

Adam Smith's Social Contract: The Proper Role of Individual Liberty and Government Intervention in 18th Century Society

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Introduction

What is the nature of the social contract that exists between business and society? Donaldson (1982) has begun exploratory work in this field, imagining a society prior to the advent of productive organizations in order to determine why corporations are desirable. The social contract method of inquiry serves three primary purposes: (1) it defines a moral ideal that is rationally acceptable to both parties, (2) it imposes obligations based on both parties' uncoerced consent to the contract, and (3) it establishes a justification for intervention when the contract is violated.¹

What were the original terms of the social contract that brought forth capitalism? A social contract between business and society can be developed through a textual analysis of Adam Smith's 18th century writings. Smith was a social reformer in the broad sense, not a social contract theorist in the narrow sense. However, when taken as a whole, Smith's *Theory of Moral Sentiments* [TMS] (1759/1976), *Wealth of Nations* [WN] (1776/1976) and *Lectures on Jurisprudence* [LJ] (1978) provide a foundation for determining a private enterprise social contract. These three works, concerned with ethics, economics and justice, encompass the general terms of the agreement between business and society. Smith's social contract, a replacement of the social contract between the mercantilists and government, establishes what activities will be permitted in the economic arena, justifications

for these activities, and enforcement policies when the terms of the contract are violated. In this sense, Smith serves as a broker between the business community (representing their own interests) and the government (representing society's interests).

The original intentions of Smith's social contract will be explored in this paper. In Part I, Smith's reputation of the social contract that was in effect during the 18th century will be presented. In Part II, Smith's conception of the moral ideal will be extensively interpreted. In Part III, the terms of the social contract will be speculated upon. In Part IV, the most contentious aspects of Smith's social contract, intervention by government and the justice system, will be explored and defended.

Part I: Smith in His Context

From 1751 to 1763, Smith lectured students at the University of Glasgow in the areas of moral philosophy, theology, ethics, jurisprudence and political economy. These lectures served as the foundation of his two primary scholastic works, TMS and WN. Two sets of student notes from Smith's jurisprudence class have been compiled and published in LJ. These three works highlight the nature of Smith's scholarly project, an integration of ethics, economics and justice. Smith's undertaking should be seen as a reaction to the problems of his day and age.

At the time of Smith's philosophizing, living conditions in Scotland were harsh. The country was primarily an agricultural society at the mercy of weather conditions.² During the 1600s and 1700s the Scots experienced a crop failure every several years. The famine of 1696-1699, caused by late frosts and summer droughts, resulted in the starvation of 5 to 10 percent of the Scottish population. Starvation affected both peasants and craftsmen as they were relegated to eating boiled deer horns and the bark of trees. When weather conditions ruined a harvest the price of available grain rose substantially. Only the wealthy could afford the higher prices. During these periods discretionary income was limited and the craftsmen had no buyers for their products. The typical Scottish family lived in a one room home 20 feet by 15 feet, paying for their rent with their services. Travelers

writing about their visits to these homes often commented on the dirtiness and the lack of privacy for the typical family of five. Life expectancy is believed to have been 28 years.

Some hope for improving the standard of living rose with the merger of the Scottish and English government in 1707. With representation in the English parliament, the Scots had hope that more charity could be funneled their way during hard times. Nonetheless, there are reports of starvation in Scotland due to the ruined harvest of 1739-1740. Meanwhile, industry was beginning to form in both Scotland and England, particularly in cities such as Glasgow, Edinburgh and London. In both *WN* and *LJ*, Smith refers to a pin factory already utilizing the division of labor.

It is in these surroundings that Smith began philosophizing about morality, jurisprudence and economics. Though Great Britain had a majestic empire that expanded the globe, Smith remarked that "no society can be flourishing and happy, of which the greater part of the members are poor and miserable."³ In searching for a culprit for the destitution, Smith did not blame the moral sentiments of individuals as others had done. The mercantilists blamed the poor for their own misfortunes. The utopians blamed the selfishness of the wealthy for the misfortunes of the poor. Smith, on the other hand, believed that the culprit was the economic system itself. He recommended that the government abandon its mercantilist policy of sanctioning monopolies, putting quotas on imports, regulating tradesmen and restricting other aspects of economic behavior. Smith believed that these policies were detrimental to the wealth of a nation and the welfare of the general populace. He lashed out at the "wretched spirit of monopoly" and suggested that both product markets and labor markets become competitive. According to Smith, monopoly power led to increased poverty as large profits were made at the expense of worker wages. Prices were raised and labor was abused.⁴ Monopoly suppliers charged artificially high prices to manufacturers. Monopoly manufacturers, in turn, charged excessively high prices for their commodities. The mercantile system had provided exclusive privileges for butchers, bakers, brewers, distillers and tanners. Lack of competition led to high prices and low quality. Competition in the product market would lower prices, and make producers more

sensitive to the needs of the consumer. Competition in the labor market would enable individuals to choose more freely what occupations they wanted to enter and raise wages.

