. Soaring medical costs threaten the very viable of health care insurance systems because individuals with insurance have a private incentive to overuse health care resources while externalizing the costs to the insurance pool. The list could go on.

Just as legal policies that apply nudging techniques can increase the likelihood that individuals will maximize their own SEUs, the same tools can be employed to encourage actors to act in ways that increase social welfare, even when doing will have either negative or uncertain effects on their individual utilities. That is, just as the use of nudging tools can differentiate between coercive paternalism and libertarian paternalism, the same tools can differentiate between coercive welfarism and libertarian welfarism.

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calls the "neoclassical" theory of regulation "is a matter of interpretation -- or at least sometimes it is -- since the neoclassicist's commitment to efficiency …is sometimes implicit or even obscured rather than laid out in plain view.")

[81] Garrett Hardin, *The Tragedy of the Commons*, 162 SCIENCE 1243 (1968).

MEANS OF IMPLEMENTATION	POLICY GOAL: Paternalism	POLICY GOAL: Welfarism
Coercive	Coercive Paternalism	Coercive Welfarism
Non-coercive	Libertarian Paternalism	***Libertarian Welfarism***

FIGURE 1

B. The Divergence Between Private and Social Costs

When behaviors that would increase the utility of the actors subject to regulation would create positive externalities, no externalities, or very small negative externalities relative to the benefits enjoyed by individual actors, the libertarian welfarism and libertarian paternalism paradigms would suggest the same policy interventions, and the category of libertarian welfarism adds little of practical importance to policy debates. Under either approach, the state would attempt to nudge individuals so as to maximize their private utility, which would also maximize social welfare. But adding the category of libertarian welfarism to the policy maker's mental model of regulation offers two distinct benefits. It offers a different – and more normatively defensible – set of policy prescriptions than does libertarian welfarism with private and social welfare diverges, as it often does. And it provides a needed justification for using nudges where the effect of such nudges on private

utility is unclear or indeterminate but the valence of the externalities that will be created by private behaviors is clear.

Many important public policy issues concern collective action problems: society as a whole would be better off if everyone did X, but each individual is better off if she does Y, whether or not everyone else chooses to do X or Y. To take one ubiquitous example, almost any policy issue involving pollution, understood broadly, has this structure. A factory owner is selfishly better off if he creates more air pollution because he would have to pay the full cost of mitigation but can externalize most of the burdens that result from the pollution his neighbors. In many (although not all) circumstances, however, social welfare would be maximized if the factory owner were to invest in mitigation. A *pure* libertarian paternalist would attempt to nudge a factory owners to pollute more if doing so would increase his expected utility, even if the costs to neighbors would be so high that the activity would reduce net social welfare.[82] A libertarian welfarist, in contrast, would support interventions that would encourage factory owners to invest in mitigation in such circumstances.

More specifically, a libertarian welfarist might ask the following questions: Given that people will often try to act in their selfish interest, how can the government regulate the provision of information so as to accentuate the private benefits of mitigation? Given that most people are altruistic to at least some degree, how can the government regulate the provision of information so as to accentuate the social costs of pollution (or the social benefits of mitigation) and thus harness altruistic impulses by making these costs more salient to decision makers? Given that many people wish to conform to social norms, how can the context of choice be structured so that activities that are privately beneficial but socially costly be made visible, thus making the socially optimal activity more privately desirable? Given that people usually prefer the status quo over change, is it possible to structure the choice so that the socially optimal decision is viewed as consistent with the status quo by most decision makers?

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[82] The proponents of liberal paternalism might claim that inherent in their specific policy proposals is the limiting condition that the state should not nudge actors to significantly reduce social welfare, but the pure theory of liberal paternalism is indifferent to social welfare.

The following sections provide some examples of how libertarian paternalist and libertarian welfarist interventions would differ in cases where private and social welfare diverge.

1. Informational Interventions

The Environmental Protection Agency (EPA) requires that manufacturers of new cars post on their windshields the estimated gas mileage and the annual cost of gasoline for that car, given the assumptions of a certain price per gallon of gasoline and an average number of miles driven annually.[83] This regulation is an informational intervention that fits comfortably within the libertarian paternalism paradigm. It is likely that the cost of operating a new car is relevant to the subjective expected utility many buyers will obtain from the purchase, and that because of the difficulty to estimate this cost, it might not be salient in the purchasing decision of many buyers. Requiring manufacturers to provide this information is likely to make it more accessible to buyers, and nudge them to buy cars that are cheaper to operate, which, all else being equal, should increase private utility.

