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THE THEORY OF THE DEMAND FOR REDISTRIBUTION: INEQUALITY, INCOME, AND THE LIMITS OF TOLERANCE



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The Theory of the Demand for Redistribution: Inequality, Income, and the Limits of Tolerance

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Abstract

This paper develops a formal model of redistributive demand with two boundaries in income–inequality space: an inequality possibility frontier (IPF), which defines the maximum feasible inequality given income relative to subsistence, and an intolerable inequality floor (IIF), above which redistribution is demanded.
Combining the IPF with Fehr–Schmidt preferences, we make the evaluation of inequality endogenous to institutions. Mobility, spillovers, contestability, entrepreneurship, and the costs of re- distribution determine whether greater inequality represents persistent exclusion or accompanies expanding opportunities and rising living standards. Institutions therefore jointly determine both inequality and its political tolerability.
This provides a positive alternative to Law and Political Economy (LPE), which emphasizes the institutional origins of distribution and power but imports normative priors about inequality into its analysis. We show that these distributional concerns can instead be incorporated within conventional rational-choice and comparative-institutional analysis, separating explanations of redistributive demand from the normative criteria ultimately used to evaluate institutional arrangements.

Résumé

Cet article développe un modèle formel de la demande de redistribution fondé sur deux frontières dans l'espace revenu–inégalités : une frontière des inégalités possibles (Inequality Possibility Frontier, IPF), qui définit le niveau maximal d'inégalité compatible avec un revenu donné relativement au seuil de subsistance, et un seuil d'inégalité intolérable (Intolerable Inequality Floor, IIF), au-delà duquel une demande de redistribution apparaît.
En combinant l'IPF avec les préférences de Fehr–Schmidt, nous rendons l'évaluation des inégalités endogène aux institutions. La mobilité, les effets de débordement, la contestabilité, l'entrepreneuriat et les coûts de la redistribution déterminent si une hausse des inégalités traduit une exclusion persistante ou si elle accompagne plutôt un élargissement des possibilités et une amélioration du niveau de vie. Les institutions déterminent donc conjointement le niveau d'inégalité et son degré de tolérance politique.
Cette approche propose une alternative positive au courant Law and Political Economy (LPE), qui met l'accent sur les origines institutionnelles de la distribution et du pouvoir, mais intègre dans son analyse des présupposés normatifs sur les inégalités. Nous montrons que ces préoccupations distributives peuvent plutôt être intégrées à une analyse conventionnelle

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fondée sur le choix rationnel et la comparaison des institutions, ce qui permet de distinguer les explications de la demande de redistribution des critères normatifs utilisés, en définitive, pour évaluer les arrangements institutionnels.

Mots-clés/Keywords : redistribution, inégalités, institutions, mobilité, économie politique / redistribution, inequality, institutions, mobility, political economy

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1 Introduction

The Law and Political Economy (LPE) project has a fairly distinctive argument about inequality. Its deeper claim is that the distributions of income, wealth, and "economic power" are endogenous to the legal rules that constitute markets. This claim is the foundation of a critique of neoclassical ("mainstream") economics as failing to recognize this fact and thus endowed with a limited ability to connect institutions to inequality (Britton-Purdy et al., 2020, p. 1792).

This, we argue in this paper, is based on a fundamental misunderstanding or a too shallow reading of what economists say about the theory of redistribution. In fact, we go one step further in showing that their framework is laborious to use (more than mainsteam economics) and that it is actually able to explain less rather than more. To see this, suppose workers receive 55% rather than 65% of total income (i.e., the labor share of income). In the LPE framework, there is the belief that economists would merely ask whether the resulting allocation is efficient and then separately ask whether taxes and transfers should redistribute it. This, it is argued, misses the questions of what institutions of bargaining rights, property rights, organizational rights, and economic power generated the 55% in the first place? LPE argues that market-oriented legal institutions create and reproduce particular distributions of economic power. Their manifesto for an alternative approach calls to make normative pre-commitments to democratic control, anti-subordination norms and egalitarian outcomes to study all the institutions that underlie markets.