Yet, Smith the social reformer could not merely recommend that monopolies be disbanded in favor of a market-oriented system. As a professor of moral philosophy, Smith understood the necessity for moral justification of the individual pursuit of self-interest, and that the new social contract he would eventually construct could not be contrary to morality or human nature. This is the chore that Smith undertakes in the work that brought him fame in his own lifetime, *TMS*.⁵

Part II: Smith's Ethical Theory

The Theory of Moral Sentiments

Smith's ethical treatise, the often neglected *TMS*, was published in 1759, seventeen years prior to *WN*. Smith, who held the chair of Moral Philosophy at the University of Glasgow at the time, was embroiled in the 18th Century debate on the place of self-interest and benevolence in moral theory. His ethical analysis is a reaction to two developing schools of thought, Bernard de Mandeville's inability to account for any virtues in social interactions and the social utopians' apparent desire to restructure social institutions in a manner that would force people to behave benevolently. Though 18th century English society was quite some distance from moral perfection, Smith argued that there were moral qualities among the citizenry. In the opening sentence of *TMS*, Smith claims that "how selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the future of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it."⁶

Smith performs this task by integrating the thought of Plato, Aristotle, the Stoics, the Platonists, Epicurus, Hutcheson, Mandeville, Hobbes and Hume. Based on this framework, Smith describes the ethical component of civil society. He is interested in the ethical component of a society that is an acceptable approximation of

perfection, a society not fixed in time but which is incrementally evolving to an improved state.⁷ Smith sets on his agenda four questions to explore: (1) What is the nature of virtue? (2) What is the impact of motives and consequences on moral judgment? (3) How are moral judgments formed? and (4) Why are moral judgments acted upon? Smith's methodology for deriving answers to these questions is a descriptive account of moral psychology. He explores the concept of morality based on everyday existence in a nonperfect world.

The nature of virtue

Smith claims that all philosophical accounts of virtue are reducible to four theories: propriety, prudence, benevolence and licentiousness. He believes the first three accounts are plausible, but, in and of themselves, too inclusive. Each is a condition for virtue, but none fully represents virtue on its own merit. He agrees with the Stoics that virtue consists of propriety, with Epicurus that virtue consists of prudence, and with the Platonists and Francis Hutcheson that virtue consists of benevolence. However, according to Smith, none of these accounts, by itself, provides a sufficient understanding of virtue. Propriety fails to distinguish the different degrees of honorable and shameful behavior. Prudence misrepresents the philosophical concepts of temperance, fortitude and justice because they cannot be fully explained based on utility value. Hutcheson's account of benevolence disregards the importance of prudence and propriety. Smith dismisses Bernard de Mandeville's licentious system as sophistry on the grounds that to desire virtue for its own sake is indeed a virtue, not vanity, if one's actions are worthy of praise.⁸

Smith concludes that there exists a plurality of virtues and he determines the significance of each virtue based on a descriptive analysis of approbation. Approbation is an appealing operational mechanism because, according to Smith, it is an outward manifestation of moral sentiments.⁹ People praise others in order to express their gratitude, as a means of rewarding someone for their behavior. People blame others in order to express their resentment, as a means of punishing someone for their behavior.¹⁰ An analysis based on approbation would help to reveal what people believe to be meritor-

ious behavior. Those who behave benevolently are highly praised by others because such behavior is not common in society. Failure to behave benevolently elicits little criticism. Those who behave justly are highly praised because such behavior maintains societal peace. Failure to behave in a just manner often elicits scorn from others. Those who behave in a self-interested manner are rarely praised, except in childhood, because such behavior is a common attribute. According to Smith, each person "naturally prefers himself to all mankind" and "is much more deeply interested in whatever concerns himself, than in what concerns any other man."¹¹ However, failure to behave in a self-interested manner--as in the case of not caring for one's own health or family--will result in scorn from others. In a very nonrigorous manner Smith labels benevolence as the most noble virtue, justice as the most essential virtue and self-interest as the most basic virtue.

<i>Virtue</i>	<i>Presence of Virtue</i>	<i>Lack of Virtue</i>	<i>Label</i>
Benevolence	High Praise	-----	Noble
Justice	High Praise	Blame	Essential
Self-interest	-----	High blame	Basic

According to Smith, justice serves as an essential virtue in civil society. He refers to it as the edifice and the foundation that holds society together. Justice maintains a special place in Smith's scheme because it is the only virtue that "may be extorted by force."¹² Society should not force people to be benevolent or self-interested, but it should punish people for behaving unjustly. Human beings have a strict obligation to act according to the dictates of justice because "the violation of justice is injury: it does real and positive hurt to some particular persons."¹³ Smith maintains that "there can be no proper motive for hurting our neighbor" and that "the prevalence of injustice must utterly destroy (society)."¹⁴

The Impact of Motives and Consequences on Moral Judgment

In *TMS*, Smith provides a brief sketch of his praxeology by differentiating three aspects of an action sequence: (1) the motive that

generated the act, (2) the act itself, and (3) the consequences of the act.¹⁵ Smith notes that when a person is praised or blamed for an action, that person is really being praised or blamed based on the motives that generated the action or the consequences that resulted from the action, not the act itself. As an example Smith discusses praise or blame associated with firing a gun. The act of firing a gun is not the source of approbation. Instead, approbation is generated based on the motive behind firing the gun (did one intend to kill somebody or did one intend to shoot a can sitting on a fence) and the consequence resulting from the gun being fired (was someone killed, was the can hit). Praise and blame are not associated with the actual pulling of the trigger.

