



THE DIMENSION OF SOCIAL COST IN THE WORK OF K. W. KAPP

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ABSTRACT

*K.W. Kapp, from the 1950's, disputes the assumptions and targets of classical and neoclassical economic theory, attempting on the one hand to formulate new concepts relating to the presence of a cost that is created as an effect of the production process of a business, is not taken into consideration in the calculation of its financial data, and burdens society as a whole, and on the other hand to shed light on evidence and data that demonstrate the failure of classical economic theory to take this social cost into consideration. Kapp argues that the current system treats man as a tool, either for production or for consumption. Therefore, he considers it an urgent need to re-define the guidelines for social action, with the only main criterion being human needs, and not the requirements of the market and proposes an immediate reconsideration of the criteria for the planning of the production process. Karl William Kapp (1910-1976) engaged in a fundamental critique of economic theory, using the language and terminology of neo-classical economists¹. He disputes the arguments and the scientific basis of prevailing economic science. He considers Western knowledge as a whole to be partially factual, with its main feature being the constant introduction of a proposed a priori assumption. This hypothetical nature of its considerations regarding human nature and its environment brings about the result that new empirical evidence that may run counter to previous considerations has led repeatedly to extensive reconstructions of all systems of knowledge. In his work *The Social Costs of Private Enterprise*, Kapp engages in critique of the theory and practices of private business. The goal of his book is to demonstrate on the one hand the existence of a cost that is not taken into consideration in a business's expenses, but appears in the form of the degradation of the natural and social environment, and on the other hand, the failure of conventional economic theory to take this social cost into consideration.*

1. The Definition of the Concept of Social Cost and Its Importance

Based on neo-classical thought, beyond the creation of a physical and legal framework that will make the functioning of the competitive market possible and maintain it seamlessly, the state must refrain from economic activity. Most problems will be solved through growth in national income. In spite of all this, however, there are some social costs that need to be tackled and corrected with more positive measures: for example, the redistribution of income for the benefit of the very poor and the provision of goods and services such as public roads and parks, which no private individual can build on his or her own and where the principle of exclusion does not apply. What Kapp shows in the above, his major work, is that social costs constitute formal data of the system, appear rather frequently, are highly important, and are much more important than the state considers and recognizes them to be. He defines as the social cost any cost that appears because of business activity and places a burden on third parties or society to a large extent and therefore is not calculated in the action plan of the





business, which is based on the principle of maximizing profit without considering probable negative consequences. He analyzes, highlights, and enumerates these costs in detail in every chapter of his book. Concerning the natural environment, he examines the pollution and contamination of the atmosphere and water³, soil erosion, the destruction of wildlife and of ecological balance and the challenge of irreversible damage to non-renewable resources. Concerning the social environment, he examines the cost of people weakening due to occupational diseases, exposure to radiation, child labor, mental illness due to extensive unemployment, the cost of annihilating competition, excessive production and the pre-planned obsolescence of products, the promotion of sales, orienting research only towards profitable fields, the slowdown in the development of science due to parallel research, the overconcentration of the population in urban centers, and the sacrifice of welfare for the production process. Let it be noted that Kapp mentions that no effort had ever been made to trace and value social cost in sectors such as banking, insurance, and real estate. None of these costs is measurable in financial terms as a loss of income or as a cost for compensation or correction after the fact. Most of them, however, are spread over the entire community, so that it is not possible for one individual or a group of individuals to avoid them or measure their burden or demand compensation. Concerning the importance of defining the social cost, Kapp observes that the success of every environmental inspection program depends on the correct analysis of the way in which environmental costs are entered into the system, the sufficient allocation of responsibilities to those that bear them, as well as the effectiveness of the practices and institutional measures adopted to neutralize them, and finally, the sufficiency of the capital available.

2. The Critique of Assumptions in Neo-classical Theory

His book “The Social Costs of Private Enterprise”⁶ published in 1950 by Harvard University Press was followed by an article that he wrote in 1971, through which he replied directly to those who criticized his book from the standpoint of current economic theory.

As Kapp mentions,

“The main body of neoclassical value theory has continued to regard social losses as accidental and exceptional cases or as minor disturbances. Analysis of existing preventive regulation reveals that present restraints are still highly ineffective in minimising social losses”.