Compare the EPA rule with a new California statute that requires manufacturers to add another sticker to the window of new cars sold in that state.[84] These stickers, adorned with a green border, provide a numerical rating of the car's greenhouse gas emissions on a scale of 1-10, with 5 signifying the increase in global warming caused by the car's emissions are average compared to other new cars.[85] This law is an example of libertarian welfarism. It is clearly a *libertarian* approach to regulation, in the sense that it mandates no behavior: consumers are free to ignore the information. It is a libertarian welfarist, rather than a libertarian paternalist intervention, because, to the extent that car's

[83] 40 C.F.R. § 600.306-08 – 307-08.

[84] CAL. HEALTH & SAFETY CODE § 43200.1 (West 2007).

[85] A score of 5 signifies that a car's emissions will have an impact on Global Warming equivalent to that of an average new vehicle. A higher score denotes a car that is 'better for the environment'. *See New Calif. Cars to Sport Greenhouse Gas Labels: Global Warming Score Will Show Buyers Estimated Emissions*, MSNBC, June 20, 2008 (http://www.msnbc.msn.com/id/25284062/).

greenhouse gas emissions are uncorrelated with its gas mileage (which is already posted on the car's window) and thus the private costs of vehicle operation, the requirement can only affect consumer behavior by making the social costs of the purchase decision more salient to the customer. The law attempts to nudge the buyer to do what maximizes social welfare even when that bears virtually no relationship to his private utility.

2. Social Proof

Whereas libertarian paternalists propose that lawmakers provide information about social practices in order to encourage individuals to take steps that are in their own interest, the libertarian welfarist will try to use state power to create or reinforce social norms that will encourage those individuals to act in a way consistent with the collective interest, even when it is inconsistent with their self-interest.

Because the way in which individuals construct preferences can incorporate a general desire to conform to social norms, a libertarian welfarist would favor providing individuals with hard-to-locate information about the content of norms when greater conformity would create positive externalities. Charitable giving usually has positive externalities, so a libertarian welfarist would favor having the Internal Revenue Service inform taxpayers of the average amount of charitable gifts made by others with similar income.[86] This tactic would create some risk that taxpayers who are more charitable than the average would reduce their gifts, but the more likely effect is that it would motivate the miserly to increase their donations in order to at least reach the average donation level. Conservation of natural resources also has positive externalities, so a libertarian welfarist would support a recent trend among utilities of reporting to customers how their level of energy consumption compares to that of their neighbors.[87] At least one utility has reported that this approach has succeeded in promoting conservation by above-average energy users motivated to conform with the

[86] This idea was proposed by Ian Ayres.

[87] Leslie Kaufman, *Utilities Turn Their Customers Green with Envy*, N.Y. TIMES, Jan. 30, 2009.

conservation efforts of their peers.[88] Neither of these interventions should appeal to a true libertarian paternalist, because there is no reason to think that a person who chooses not to donate or conserve when he is ignorant of what others do but would do one or both given knowledge of norms would enjoy more SEU in the latter case than in the former.

Recycling of household refuse presents a classic example of a collective action problem that a libertarian welfarist might seek to address, but that a libertarian paternalist would not. Recycling produces significant social benefits – reduced use of landfills, fewer emissions from incinerators, less litter, energy conservation, etc. – but nearly all of these benefits are externalized. For any individual, sorting household trash is costly and the benefits are virtually nonexistent, so lawmakers strictly applying the lessons of libertarian paternalism would have no interest in attempting to nudge people to recycle, while libertarian paternalists would want to do precisely that.

Government-sponsored, curbside pick-up programs for recyclable materials, which are now ubiquitous in American cities,[89] demonstrate how a libertarian welfarist might go one step beyond merely providing information about hard-to-see norms and actually encouraging the development of norms that will create positive externalities. Curbside pick-up programs have been tremendously effective at encouraging recycling.[90] Much of the explanation for this success is that curbside pick-up substantially reduces the private cost of recycling. That reducing cost is a primary driver of behavior is indicated by the fact that recycling rates are higher in municipalities that permit residents to commingle all their recyclable materials (i.e., those that make it as easy as possible) than in municipalities that require residents to separate different types of

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[88] *Id.*

[89] *See, e.g.*, Ann E. Carlson, *Recycling Norms*, 89 CAL. L. REV. 1231, 1265 (2001).