But, what is the ultimate source of praise and blame, the motive or the consequence? Smith distinguishes himself from the utopians by focusing on a descriptive account of the event, not a prescriptive account. In a perfect society, one intends, acts and then the consequences arise. Under these conditions, the praise and blame should be ultimately attributed to motives and intentions because they causally generated the consequences.¹⁶ However, in the ambiguous world of everyday affairs, there are many deviant causal chains. A harmful intention may yield a beneficial consequence, or a beneficial intention may yield a harmful consequence. In such an impure laboratory as that of society, Smith argues, consequences are held to be more prominent than motives. Criminals who intend to kill someone are not punished severely unless their intentions are transformed into acts and the resulting intended consequence. In the case of intent to kill, the criminal may be punished, but not as severely as if the consequence had arisen. Smith notes that "the humanity of a civilized people disposes them to either dispense with, or to mitigate punishments wherever their natural indignation is not goaded on by the consequences of the crime."¹⁷

Smith further examines this phenomenon with an example of a man tossing a rock over a wall into a public square. If no harmful consequence is generated, the negligent man is only scorned. However, if a passerby is killed by the thrown rock, the negligent man is treated as though he had intended the death and is severely punished. Smith concludes that "that necessary rule of justice,

therefore, that men in this life are liable to punishment for their actions only, not for their designs and intentions, is founded upon this salutary and useful irregularity in human sentiments concerning merit or demerit, which at first sight appears so absurd and unaccountable."¹⁸ According to Smith, this "irregularity of sentiments" is present in normal human affairs. The range of Smith's approbation analysis of motives and consequences appears below.

Motivation	Actual Consequence	Approbation
Outer-directed (benefit general welfare)	Benefits general welfare	High Praise
Inner-directed (benefit self)	Benefits general welfare	Neutral
Outer-directed (benefit general welfare)	Harms general welfare	Blame
Inner-directed (benefit self)	Harms general welfare	High Blame

The Impartial Spectator and Moral Judgments

Will the habituation of the most basic virtue, self-interest, result in the diminishing of all the other virtues? For example, in the economic sector, will reliance upon people's self-interested motives foster greed and inhibit benevolent motives? These questions bring us full circle to Smith's opening inquiry in TMS. Smith argues that although people are basically self-interested individuals, they temper their self-interests when they form moral judgments. According to Smith, people are not slaves to their own self-interested passions. They typically form moral judgments not according to a Hobbesian notion of self-love, but based on Hume's account of sympathy. One possesses the ability to enter into another person's point of view, one can experience the joys and griefs of others. Smith maintains that one does this by imagining how one would feel if one were the other person; one sets aside one's own self-preferences and enters into the other person's experiences.

Smith follows Hume's analysis of sympathy up to a certain point and then departs. He disagrees with Hume on three counts: (1) not

all sympathy is agreeable or praiseworthy, (2) not all moral judgments arise from sympathy, and (3) the value of sympathy rests beyond a utilitarian analysis. Sympathy, for Smith, is a "correspondence of sentiments."¹⁹ This correspondence is, implicitly, a sign of approval for another person's action, a moral judgment. Smith notes, however, that one possesses the ability to sympathize with *any* sentiment; sometimes people sympathize with the initiator of a premeditated tragedy rather than with the victim. These sympathies are not praiseworthy. Smith also argues that sympathy cannot account for all moral judgments and accepts, in part, the philosophical analysis of Ralph Cudworth, which traces moral judgments to the notion of reason. In regard to utility value, Smith argues that one does not act morally merely to receive another's praise; one acts morally to be *worthy* of such praise. Thus morality has an intrinsic, as well as an instrumental or utilitarian, value. One desires to do what is approved of and one also desires to do "what ought to be approved of; or of being what he himself approves of in other men."²⁰

According to Smith, it is possible to have a distorted notion of sympathy, or to have a conflict of sympathies. A person may have a correspondence of sentiments with a criminal, praising the harm which occurred to an innocent victim, or a person's sentiments may correspond with both those of the criminal and the victim. Smith distinguishes between two components of sympathy, the nature of the event that gave rise to an agent's sentiments and the pleasure which the agent feels when his or her sentiments coincide with those of another person. The second component of sympathy is always agreeable, but the first is not.²¹

How then are moral judgments formulated in order to differentiate between proper and improper sympathies? Smith utilizes the notion of an *impartial spectator* to explain this phenomenon. Though Smith does not make these distinctions explicitly, he accounts for at least five types of impartial spectators: (1) our conscience; (2) an imagined moral agent observing our actions and motives; (3) an imagined group of moral agents observing us; (4) communal law; and (5) God.²² Smith explains that the correct interpretation of morality is derived from the interrelationships among these various types of impartial spectators. These spectators relate to one another, through their

discourse an agreement is reached as to the correct moral act. Moral ambiguity occurs when these spectators are in conflict with one another. When they do not correspond--if disagreement exists between any of these various types of spectators--moral behavior becomes more difficult to assess. Smith argues, however, that the different types of spectators influence one another--i.e., our conscience is influenced by communal law and vice versa; thus, moral ambiguity does not arise very often. This is not to say that the justice system is always correct; matters of justice stimulate lively debates and are influenced by the moral sentiments of the citizenry.