K.W. Kapp's criticism focuses on the following basic assumptions of neo-classical economic theory, and specifically, on its analysis in contemporary Welfare Economics⁸: that elements of the economy may be isolated from the whole of social evolution and be considered selfregulatory for the purposes of analysis, as well as that these elements contain inputs (resources, costs) and outputs (results, satisfaction) that can be measured in monetary terms on the market. That the choices of actors of economic activity (businesses, producers, and consumers) are rational and the market precisely reflects the satisfaction and opportunity costs of the specific uses of resources and that changes in demand and supply tend, due to the competition existing on the market, to move towards equilibrium, correcting any imbalances that may arise. That the achievement of external savings in individual businesses becomes achievable only through their merging with large businesses, and that the risk of monopolies appearing on the competitive market may be compensated by the reduction of barriers to international free competition among very large businesses. Finally, that every social cost beyond the cost fore the business may be corrected by imposing taxes on the actors who create the cost and providing compensation to the actors who undergo the cost, as well as with the legal application of individual claims for compensation, since welfare is measured only in terms of the satisfaction or displeasure of every individual.



3. Criticism of Kapp's Work

The main criticism received by Kapp's work was produced by Wilfred Beckerman. Beckerman describes Kapp's book *The Social Costs of Private Enterprise* (1950) as a pioneering work which was not duly appreciated when it was published "because it came ahead of the time when environmental issues became the fashion", but he considers the criticism and "the overall tone" of his essay "Environmental Disruption and Social Costs: A Challenge to Economics"¹⁰ (1970) excessive. Specifically, Beckerman considers that Kapp's goal is the revision of overall economic theory and he accuses him of lacking examples and engaging in obsolete and misleading use of the concept of social cost. It should be noted that Beckerman's critique focuses exclusively on the social costs that concern the natural environment. According to Beckerman's view, economists have developed new analytical tools and the logic of choice and optimization has reached such levels of generalization that they can be applied to apparently new problems that relate to environmental crisis and in parallel, it is possible to assess the decisions required for their elimination or control in financial terms. Thus, according to Beckerman, on the one hand, economists have obtained the capacity to handle problems that are difficult to solve with numerous cumulative heterogeneous variables by reducing them to monetary terms, and on the other hand, the principles of the economics of well-being are perfectly applicable to the tackling of the new environmental problems that we are facing. Kapp replies first of all to Beckerman's objections as follows:

"Beckerman believes that my book was not duly appreciated because it was written before the discussion of the disruption of the environment by economic activities became popular. I believe rather that what was not appreciated was the association of social costs and business enterprise and the confrontation of economic theory with my empirical data and observations -i.e., the great variety of losses borne by third persons and society as a whole¹¹."

He claims that his main position was and continues to be that the maximizing of the net income of micro-economic units will probably reduce the income (or the usefulness) of other economic units and of society as a whole and that the conventional measurements of the economy's performance are unsatisfactory and therefore misleading. As he specifically mentions:

"To my mind, traditional theoretical inquiry was neither guided nor supported by empirical observations and available data. I tried to show that microeconomic analysis ignored important relationships between the economy (wrongly viewed as a closed system) and the physical and social environment and that these intrinsic relationships gave rise to negative consequences of the economic process. It was and is my contention that the nature and scope of economic theory is too narrow. This restriction has affected economic theory at its foundation: i.e., at the stage of concept formation (e.g., costs and returns), in the choice of criteria of valuation and aggregation (in terms of money and exchange values) and hence in the delimitation of the scope of the inquiry¹²."

Regarding the comment by Beckerman that Kapp's goal is to start economic theory over from zero, he replies:

"It seems to me that Beckerman fails to see that my critique is not quite as novel as he implies and that in fact both my book and my article must be seen within the context of a body of critical analysis which has been advanced over the last decades. I shall deal with this point by outlining a whole pattern of reaction of an entrenched community of scholars against its critics. One reaction is to ignore them by a conspiracy of silence by all those who have "invested" in the established body of doctrine and thus may be said to have a "vested interest" in it, to use a favourite term of Veblen."