[90] The portion of solid waste recycled in the United States increased from 10 percent in 1990 to nearly 30 percent in 2000, and this is due, at least in part, to curbside recycling programs. *See* Thomas C. Kinnamon, *Policy Watch: Examining the Justification for Residential Recycling*, J. ECON. PERSPECTIVES, Fall 2006, at 219, 219 (citing BioCycle's annual *The State of Garbage in America* study for 2004); *see also* Ljupka Arsova et al., *The State Of Garbage In America*, BioCycle, Dec. 2008, at 22, 22-23 (http://www.jgpress.com/archives/_free/001782.html).

recyclable material.[91] But reductions in private cost cannot fully explain household recycling, because dividing refuse into even two categories – garbage destined for the landfill and recyclable material – is inconvenient compared to throwing everything into a single garbage bin.

Curbside recycling programs not only make recycling more convenient, the presence of the bins on the street provides information to individuals about whether their neighbors recycle.[92] The evidence suggests that this matters quite a bit: people who recycle report a much higher percentage of their friends and neighbors recycle than do non-recyclers.[93] When some people engage in a behavior that increases social welfare and that behavior is visible, a norm can emerge that then increases the likelihood that others will decide that they prefer to act in accordance with the norm.

3. Policy-Forcing Default Rules

Whereas a libertarian paternalist would select default rules in an effort to encourage individuals to maximize their SEU, a libertarian welfarist will choose default rules that encourage individuals to act in the best interests of society in general by minimizing negative externalities and maximizing positive externalities. Elsewhere I have called these "policy-forcing" default rules.[94]

As an example, consider some of the facts of the well-known case of *Moore v. Regents of the University of California*[95]: John Moore, suffered from hairy-cell leukemia and needed his spleen removed. His physician, also a medical researcher, used Moore's spleen to create the financially valuable Mo cell line but shared none of the profits with Moore, who sued for compensation. Although the court ruled that the

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[91] Carlson, *supra* note __, at 1275-78.

[92] *Id.* at 1266.

[93] *Id.* at 1290.

[94] Russell Korobkin, *"No Compensation" or "Pro Compensation":* Moore v. Regents *and Default Rules for Human Tissue Donations*, 40 J. HEALTH L. 1, 18 (2007).

[95] 793 P.2d 479 (Cal. 1990).

physician had violated the rules of informed consent, it held that Moore was not entitled to compensation for the value of his spleen.[96]

This holding is usually explained as a rule of property or tort law, but it can also be understood as a default rule of contract law. There is little doubt that Moore legally could have negotiated a fee for the use of his organ prior to the surgery -- other individuals with unique physical properties have sold blood, for example, to medical researchers, and federal law prohibits the sale of organs only for "transplant" purposes -- but there was no discussion about compensation between Moore and his physician. The court's ruling established a "no-compensation" default for when physicians and patients do not explicitly discuss compensation for the research use of human tissues.[97] A decade later, in *Greenberg v. Miami Children's Hospital*,[98] a case involving the use of tissue samples from patients with Canavan disease that were used to develop a patentable genetic test for the mutation that causes the disease, a federal district court in Florida expanded the rule to apply also to tissue donors who lack a therapeutic relationship with the medical researcher.

There are many reasons to think that the choice between "pro-compensation" and "no-compensation" default rules will affect the number of uncompensated tissue donations for medical research by affecting the context in which the decision is made. First, there is the pure fact of inertia, which favors the status quo over a deviation from the status quo in any situation.[99] Second, under a non-compensation default, in order to even potentially obtain compensation, donors must raise the issue of payment with medical researchers, which would undoubtedly be uncomfortable for many. Third, the default rule might suggest a social norm of altruism, making a request for compensation appear greedy in this circumstance. In contrast, a pro-compensation default might suggest that payment is deserved and that someone who would waive it is a rube.[100]

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[96] *Id.* at 480-85.

[97] Korobkin, *No Compensation*, *supra* note __, at 9-10.

[98] 264 F.Supp.2d 1064 (S.D. Fla. 2003).

[99] *See* Korobkin, *Endowment Effect*, *supra* note __,at 1228-29.

[100] Korobkin, *No Compensation*, *supra* note __,at 20.