Smith has accounted for how moral judgments are formulated, but why do people act according to moral judgments? Why do people act based on the perspective of an impartial spectator? Why not act on the more basic motive of self-interest? Smith provides at least five reasons why people temper their self-interests and act according to the moral judgments of the impartial spectator: (1) an innate desire to please others, (2) an intrinsic desire to be worthy of praise, (3) a desire for peace of mind, (4) habituation from childhood, and (5) recognition of the central role of justice in society.²³

Smith's trump card is the last reason. It would not be difficult to create counterexamples, based upon the first four reasons, to show how an impartial spectator could encourage an act which many other people in society would consider to be immoral. For example, individuals who are habituated in a criminal environment could justify committing crimes because it would please their friends, gain them praise, provide them with peace of mind and would be a natural outgrowth of their habituation. Smith, however, escapes this problem by distinguishing between civil and barbaric societies, with a necessary condition of civil society being a fair system of justice. He argues that society "cannot subsist unless the laws of justice are tolerably observed, as no social intercourse can take place among men who do not generally abstain from injuring one another."²⁴

Smith's ethical analysis is summarized below through twelve descriptive premises. He believes there is a multidimensional universe of virtues (premises i-iv) and that self-interest maintains a subservient role in the formation of moral judgments (premises v-vii). In some circumstances, pursuit of self-interest may generate benevolent

consequences, but due to unrestrained passion, self-interested behavior may generate harmful consequences (premises viii-ix). In those instances when harms are generated, the justice system is appealed to for resolving the case (premises x-xi). As such, consequences take priority over motives in the formation of approbation (premise xii).

Descriptive Premises

- (i) There exists a multi-dimensional universe of virtues. These include self-interest, justice and benevolence.
- (ii) Self-interest is the most basic virtue. People receive no praise for acting based on their self-interests, and are blamed when they fail to tend to their own self-interests.
- (iii) Benevolence is the most noble virtue. People receive high praise for acting benevolently, and no blame when they fail to act benevolently.
- (iv) Justice is the most essential virtue. People receive high praise for acting justly, and are blamed when they act unjustly.
- (v) Though predominantly self-interested, people form moral judgements in an outer-directed manner. Moral judgements are derived from the perspective of an impartial spectator.
- (vi) The view of the impartial spectator is an amalgam consisting of conscience, an imagined moral agent observing our actions and motives, an imagined group of moral agents observing us, communal law, and religious beliefs.
- (vii) Three mechanisms that restrain self-interested pursuits in social situations are reason, the impartial spectator, and the justice system.
- (viii) In some instances, pursuit of self-interest generates benevolent consequences; in some instances it does not.

- (ix) People are motivated by their passions.
- (x) Harm is a socially agreed upon, agent-centered restriction.
- (xi) The justice system, though imperfect, is a socially agreed upon institution that resolves cases involving harms.
- (xii) Though both motivation and consequences are important concerns, people are held more accountable for the consequences of their action than for the motivation behind their action.

Part III: The Social Contract

In Part I, reasons were provided as to why Smith saw the need to cancel the social contract established by the mercantilists. In Part II, an in-depth analysis was offered, establishing Smith's conception of the moral ideal, based on descriptive assumptions of human actions. In this section, the terms of Smith's social contract, which build on the descriptive premises, will be presented. The social contract establishes obligations on the part of business and government. Below are the terms of Smith's social contract.

The Social Contract

- (i) Liberty to pursue one's own economic self-interests should be permitted as long as there is a corresponding (though it could be unintentional) improvement in social welfare.
- (ii) If liberty to pursue one's own economic self-interests does not improve the social welfare, then government intervention is justified.
- (iii) If liberty to pursue one's own economic self-interests improves the social welfare, but harms are also generated, then intervention by either the government or the justice system is justified.

The first provision of the social contract establishes the right of individuals to pursue their own economic self-interests and government's duty not to intervene in these pursuits. The second and third provisions of the social contract establish the circumstances under which government and/or the justice system has an obligation, on behalf of the citizenry, to intervene in economic activities. When defenders of the private enterprise system pay homage to Smith, they usually pay homage exclusively to a water-downed version of the first provision. When critics of the private enterprise system castigate Smith, they are usually contesting the first provision and are ignorant of the second and third provisions. Only a small handful of liberal critics, such as Heilbroner (1984), have taken notice of the second and third provisions in Smith's analysis.

The first provision is supported by the writings of Smith's most widely read work, *WN*. In *WN*, Smith documents the many instances where individual pursuit of economic self-interest improves the social welfare. Improving the social welfare may not have been the intention of the economic actors, yet due to a variety of factors there were corresponding social improvements. In the most concise explanation of Smith's theory of natural liberty, Smith argues that "every man, as long as he does not violate the laws of justice, is left perfectly free to pursue his own interest, his own way, and to bring both his industry and capital into competition with those of any man or order of men."²⁵ I will not argue this well-known aspect of Smith's social contract, except to note that even in this instance, Smith's "hands-off" approach assigns government the duty to monitor the social welfare improvements.

The more contestable aspects of this social contract pertain to the second and third provisions. Do these provisions faithfully represent Smith's original intentions? If I am to argue that the social contract does indeed describe Smith's economic recommendations, I am left with two chores: (1) demonstrating that Smith did call for government intervention in some instances and (2) demonstrating that Smith had developed a theory of individual rights that he believed guided the justice system.

Part IV: The Intervention Provisions

Smith and Government Intervention

Smith's most overarching call for government intervention in human affairs is established through the formation of laws monitored by the justice system. In *WN*, Smith assigns government three intervention functions: (1) national defense, (2) administration of justice, and (3) maintenance of certain public works.²⁶ All three situations are instances where the social welfare is not benefited by individual pursuit of self-interests.

First, nations must maintain a standing army as a prevention against hostile invasions. It is inefficient for each family to fend for itself. The ad-hoc formation of militias, which typically lack adequate training, is an inefficient method of defending a nation.²⁷ As such, the government is responsible for maintaining a well-trained standing army.