It is entirely wrong that mainstream economics has *nothing to say* about this.[1] In fact, standard economic analysis can say more and explain more without any normative pre-commitments. Because the normative pre-commitments regarding inequality, LPE ignore the complex nature of inequality as a piece of economic information (Hirschman and Roth-

[1]While we will not belabor this point, some work dismissed by the LPE, on inequality and income mobility and institutions have actually gone where LPE pretends to pioneer and some of it by early nobelists (Buchanan, 1975; Tullock, 2013; Meade, 1993; Fogel, 2000). However, with the exception of Fogel, we will not rely on these works.

schild, 1973; Lazear and Rosen, 1981; Galor and Tsiddon, 1997; Welch, 1999; Foellmi and Zweimüller, 2006; Kufenko and Geloso, 2021; Callais and Geloso, 2023; Callais et al., 2025).[2] They fail to understand that it is an element in a complex trade-off between multiple dimensions of what constitutes living standards. Thus, they misunderstand what standard economic analysis offers in the matter. From that "original sin", the problems pile up. The LPE framework offers no ability to explain *why* people would ask for *any* redistribution or even tolerate existing distributions. It fails to explain regular findings that people *prefer* highly inegalitarian distributions in the presence of rapid economic growth and/or high mobility. Indeed, their framework is merely that inequality is bad (an normative pre-commitment) and there is no role for people making trade-offs about the initial (pre-redistribution) and final (post-redistribution) distribution of income.

In this paper, we show that – building on very well-known works of economic theory, such that we cannot be accused of pulling an unknown rabbit out of a not-well-known hat to slay a strawman – a simple model exists to explain both the initial and final distributions via people's trade-offs in designing institutions. We start by distinguishing feasible inequality (via the inequality possibility frontier, or IPF) from politically tolerated inequality (the intolerable inequality floor, or IIF). The IPF tells us how much inequality is technologically/economically feasible at a given income relative to subsistence and is borrowed from Milanovic et al. (2011); Milanovic (2013, 2018). The IIF is built from a standard Fehr-Schmidt utility function, as exposed in Fehr and Schmidt (1999), to incorporate an efficiency-redistribution trade-off.[3] The IPF is just a "natural boundary" imposed by human physiology (inequality cannot be so high that average income prevents subsistence income from being met for everyone except the richest) and has little economic content other than as a constraint. The IIF, however, is determined by people's trade-offs over institutional possibilities.

[2]Interestingly, we note that this point is not to be attributed to ideological priors. It seems to be a point shared across the spectrum as it includes strong free market apologists (Welch, 1999) but also strong left-wing apologists (Varoufakis, 2002). Both cited examples are interested because they are in direct conversation with each other with strong disagreement over the empirical approach. But they agree that inequality cannot be evaluated simply by its magnitude; its source and the process generating it matter.

[3]See also the discussion in Muñoz-Garcia (2017).

The key insight is that a choice of institution that permits rapid economic growth and high income mobility might depress the demand for redistribution *even if it generates greater contemporaneous inequality*. In the IIF, the relevant object is not inequality alone, nor even the institutions that generated inequality, but the value individuals attach to inequality conditional on those institutions. The same observed distribution can have very different implications for the demand for redistribution. It depends on whether income differences are interpreted as the product of exclusion and persistent rents or as the temporary consequence of a process characterized by entry, mobility, entrepreneurship, and positive spillovers. This is why we say that inequality has continuation value associated with others' current success: inequality is interpreted as information about the degree of spillovers, opportunities, and future gains (inclusive of intra-generational and inter-generational mobility). Institutions therefore determine not only *how much* inequality is generated but also *what that inequality means* to individuals. In doing so, our view of inequality is richer and has more depth than the real-number line implicit in LPE where more is worse. At the same we end up accepting the general claim of LPE that inequality is endogenous to the rules that underlie markets (a claim that no economist would actually dispute anyways).

From there, it is entirely possible to resume the usual, and LPE-condemned, rational choice analysis over institutional choices. Individuals *can* pick between feasible institutional choices and feasibility can be analyzed using standard transaction costs logic as per Alchian (2006a,b,c), Coase (2012), Acemoglu (2003) and Djankov et al. (2003).[4] Institutions bundle complementary rules because separating those rules, contracting around them, enforcing them, or combining them with rules from other arrangements may be prohibitively costly (in term of transaction costs) or simply technologically/institutionally impossible. In doing so, we engage in inequality analysis along highly conventional lines in economics but derive far more explanatory power than the LPE project can muster on its best day with its best suits.

