

# IP: BUSINESS ETHICS

## Ethics and Economics and Game Theory

### *Arrow's Responses*

How does Arrow answer arguments such as Friedman's? Well, Arrow argues five things:

1. The forces of competition are not always so strong, and firms may be able to exercise *market power*, in the limit as a monopolist.
2. Even if perfect competition exists, and no firm can exercise market power (facing a downwards-sloping demand curve), there is no guarantee that the market allocation of income and wealth will be *equitable*, even if the market is extremely *efficient* in transforming inputs into outputs.

3. **We may be unhappy and uncomfortable about an appeal to our selfish, self-centred natures — where is a rôle for other-centred *altruism*?**
4. **Further, market *externalities*, such as pollution and congestion, mean that firms and individuals may not be paying for all costs they impose on others.**
5. **And *information asymmetries* may lead to bad decisions and to deceit: the “lemon” new car, the new pharmaceutical drug.**

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## ***Means to achieve changed corporate behaviour?***

**Arrow goes on to suggest four ways to change corporate behaviour:**

- a. legal regulation, e.g., of polluting behaviour**
- b. taxes**
- c. common-law legal liability — firms can be sued**
- d. ethical codes**

**We shall examine these.**

## ***Reputation.***

**Further — and here is game theory — firms value their reputations — when interactions are repeated or when people talk.**

**Although Adam Smith, of the “invisible hand”, has been taken up by people who think of the market process as ethics-free, in fact Smith (author of *The Theory of Moral Sentiments* in 1759, before his 1776 *Wealth of Nations*) was very aware of the ethical content of markets.**

**Smith speaks of virtue as the “fine polishing” on the wheels of society, and vice as the “rust” on the wheels.**

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**In 1968 Ken Boulding's presidential address to the American Economics Association was on the theme *Economics as Moral Science*.**

**The 1974 Nobel laureate Friedrich von Hayek wrote about *The Origin and Effects of Our Morals: A Problem for Science*.**

**The 1998 Nobel laureate Amartya Sen wrote in *On Ethics and Economics* that value judgements are pervasive, that ethics doesn't subvert economics as a science, that ethics is part of economics as a science.**

## ***Game theory and the evolution of fairness***

**Is it rational to be ethical?**

**Would we really all be better off if we looked after Number One?**

**Plato, Kant, and John Stuart Mill — and most recently John Harsanyi, another Nobel laureate — have tried to show that there is more to life than selfishness.**

**Darwin's evolutionary biology was used by others (such as Herbert Spencer, who coined the phrase “survival of the fittest”) to argue that altruism was unnatural and weak.**

## **And recently ...**

**In the past twenty years, however, game-theoretic models have been used by Robert Axelrod and others to show that altruism can evolve even in the repeated Prisoner's Dilemma.**

**In fact, we are social animals and evolved in societies where cooperation conferred some fitness on our ancestors and those of other mammals.**

**There has recently been evidence of the concept of “fairness” among monkeys in the lab, which suggests hard-wiring via evolution in the brain.**

## Utilitarianism

**Includes two doctrines:**

- 1. The *right* action: actions are right if they maximise the good for the majority.  
(The greatest good for the greatest number.)**
- 2. The *good*: happiness/satisfaction is good.**



## Criticisms of utilitarianism:

1. What does “for the majority” mean?  
Who is referred to? everyone? a nation? a town? an ethnic group? the unborn? animals?
2. But “the end doesn’t justify the means” (Kant)
  - It’s possible to justify greater inequality of good, against fairness or equality or *redistributive justice*
  - or to punish the innocent for maximum gain, against *retributive justice*
  - or against duties of *truth-telling* or *promise-keeping*

## Rights?

### 3. What of *rights*?

If A injures B, for the good of the majority, but may violate B's rights.

### 4. A is on a bus party which is captured by bandits.

The (honourable) bandit chief promises to release A + the rest if A agrees to shoot any member of the party.

If A refuses, then the bandit chief will shoot all.

Should A shoot 1 → the rest set free?

Utilitarianism missing a link to *morality of the person*.

## Efficiency v. Equity

**Less efficiency,  
greater equality.**

*Smaller cake,  
more even slices.*

more equal

• **A**

**Greater efficiency,  
greater equality.**

*Larger cake,  
more even slices.*

• **B**

**Status Quo Ante**

**efficiency**

**Less efficiency,  
less equality.**

*Smaller cake,  
less even slices.*

**Greater efficiency,  
less equality.**

*Larger cake,  
less even slices.*

less equal

## ***Efficiency v. Equity or Fairness***

**(lexicographic ordering)**

## **Vilfredo Pareto (1848–1923) —**

**Proposed a limitation on utilitarianism:**

***The Pareto Improvement Criterion:***

**An action should be undertaken if it improves the welfare of at least one person, while making no-one worse off.**

**Consequences?**

## Confucian Ethics

**Kong Zi or Confucius (550–479 B.C.) has influenced over 2000 years of thought in China and beyond.**

**Master Kong developed the three principles of *Li*, *Jen*, and *Chun-Tzu*.**

**Li:** the ideal standards of conduct: religious, moral, and social

**Jen:** the virtues of goodness and benevolence; a recognition of value and concern for others

**The Silver Rule:**

**“Don’t do unto others what you would not like them to do to you.”**

**Li provides a structure for social interaction  
Jen makes it a moral system.**

## **Chun-Tzu**

**Chun-Tzu (or Junzi, ruler's son):**

**the true or virtuous gentleman or person  
he who lives by the highest ethical standards,  
and displays the five virtues:**

- 1. self-respect**
- 2. generosity**
- 3. sincerity**
- 4. persistence**
- 5. benevolence**

## Chun-Tzu

### Relationships:

as a son	loyal
as a father	just and kind
as a husband	righteous and just
as an official	loyal and faithful
as a friend	faithful and tactful

**Note: Confucius held that we are inherently good creatures.**

**Against Christianity: ? Original sin.**

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**see <http://www-chaos.umd.edu/history/ancient2.html> for discussion of his disciples Meng Zi and Xun Zi and the schools of Literati and Legalism and of yin-yang and of Mo Zi.**