Second, a system of justice is maintained by government since it too cannot be left to the pursuits of individual liberty. Anarchy would arise if each citizen took it upon himself to maintain justice. As such, the justice system is centralized under government. Smith maintains that the justice system should be financed by government, yet be independent of government. Government financing is necessary to prevent the bribery of judicial officials by the wealthy, yet the judicial system must be independent of government in order to prevent it from being corrupted by politicians seeking to use the system for their own gain. Smith viewed the subject area of police as a subset of the justice system. In *WN*, Smith concludes his talk on justice by noting that "upon the impartial administration of justice depends the liberty of every individual, the sense which he has of his own security."²⁸

Third, certain public works must be maintained by government because they are useful for every citizen yet do not appear to be profitable for any one individual, or group of individuals, to undertake.²⁹ Smith has in mind roads and bridges, communication networks, public education and religious instruction. All these are beneficial to local societies, thus funds should be provided by local

governments. Some of the costs for these public goods could be offset by a user's fee where appropriate.³⁰

Smith's Theory of Justice

What did Smith mean by a system of justice? In *WN*, Smith argues that a respectable system of justice is essential for the maintenance of a commercial society. Simply reading *WN* provides a distorted picture of Smith's theory of justice. In describing essential aspects of a justice system for a commercial society, Smith emphasizes particular rights that merchants and manufacturers would be interested in, namely, property rights, contract rights and rights associated with collecting debts.³¹ But this is a highly skewed presentation of rights in favor of the owners of production. In the final publication of *TMS* during his lifetime, Smith apologizes for not having finished his entire project. In *TMS*, Smith had developed an ethical theory. In *WN*, he had developed an economic theory. But, he never completed his theory of justice, thus leaving a gap which has been neglected in most scholastic undertakings of Smith's theory. Nonetheless, there is substantial evidence for Smith's theory of justice found in two sets of lecture notes taken by students in the Jurisprudence classes he taught at the University of Glasgow. Though an uncompleted project, these lecture notes provide substantial information on Smith's views of the justice system, which are consistent with comments that appear in *TMS* and *WN*.

Jurisprudence scholars have distinguished two essential questions: (1) What is law? and (2) What does the law say? The former is concerned with the source of law and the latter with the content of law. Smith developed his theory of justice along these two lines of inquiry. An in-depth explanation of Smith's answers to these questions is necessary to firmly establish the authority Smith assigns the justice system in monitoring business activity and enforcing the social contract.

Smith traces the evolution of civil society through four ages of history: hunters, shepherds, agriculture and commerce.³² According to this evolutionary scheme, which is a description of history and not deterministic, the judicial system was established by government as a means of settling disputes. In the age of hunters, the primary disputes

focused on issues of going to war or maintaining peace. There was no judicial body. Smith describes this age as that of a communal society where no one person had authority to legislate behavior for the entire tribe.³³ Individuals took justice into their own hands when resentment arose due to an injustice committed against them; on occasions, a court might be formed, but only on a temporary basis. The court, as well as the society, was led by a chief, an individual possessing some extraordinary ability--usually the best warrior--that commanded the respect of others.

It was not until the formation of a shepherd society that a set of laws emanating from a legitimized government was established, and this was due to an inequality of property. During this age, property claims were made which often resulted in disputes. Certain individuals would accumulate larger flocks and herds, a product necessary for each person's survival. As a result, permanent laws and regulations were established to protect their property and a system of punishment was devised for infringement of these property rights. Smith notes that:³⁴

Laws and government may be considered in this and indeed in every case as a combination of the rich to oppress the poor, and preserve to themselves the inequality of the goods which would otherwise be soon destroyed by the attacks of the poor, who if not hindered by the government would soon reduce the others to an equality with themselves by open violence. The government and laws hinder the poor from ever acquiring the wealth by violence which they would otherwise exert on the rich; they tell them they must either continue poor or acquire wealth in the same manner as they have done.

Besides property rights, concerns of law in the age of the shepherd pertained to treachery and cowardice since the desertion of one person at a time of war could ruin a small community. During this age, Smith notes, theft and robbery had pecuniary fines while cowardice or treachery were punishable by death. As property was passed from one generation to the next, the role of chief or king

became hereditary, the two distinguishing characteristics of the chief being superior wealth and family descent. The judicial system was transformed from that of a landowner intervening in disputes as an arbitrator and issuer of punishments for particular crimes, to the establishment of a judicial body fulfilling this function through written and formal laws binding on all members of the community.³⁵

The third age, agriculture, began with the collapse of the Roman Empire and emerged as feudalism. Following the collapse of the Roman Empire, the northern tribes divided the land. The leader or king would divide the land among the tribe's lords and nobles, thus shifting the determination of wealth from one of cattle ownership to one of land ownership. Since these lords could not maintain control over those whom they employed as tenants with the threat of their own standing army, the king had to give them the power to make laws in order to maintain peace. As conflicts eventually arose between the lord and king, an independent supreme court was established. Those who sat on the court were chosen by the king and thus represented his interests. The rulings were binding on everyone within the king's domain. This supreme court, as well as lower courts established by the lords, established a judicial system of trial by one's own peers. Over time, these courts became pawns in the hands of the powerful king or lord who ruled over them. It is necessary to note that through these evolutionary ages, the number of those governed by a set of laws grew dramatically. In the age of hunters, those governed by any set of rules numbered around 150. In the age of shepherds, the subjects numbered 1,000. In the age of agriculture one lord now governed 6,000.³⁶