4. Conclusion: Kapp's Proposals

Kapp claims that the current system treats man either as a production tool or a consumption tool. Increased unemployment, the degrading of the working environment even in developed countries (absence of measures, health risks, tension, anxiety, accidents), the contamination of the natural environment, the aggressive promotion of sales, and the consumption of useless products constitute typical examples of social cost. Therefore, he considers it an urgent need to redefine the guidelines for social action with human needs as the sole main criterion, and consequently, to choose inputs that serve these needs and not the demands of the market. He proposes an immediate reconsideration of the criteria for the planning of the production process. He proposes change and control of the "input mixture" and the technical process for production. He uses the following eloquent example:

"If we want to avoid the destruction of plants by insects and pests, we can use insecticides and pesticides. We have done so in the past only to discover that the insects and disease carriers develop immunity and the increasing amounts of chemicals or their residues pollute our environment and tend to become serious health hazards to man. Instead of developing more and 'better' pesticides which, moreover, tend to attack not only pests but insects in general, plant geneticists and plant breeders are experimenting today with breeding plants with greater resistance to attacks by insects and pests. This type of control, by changing the nature of capital inputs, may be more economical and more effective in the long run than the use of chemicals, while at the same time avoiding the dangers of the pollution of the environment. Similarly, the control of air pollution by automobiles seems to me to be more economical and more certain by the design of new and more effective engines and/or by substitutes for gasoline than by indirect controls or better law enforcement."

In procedural terms, first of all, the following are considered indispensable: recognition of the systemic nature of the environmental problem and acceptance of the fact that environmental relations are of a radically different type from market relations. Consequently, the elaboration and acceptance of environmental goals require a collective or social choice with the direct participation and expression of the preferences of all the members of society, even those who are found outside the market and do not shape active demand. Finally, systematic studies of cost-effectiveness are required for alternative goals and plans, with the suitable application of rules and procedures. Essentially, the issue of introducing an increased level of politically shaped choices into the socio-economic process is being posed. To what extent the application of such a plan is feasible depends on institutional changes.

References

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- Kapp, K. W. (1975) *The social costs of private enterprise*, Schocken books, second printing 1975, p. 1 ff.
- Kapp, K. W (1978) "Environmental Disruption and Social Costs", *Kyklos*, 23, 1970, pp. 833-4.
- Kapp mentions the case of multiple parallel studies by state bodies and universities, with the prevalence of extreme isolation and secrecy, a lack of coordination, the absence of exchanges of information, and naturally, efforts taking up much more time and costs for a limited result. He cites cases mentioned by H. Langier, ("How Science Can Win the War," *Free World*, 1941, vol. No.1, p. 59) and J. D. Bernal (*The Social Function of Science*, (London, George Routledge and Sons, Ltd., 1939), ch. 3) in which army researchers worked for a long time to solve problems that had already been solved by their colleagues in the navy or the air force, or army and navy technicians were led to different solutions for the same problems and continued to apply the results of their research, without having proceeded to their comparative evaluation in order for the optimal choice to prevail.



- Kapp, K. W. (1978) The social costs of business enterprise, ανατύπωση 2000, ed.Spokesman (Nottingham), p. 248 ff
- Kapp wrote this book when he was a professor at Wesleyan University with the title The Social Costs of Private Enterprise (Harvard University Press 1950) and since then it has been translated into six different languages. In subsequent editions, starting from the second extensively revised edition in 1963, which was printed in India, and the revised and expanded edition in 1978, until its reprinting in 2000 by Spokesman Publishing (Nottingham), the title of the book is The Social Costs of Business Enterprise. It appears from the publisher's prologue that Kapp proceeded to this change of title because he wanted to take into consideration the same social costs where state companies in the Soviet Union and elsewhere are guided by similar principles of economic calculation.
- Included in the annex to the 1978 edition and the 2000 reprinting of the book The Social Costs of Business Enterprise. This article was originally presented by K.W. Kapp at the symposium "Political Economy of Environment: Problems of Method", which was held at the Maison des Sciences de l'Homme in Paris on July 5-8, 1971 and constituted his reply to Wilfred Beckerman's article "Environmental Policy and the Challenge to Economic Theory".
- Ibid.
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