The no-compensation default rule cannot be justified on the basis of paternalism, assuming that the intended targets of the rule are tissue donors. Both John Moore and the Greenberg plaintiffs would undoubtedly have been objectively better off had they received compensation. Even had they been altruistically inclined, as the *Greenberg* plaintiffs were,[101] they could have used their compensation to fund further medical research of access to diagnostic tests and treatments for people suffering from the illnesses that affected them. Libertarian paternalism lends support to a pro-compensation default, under which the donor of valuable tissues that led to a medical breakthrough would be entitled to some amount of compensation absent an affirmative decision to forego it. The no-compensation rule is justified, however, under the libertarian welfarism paradigm. By encouraging more people to donate tissues to medical research altruistically, the no-compensation rule reduces the cost of medical research – a result that clearly enhances social welfare.

Another example of a divergence between libertarian paternalist and libertarian welfarist approaches to default rules can be seen in an example discussed in detail by Thaler & Sunstein.[102] In the United States, the default rule concerning the donation of bodily organs for transplantation following death is "no donation." Most states couple this default rule with low cost opt-in provisions, such as signing a donor card or indicate their willingness to be a donor at the time they obtain or renew their driver's license.[103] Based on research that shows that Americans (and Europeans from countries with the same default rule) are far less likely to become organ donors than European from countries with "presumed consent" default rules and opt-out provisions,[104]

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[101] The plaintiffs' goal was to ensure affordable access to diagnostic tests. *Greenberg*, 264 F.Supp.2d at 1066-67.

[102] Thaler & Sunstein, *supra* note __, at 175-82.

[103] *See, e.g.*, Michelle Oberman, *When the Truth is Not Enough: Tissue Donation, Altruism, and the Market*, 55 DEPAUL L. REV. 903, 938 (2006).

[104] Eric J. Johnson & Daniel Goldstein, *Do Defaults Save Lives?*, 302 SCIENCE 1338 (2003).

Sunstein & Thaler propose changing the default rule in the United States.[105]

While it is almost certain that changing the default rule to presumed consent would increase the number of cadaveric organ donations in the United States, it is implausible that this change would increase the SEU of individual donors, who are, of course, dead at the time of donation. There are several reasons that American organ donation rates are low under the no-donation default. The first is that some people don't care one way or another about being donors, but they do not wish to think about their mortality, which they must do in order to opt out of the default.[106] A second group of people do not become donors because they would suffer psychic costs while still alive thinking about their bodies being carved into pieces after they die.[107] A third group fear that if they are potential cadaveric donors an overzealous transplant physician lusting after their organs might prematurely end their life,[108] a small but presumably non-zero risk.[109] The experienced utility of individuals who fall into the first category might be unchanged by a change in default rules, but the experienced utility of those in the second and third group who chose not to opt out of a presumed consent default would, if anything, decrease. It would be exceedingly difficult to argue that a change in default rules that caused some members of each of these groups to become cadaveric donors would be utility enhancing for

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[105] Thaler & Sunstein, *supra* note __, at 177-79.

[106] *See* Carmen M. Radecki and James Jaccard, *Psychological Aspects of Organ Donation: A Critical Review and Synthesis of Individual and Next-of-Kin Donation Decisions*, 16 HEALTH PSYCHOL. 183, 183 (1997) (noting that beliefs about organ donation are influenced by the consequences of choosing to donate, including confronting the issue of mortality).

[107] Margareta Sanner, *Attitudes Toward Organ Donation and Transplantation: A Model for Understanding Reactions to Medical Procedures After Death*, 38 SOC. SCI. & MED. 1141, 1147 (1994) (discussing discomfort with a dead body being cut and the organs removed as a motive for individuals' reticence towards organ donation)

[108] *Id.* at 1148 (discussing individuals' fear that death will be hastened for the sake of someone more highly regarded who is in need of organs).

[109] *Cf.* Charles Ornstein & Tracy Weber, *Death in San Louis Obispo Organ Donor Case is Ruled Natural*, L.A. TIMES, Mar. 9, 2007, at B5 (discussing allegation that an organ donor's death was hastened by doctors for the benefit of the presumptive donee).

the donors. For a libertarian paternalist, the policy implication seems clear: leave the no-donation default rule in place.