Eventually, the power previously granted to the lords was undermined by the king. Improvements in agriculture and the arts greatly increased the king's wealth and thus came the absolute power of the monarch. With the collapse of the power of the lords, more liberty was granted to those whom they had governed. During this period of luxury for the king, the king's army had weakened; it soon became necessary to institute a parliament in order for the king to maintain control. The king depended upon the parliament to establish laws and levy taxes. This parliament then began to establish power independent of the king. In order to ensure its own power, parlia-

ment had to gather the support of those whom it governed, a process which resulted in more democratic forms of government. To ensure order in society, parliament established an independent system of justice whereby the judges were appointed for life and had no dependence upon political officials, particularly the monarch. It is due to this newly found emphasis on individual liberty that a commercial society began to develop.³⁷

Based upon this interpretation of judicial development, Smith discusses individual rights. The judicial system is responsible for establishing precise and accurate laws protecting certain rights that are known to the populace and binding upon them.³⁸ People initially view these laws as a restraint. Soon thereafter, however, people interpret the laws as a source of individual security and a guarantee of individual liberty. Smith argues that "a judge . . . is the source of our liberty, our independence, and our security."³⁹ With the emergence of the age of commerce, where people independently enter into exchanges in greater frequency, there is a call for even more laws.

In *LJA*, Smith distinguishes between natural rights and acquired rights. Natural rights are those rights granted to all human beings regardless of place or time. Acquired rights are those rights pertaining to unique situations that have been acquired over time. According to Smith, natural rights are rights an individual has against an attack on personhood, such as "killing, maiming, beating, or mutilating our body, or restraining our liberty, as by wrongous imprisonment, or by hurting our reputation and good name."⁴⁰ Acquired rights are those rights one has as a property owner, a member of a family (i.e. marriage laws, divorce laws) and as a citizen.⁴¹

Winch (1983) has argued that "Smith regarded rules of justice in some form or other as the essential prerequisite for any type of social existence."⁴² As such, Smith's notion of justice extends far beyond property rights and contract rights. Two areas of justice worth noting are: (1) natural rights against physical harm and invasion of individual liberty, and (2) acquired rights pertaining to the relationship between a master and a servant. In regards to natural rights, offenses to one's physical well-being include homicide,

assault, battery and maiming; offenses to the right of liberty include wrongful imprisonment, coerced obligations and rape.⁴³

Smith's views on acquired rights of slaves is helpful in understanding what he expected from the judicial system and government in preventing labor abuses. According to Smith, no master has a right to enslave a servant. In *TMS* Smith called slavery "the vilest of all states."⁴⁴ In *WN*, he refers to slavery as an "unfortunate law" and argues that "common humanity" disposes the government to intervene on behalf of the slave.⁴⁵ Under conditions of slavery the master typically revokes the slave's right to life, liberty and property.⁴⁶ Smith sees slavery as a historical problem that was eradicated in Europe due to the combined self-interests of both the king and the church against the lords. The slaves had been the property of the lords and the king believed it was in his self-interest to liberate the slaves in order to remove the power base of the lords. The church believed it was in its self-interest to end slavery because many of the slaves were Christian; their liberation would give the church greater power.⁴⁷ Smith argued that the presence of slavery in a republican form of government would make it particularly difficult to abolish the practice since those having political power are the slave-owners themselves.⁴⁸ Smith notes that a form of slavery still existed in Scotland and Wales in the coal and salt mine industries. Besides being revolting to an impartial spectator, slavery, Smith argues, cannot even be defended on utility grounds because free men are better workers than slaves. Smith argues that the master-slave relation developed out of the desire of the well-to-do to dominate, rather than bargain with, the less fortunate.⁴⁹

But aren't the poor, who earn a pitiful wage, in a similar position? Smith discusses this problem in *LJA* from a historical perspective. He notes that there is a "natural inequality of wealth," which is a function of one's ability, capacity and inheritance.⁵⁰ He then argues that in civilized societies the poor do indeed maintain the rich. The rich and opulent hardly do any labor and they are served by the clerks who do their business, artisans who supply their commodities, and the poor laborer who "bears on his shoulders the whole of mankind."⁵¹ Nonetheless, Smith claims, the poor in civilized countries exhibit a better quality of life than the savage in a more

egalitarian community.⁵² Smith also argues that by breaking the stranglehold mercantilism has on society, the lot of the poor will improve. Through division of labor they will learn a skill and earn higher wages. It is at this point in the lecture notes that Smith begins to introduce his economic policies and his belief that government should not regulate wages, prices of commodities or the production of commodities.

Smith clearly overestimated the ability, or willingness, of government and the justice system to intervene when harms were incurred. Horror stories abound as to the horrendous working conditions in both Scotland and England during the 1800s. Competition for jobs was high and wages low. Children and women were put to work in the coal mines and textile industry out of economic necessity, working 11 to 13 hour days, or more, 6 days a week. Fortunes were made in smuggling, piracy and catching and selling slaves. Of the 74,000 slaves transported from Africa to America in 1790, 38,000 were shipped by the British.⁵³ In Clyde, Scotland, a union of Scottish weavers appealed to Parliament in 1811-1812 for just wages.⁵⁴ Though turned down by parliament, they eventually obtained judicial approval for better wages; nonetheless, the manufacturers resisted this collaboration and had striking weavers imprisoned. It wasn't until 1833 that a law was passed that forbade the employment of children under nine years of age and restricted the working hours for children under 13 to eight hours a day.

Implication of the Social Contract's Original Intent

As noted earlier, the social contract defines a moral ideal that is rationally acceptable to both parties of the contract, imposes obligations on both parties based on their uncoerced consent to the contract, and establishes justification for intervention. Smith never classified himself as a social contract theorist and he was skeptical of philosophical speculation on voluntary agreements made in a hypothetical original society. Nonetheless, Smith's sweeping analysis of moral philosophy, economics and jurisprudence is a revised social contract, not from the point of view of a hypothetical society but

from the point of view of 18th century English society. Social contract theory has a long reformist history which Smith fits into.

Why go through the pangs of delving into Smith's often unexplored and extremely dense moral and social theory in order to construct Smith's social contract? In the American legal system, much emphasis is placed on the original intent of the Constitution and its interpretive message for modern dilemmas. Smith's social contract deserves similar respect, at least as a starting point for debate. By accepting the economic system that Smith systematized, there is an implicit acceptance of the social contract Smith brokered between the business community and government.

In many modern economic, social and political debates, appeals are often made to the provisions of the social contract, though not in a systematic manner. Respect for the moral ideals stated in the first provision has been consistently appealed to in the rhetoric of many private enterprise defenders. The second provision has been appealed to by both the private enterprise defenders and private enterprise critics. The defenders have requested government intervention in the form of subsidies in those instances when, from their point of view, the market system is inadequate--such as in requests for tax abatements to encourage companies to do business in enterprise zones, or in requesting protection from unfair foreign competition. Likewise, critics have appealed to government intervention to restrain banks from red-lining and to argue for plant closing legislation. In either case, whether the pursuit of economic self-interests will or will not improve social welfare is primarily an empirical question. The issue of which factors should be considered in this calculation, however, is still open to debate.

The third provision has been the focus of attention in much of the corporate social responsibility and business ethics literature.⁵⁵ What are the harms generated by business transactions? Why do companies generate these harms? How do they justify these harms? Company transactions have an impact, whether direct or indirect, on a wide range of moral agents, including its employees, suppliers, consumers, and the community-at-large. What harms incurred by which moral agents are absolutely impermissible? Assuming that government or

the justice system do intervene, what are proper and effective remedies?

It is worthwhile to note that Smith foresaw two micro-economic problems that still remain unsolved: wages and worker alienation. Smith had recognized that the self-interest of business owners would drive wages very low since they had an unfair bargaining position--the ability to "hold out much longer."⁵⁶ Smith's response to the wage problem was an appeal to the owners' moral sentiments not to do so. He noted "that men in general should work better when they are ill fed than when they are well fed, when they are disheartened than when they are in good spirits, when they are frequently sick than when they are generally in good health, seems not very probable"⁵⁷ Smith was opposed to piece-rate wages, claiming that people paid by the piece "are very apt to over-work themselves, and to ruin their health and constitution in a few years."⁵⁸

Smith's response to the excess use of division of labor was intervention by government. In an extended diatribe Smith harshly stated that:⁵⁹

But the understandings of the great part of men are necessarily formed by their ordinary employments. The man whose whole life is spent in performing a few simple operations, of which the effects too are, perhaps, always the same, or very nearly the same, has no occasion to exert his understanding, or to exercise his invention in finding out expedients for removing difficulties which never occur. He naturally loses, therefore, the habit of such exertion, and generally becomes as stupid and ignorant as it is possible for a human creature to become. The torpor of his mind renders him, not only incapable of relishing or bearing a part in any rational conversation, but of conceiving any generous, noble, or tender sentiment, and consequently of forming any just judgment concerning many even of the ordinary duties of private life . . . His dexterity at his own particular trade seems, in this manner, to be acquired at the expense of his intellectual, social, and

marital virtues. But in every improved and civilized society this is the state into which the laboring poor, that is, the great body of the people, must necessarily fall, unless government takes some pains to prevent it.

Taking into consideration the third provision's call for intervention, how should these problems be remedied? Smith was worried about worker alienation but did not propose that the division of labor be abandoned. Instead, there is an appeal to government intervention in order to improve the mental status of laborers. The contentious aspect of this issue is *not* whether government should intervene (it should), but that of determining the best method of remedying the problem. Free market advocates would likely consider this conclusion heretical. Nonetheless, I have provided sufficient argumentation to lend credence to the view that Smith's original intention for capitalist activity would justify government or judicial intervention on the behalf of employees.

Some scholars may argue that the terms of Smith's social contract constructed in Part III are too liberally derived. For instance, the first provision can be, and often is, watered-down to state that liberty to pursue one's own economic self-interests should be permitted "as long as there is no social harm," instead of "as long as there is a corresponding (though unintentional) improvement in social welfare." The former phraseology, maintained by most neoclassical economists, severely misrepresents Smith's project by taking him out of his 18th century context and denies Smith his teleological concern. Smith was reacting against mercantilism, not defending the modern day private enterprise system. The driving force behind Smith's vigorous critique of the status quo was his desire to improve the harsh living conditions he saw in Scotland and England. In the opening sentence of *WN*, Smith states his basic premise that productive labor is responsible for providing "all the necessaries and conveniences of life."⁶⁰ Smith was not simply a moral philosopher concerned with liberty, he was also an economist wanting to alleviate poverty and foster prosperity. He was willing to recommend radical changes in the business and society relationship only on the assumption that some positive outcome benefiting the general welfare would be generated.