On the other hand, the positive externalities associated with cadaveric organ donation are large, and the positive consequences for social welfare clear. Each year, thousands of Americans on the waiting lists for donor organs die every year because the demand for donations far exceeds supply.[110] If the U.S. were to achieve organ donation rates as high as the European countries with presumed consent default rules, many if not most of these lives could be saved. If it is possible to make any interpersonal utility comparisons of any kind, it seems safe to predict that the increased welfare enjoyed by the people whose lives would be saved by such a policy would outweigh the decreased welfare suffered by the individuals who are not now organ donors but do not care enough about the issue to exert the minimal amount of effort needed to opt out of a presumed consent regime. A presumed consent rule thus clearly fits within the libertarian welfarist model.[111]

C. An Alternative to the Indeterminacy of Libertarian Paternalism

Recall from Part III the two indeterminacy problems that undermine the libertarian paternalism paradigm. First, when informational interventions would alter choice by making some information more salient than it otherwise would be, it is often practically difficult to predict with a high degree of certain which choice would actually maximize the subjective expected utility of most

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[110] In 2006, 130,527 individuals were on the waiting list for an organ donation. Of those on the waiting list in 2006, 7,191 died. *Reported Deaths and Annual Death Rates Per 1000 Patient-Years at Risk Waiting List, 1997 to 2006*, 2007 Annual Report of the U.S. Organ Procurement and Transplantation Network and the Scientific Registry of Transplant Recipients: Transplant Data 1997-2006, U.S. Dept. of Health & Human Services (http://www.optn.org/AR2007/chapter_index.htm).

[111] To be fair, Sunstein and Thaler recognize in the article-version of their argument that the organ donation example is inconsistent with many of their other policy examples (in that the benefits of a presumed consent default flow to third parties rather than the choosers) and call the consequence or organ donation "libertarian benevolence." Sunstein & Thaler, *supra* note __, at 1192-93. Puzzlingly, this distinction is not made when they elaborate on organ donation and recommend a presumed consent default in *Nudge*.

individuals. Second, when the government action changes behavior of individuals by altering the context in which preferences are constructed, it is theoretically impossible to say which choice maximizes subjective expected utility: one choice does in the first context, and the alternative choice does in the second context. A libertarian paternalist might try to avoid this criticism by judging SEU based on hypothetical choice in a world devoid of context, but this would not avoid the practical problem of determining which choice would maximize SEU under such a set of nonexistent conditions.

Libertarian welfarism has the advantage of avoiding these problems in many circumstances. In some cases, it will be practically difficult to determine which individual behavior would maximize social welfare, but in many more instances the valence of externalities will be strongly in one direction: i.e., the production of greenhouse gasses will almost always have a large negative externalities; cadaveric organ donation will always have positive externalities. In these situations, the libertarian paternalism paradigm can lead to clear policy prescriptions even when libertarian paternalism does not.

New York City recently enacted a law requiring restaurant chains to post the number of calories in their offerings along side the prices.[112] This requirement could possibly be defended as consistent with the libertarian paternalism paradigm, on the grounds that the calorie content of food is relevant to diners' choices but difficult to come by with out assistance from the regulatory state. And, quite obviously, people who aren't calorie sensitive can ignore the information, just as those who are not price sensitive can ignore the prices. This argument has some force, but is it really clear that the information will increase the SEU of diners? By making calories more salient to the choice process, the law is likely to alter behavior. But by making calories more salient, other features of potential meals, such as expectations of how the items will taste, will become relatively less important in the decision making processes of diners. As a *New York Times* columnist sarcastically put the point: "How

[112] 24 RCNY HEALTH. CODE § 81.50. King County, Washington, has adopted a similar mandate, and at least 21 other state and local governments are considering following suit. Stephanie Saul, *Conflict on the Menu*, N.Y. TIMES, Feb. 16, 2008.

enticing: a fistful of calories on a bed of cholesterol, to go."[113] Research on judgment and decision making teaches us there is no truly neutral presentation of information, so how do we know that people who respond to the calorie listings by switch to lower calorie entrees that don't taste as good are actually subjectively better off as a result?

The calorie-posting requirement is far better justified by the libertarian welfarist paradigm. It is well-known that obesity is a growing problem in the United States, with 33% of adults and 17% of children now obese compared with 15% and 6% respectively 30 years ago.[114] The health consequences of obesity are not just limited to individuals. Experts have estimated that treating obesity-related illnesses costs the nation's health care system $93 billion per year,[115] much of which is paid by Medicare, Medicaid, and other public programs.[116] The financial consequences of obese individuals with private group insurance have less of a direct effect on the taxpayers, but they do affect the health insurance premiums of the other members of their rating groups. In other words, obesity has significant negative externalities, which itself justifies a policy of nudging people toward eating fewer calories, whether or not it is possible to say that the intervention will increase the utility of the individual targets.

A similar analysis applies to selecting the default rule for enrollment in 401(k) retirement programs, discussed by Thaler &

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[113] Timothy Egan, *Nanny Nation*, N.Y. TIMES, Aug. 6, 2008 (http://egan.blogs.nytimes.com/2008/08/06/nanny-nation/?ex=1218772800&en=a557aa731c21677e&ei=5070&emc=eta1/)

[114] Cynthia L. Ogden et al., *The Epidemiology of Obesity*, 132 GASTROENTEROLOGY 2087, 2090-91 (2007).

[115] Ceci Connolly, *Obesity Gets Part of Blame for Care Costs*, WASH. POST, Oct. 20, 2004, at A03,

[116] According to one study, in 1998 the public sector was responsible for financing nearly half of medical spending attributable to excessive weight. Eric A. Finkelstein, *National Medical Spending Attributable to Overweight and Obesity: How much, and Who's Paying?*, HEALTH AFF., 223-24 (2003). Another found that nearly 1/4 of Medicare spending in 2002 was attributable to obese patients. Kenneth E. Thorpe & David H. Howard, *The Rise In Spending Among Medicare Beneficiaries: The Role Of Chronic Disease Prevalence And Changes In Treatment Intensity*, HEALTH AFF., 384 (2006),

Sunstein. We know, not only from theory but also from actual experience with 401(k) plans, that a large number of individuals will enroll in an employer-sponsored plan if participation is the default but will not enroll if non-participation is the default.[117] But this insight alone doesn't determine which default policymakers should choose. Since accepting the default outcome is a local optimum for the group of individuals in question, and since it is difficult to knowing which default will maximize their individual utilities in a global sense, there is no compelling reason not to choose the default that will have greater positive externalities (or fewer negative externalities) and thus benefit society as a whole. If greater individual retirement savings increases capital available for investment in the short term and minimizes the nursing home expenses of the destitute ultimately shouldered by the taxpayers through the Medicaid program in the long term,[118] the enrollment in a 401(k) plan might be justified as the default option for new employees under the theory of libertarian welfarism.

It bears noting that, in some cases, the social welfare impact of individual choices will be just as uncertain, or even more uncertain, than the individual utility consequences for the actors potentially subject to nudges. The category of libertarian welfarism will not always be immune for the indeterminacy critique. For example, if the benefits to the taxpayers of 401(k) enrollments in the form of fewer elderly making claims on the public fisc are counterbalanced by the cost of additional children claiming public resources (or suffering without them) as crucial income of poor parents is siphoned into retirement accounts, libertarian welfarism will fail to provide clear policy guidance to lawmakers. It many situations, however, the net valence of externalities created by individual behavior will be clear. For example, it seems implausible that a serious argument could be made that increased cadaveric organ donations somehow has a net negative effect on social welfare. In these

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[117] *See* note __, *supra*.

[118] In 1995, Medicare and Medicaid accounted paid $50 billion, or about 56 percent, of long term care expenditures for the elderly. The Congressional Budget Office has projected this figure will rise to $126 billion in 2020, or about 61 percent of total long term care expenditures for the elderly. *Projections of Expenditures for Long-Term Care Services for the Elderly*, Congressional Budget Office Memorandum, Congressional Budget Office, (1999).

situations, the libertarian welfarism framework can generate determinate policy proposals when libertarian paternalism cannot.

V. LIBERTARIAN WELFARISM VS. COERCIVE WELFARISM

Because a paternalist seeks to make individuals better off, as judged by their own standards, it is clear why policy makers ought to prefer libertarian paternalism to coercive paternalism, at least if it is possible to nudge errant individuals in the right direction. Assuming that the transaction costs associated with avoiding a government nudge are low, nudges strictly dominate mandates. Under a libertarian paternalism approach, a targeted individual who would be better off making a different choice than the one the state thinks is superior – either because the state is mistaken or because preferences are heterogeneous and the individual has a minority preference – can take evasive action.