In this article, I have presented Smith's views based on a systematic interpretation of his three intellectual concerns--ethics, economics and jurisprudence--and have constructed a social contract between business and society based on this interpretation. If my interpretation is correct, then many of the policy positions held by those whom claim Smith as their icon are undermined. This, however, is not the primary concern in determining the original intent of Smith's social contract. Instead, my hope is that, assuming the terms of the social contract are acceptable to both business and society, agreement can be reached as to when government, or the judicial system, is justified in intervening in business activities.

NOTES

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1. Thomas Donaldson (1982) *Corporation and Morality*, Englewood Cliffs, New Jersey: Prentice-Hall, Inc., chapter 3.
2. Rosalind Mitchison (1978) *Life in Scotland*, London: B. T. Batsford, Ltd, pp. 28-96.
3. Adam Smith (1776/1976) *Wealth of Nations [WN]*, Chicago: University of Chicago Press, vol. 1, p. 88.
4. Adam Smith (1978) *Lectures on Jurisprudence*, edited by R. L. Meek, D.D. Raphael & P.G. Stein, Oxford: Clarendon Press. As noted in the text, there are two sets of notes related to Smith's jurisprudence lectures. "LJA" refers to the lecture notes from the 1762-1763 school session. "LJB" refers to the lecture notes from the 1763-1764 school session. Both sets of notes are published in this collection.

5. Adam Smith (1759/1976) *The Theory of Moral Sentiments [TMS]*, Glasgow Edition, Indianapolis Indiana: Liberty Classics,

impressed Charles Townshend so much that he offered Smith a guaranteed lifetime pension to tutor his stepson, the young Duke of Buccleuch, an offer Smith gladly accepted.

6. *TMS*, p. 9. Thomas D. Campbell (1971) *Adam Smith's Science of Morals*, London: George Allen & Unwin, is the best secondary source that analyzes Smith's ethical theory.

7. *TMS*, p. 26.

8. *TMS*, pp. 265-314.

9. Aristotle, in *Nicomachean Ethics*, also uses approbation as a method for understanding morality.

10. *TMS*, p. 69.

11. *TMS*, p. 83. Unlike modern philosophers, Smith rarely defined his terms. In *TMS*, Smith tends to use the term "prudence" to represent the praise-worthy dimension of "self-interest" and "selfishness" to represent the blameworthy dimension of self-interest. In *WN*, Smith uses the term "self-interest" as a synonym for what he earlier referred to as prudence. Throughout the remainder of this article, I will also use the term "self-interest" as Smith invoked it in *WN*.

12. *TMS*, p. 79.

13. *TMS*, p. 79.

14. *TMS*, pp. 82 and 88.

15. *TMS*, p. 92.

16. *TMS*, p. 93.

17. *TMS*, pp. 100-101.

18. *TMS*, p. 105.

19. *TMS*, p. 17.

20. *TMS*, p. 117.

21. *TMS*, p. 46.

22. *TMS*, pp. 130, 131, 206, 218 and 276.

23. *TMS*, pp. 23, 89, 113, 145 and 166.

24. *TMS*, p. 87.

25. *WN*, ii, p. 208.

26. *WN*, ii, p. 208.

27. *WN*, ii, p. 222.

28. *WN*, ii, p. 244.

29. *WN*, ii, p. 244.

30. *WN*, ii, p. 340.

31. *WN*, ii, p. 444.

32. *LJA*, p. 14.

33. *LJA*, p. 208.

34. *LJA*, pp. 208-209.

35. *LJA*, pp. 210-215.

36. *LJA*, pp. 244-260.

37. *LJA*, pp. 265-271.

38. *LJA*, p. 282.

39. *LJA*, p. 313.

40. *LJA*, p. 105.

41. See Kaud Haakonssen (1981) *The Science of a Legislator: The Natural Jurisprudence of David Hume and Adam Smith*. New York: Cambridge University Press, p. 105, for a succinct typology of Smith's theory of rights. For other sources discussing Smith's jurisprudence see Istvan Hont & Michael Ignatieff (1983) *Wealth and Virtue*, New York: Cambridge University Press and Peter Stein (1979) "Adam Smith's Jurisprudence--Between Morality and Economics," *Cornell Law Review*, 64(4), 621-638.

42. Donald Winch (1983) "Adam Smith's 'enduring particular result': A Political and Cosmopolitan Perspective," in Hont & Ignatieff, p. 261. See Donald Winch (1979) *Adam Smith's Politics*, New York: Cambridge University Press, for an analysis of Smith's political positions.

43. *LJA*, pp. 106-122.

44. *TMS*, p. 282.

45. *WN*, i, p. 100.

46. *LJA*, pp. 176-177.

47. *LJA*, p. 188.

49. *LJA*, pp. 191-192.

50. *LJA*, p. 338.

51. *LJA*, p. 341.

52. *WN*, i, p. 11.

53. Will Durant & Ariel Durant (1965) *The Story of Civilization*, New York: Simon and Schuster, vol. 9. See also T.C. Smout (1986) *A Century of the Scottish People: 1830-1950*, London: William Collins Sons & Company.

- 54. Michison, p. 99.
- 55. Denis Collins (1989) "Organizational Harm, Legal Condemnation and Stakeholder Retaliation: A Typology, Research Agenda and Application," *Journal of Business Ethics*, 8(1), 1-14.
- 56. *WN*, i, p. 74.
- 57. *WN*, i, p. 92.
- 58. *WN*, i, p. 91.
- 59. *WN*, ii, 302-303.
- 60. *WN*, i, 1.

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