The welfarist lawmaker, in contrast, seeks to maximize social welfare, even if this reduces the utility of the individuals targeted by a legal rule. For example, coercive criminal statutes that prohibit murder and mayhem can be justified on welfarist grounds: the harms to the victims and the negative third-party externalities far exceed (at least usually) the benefits to the perpetrators. No one seriously considers merely "nudging" would-be perpetrators to choose not to assault their neighbors, because those who choose to ignore or avoid the nudge would seriously reduce net social welfare, even if their individual utilities were increased. Why would policy makers concerned with social welfare ever prefer to libertarian welfarism to coercive welfarism? Why nudge, when you can mandate?

A. Freedom-of-Choice Enhances Welfare

There are three reasons why welfarists should prefer, at least in some situations, libertarian policy interventions to state coercion that requires individuals to engage in socially desirable behavior or create collective goods. First, freedom of choice is itself a value that is a constituent part of social welfare. Holding all else constant, members of a society in which freedom of action is widespread will enjoy more individual utility than members of a society that relies heavily on coercion, and thus there will be greater social welfare in the former

society. Where a nudge can cause most people to act consistently with the maximization of social welfare, the benefits of widespread freedom of action might outweigh the costs attributable to the actions of the few who are not affected by the nudge.

Even in cases in which a nudge will motivate only a small number of people to act in a way that promotes social welfare, a nudge will often be preferable to a mandate if the mandate would place severe restrictions on autonomy. Obesity probably could be reduced if the government required restaurants to serve only low calorie food items, but even most welfarists would find this cure worse than the disease because the positive social externalities would pale in comparison the significant reduction in the utility enjoyed by diners.

B. Costs of Coercion

Second, in many circumstances, using coercive regulation to promote social welfare will either be (a) politically infeasible or (b) so expensive that the costs of enforcement will substantially (or even entirely) offset the expected benefits. In the former case, the only available policy tools might be libertarian welfarist approaches; in the latter case, such approaches could provide the greatest net expected increase in welfare. A recycling mandate would increase recycling, but the government would have to pay garbage police to pick through the trash to ensure compliance. A deposit requirement would avoid having to inspect refuse, but there are significant administrative costs associated with operating such a program, and the size of the deposit might need to be very large to change behavior. Either of these might produce substantial political opposition.[119] Distributing recycling bins to each household is almost certainly a much cheaper alternative, and, could potentially produce enough voluntary compliance to maximize social welfare.

C. Encouraging Low-Cost Producers

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[119] *See* Carlson, *supra* note __, at 1298 (noting that "bottle bills remain politically contentious" and that none have been enacted by a state since the mid-1980s).

Third, nudging can help ensure that desirable externalities are produced by the people able to do so at the lowest possible private cost, which in turn helps to maximize social welfare. Consider, again the issue of cadaveric organ donation. If the government announce a policy of seizing all cadaveric organs, everyone would become a donor, regardless of the depth of his individual opposition. Although social welfare would increase immensely if the number of donors were to increase sharply, it is not necessary that every American become a donor. By instituting a presumed consent law, and thus shifting the default rule from no donation to donation, two groups of individuals who would not opt-in under the no donation default will be added to the donor pool: people with a mild inherent preference for donating that was swamped by the status quo bias under the no donation default, and people with a mild inherent preference not to donate but who will not opt out under a presumed consent law. The people with the highest disutility for becoming a cadaveric organ donor – those who have firm religious convictions, find the prospect particularly disgusting, or are deeply suspicious of the medical community – will opt out of doing so, overcoming the inertia that accompanies the status quo. Assuming that the number of people who opt out would be relatively low, as it is in European countries with presumed consent defaults, the social need for a large number of organs would be satisfied without unnecessarily imposing large personal costs on the individuals who find the practice most objectionable.

VI. CONCLUSION

Legal policy makers can use findings of empirical research from the field of behavioral decision making to fashion tools for shaping individual behavior without mandating it or providing direct economic incentives. This insight underlies the *libertarian* portion of "libertarian paternalism." But these tools are not useful only for paternalistic ends. The category of libertarian paternalism implies the complementary category of libertarian welfarism. And, in fact, libertarian welfarism will likely prove to be the more useful of the two categories for public policy, both because welfarism provides a sounder normative basis for government action (because it takes externalities into account), and because it will often be more clear which actions will generate the most

social welfare than which actions will generate the most private utility for a particular individual.

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