[4]See also Leeson (2020).

The paper proceeds as follows. Section 3 presents the environment, the IPF, and the institutionally augmented preference structure. Section 3.3 derives the intolerable inequality floor. Section 3.4 defines the tolerated and redistribution regions and compares free and unfree societies. Section 5 concludes.

2 Institutions and Inequality

2.1 LPE

LPE's[5] founding narrative begins with a catalogue of crises, the first of which is that "income inequality has returned to the levels of the Gilded Age" (p. 1786).[6] Precarity, ecological threat, and democratic decay follow, and the project holds that developments in legal scholarship and policy over recent decades "helped to facilitate" all of them (LPE Project, nd). The culprit, on this account, is what LPE calls the "Twentieth-Century Synthesis," a "pervasive view of law that encases 'the market' from claims of justice and conceals it from analyses of power" (p. 1784). The Synthesis worked through a division of labor. In public law, scrutiny was confined to the differential treatment of individuals, especially by the state, and economic power was left out of view (p. 1790). In the private-law fields understood to be "about the market" (contracts, property, antitrust, intellectual property, and corporate law), law and economics "centered efficiency and sidelined questions of distribution, power, and democracy" (pp. 1790, 1794). The second half, in which economics stands accused, is the one that concerns us.

LPE presents law and economics as an heir that squandered its inheritance. The project

[5]We use "LPE" to refer to the LPE Project's statement of purpose (LPE Project, nd), its manifesto (Grewal et al., 2017), the programmatic statement of Britton-Purdy et al. (2020), and the introduction to the first issue of the *Journal of Law and Political Economy* (Harris and Varellas, 2020). We also draw on Grewal and Purdy (2014) and Kapczynski (2026), both written by authors of the programmatic statement. Unless otherwise noted, page references in this section are to Britton-Purdy et al. (2020).

[6]The supporting citation is Thomas Piketty's *Capital in the Twenty-First Century* (p. 1786, n. 1), so the claim rests on top-income series whose accuracy is disputed. We return to the measurement debate at footnote 10 and note merely that this entire empirical foundation of LPE with respect to inequality is as precarious as King Louis XVI's finances on the eve of the French Revolution.

roots itself in the realist "insight that politics and the economy cannot be separated and that both are constructed in essential respects by law" (LPE Project, nd). Its favored ancestor is Robert Hale, who described economic life as a system of mutual coercion in which each person's coercive power comes from the legal entitlements they hold (p. 1819). From Hale and the other realists, LPE takes the lesson that "legally constituted and distributed coercion is the sine qua non of market relations" (p. 1796) and that markets are "creatures of law and politics, crafted by the state" (Harris and Varellas, 2020, p. 5).[7] Law and economics, in LPE's telling, inherited this realism and even "embraced the realization that law makes markets" (p. 1796). It then defined law's goals in a way that "demanded a new kind of rule of the market" and, along the way, "abandoned the concern with economic life's character as a site of struggle amid unequal power" (p. 1796). What followed was "market supremacy," the subordination of the political to the economic (p. 1796).[8]

Their claim is that by organizing legal analysis around transaction costs, externalities, efficiency and the feasibility of bargains, "mainstream" economics places the initial distribution of rights and bargaining power outside the central analytical frame. Efficiency, in the form of wealth maximization, supplies the criterion, and elevating "marginalized questions of distribution" (p. 1797). The feasibility of bargains supplies the frame. In LPE's reading of the Coase theorem and its subsequent development in law and economics, entitlements flow to their highest-valued use wherever the law first places them when bargaining is cheap, while, when bargaining is costly, the law should assign them as the hypothetical market would have done (p. 1799). Either way, the theorem "effaces the otherwise inescapable nub

[7]LPE uses "political economy" in this realist sense, as the study of an economy that is "always already political in both its origins and its consequences," and explicitly not in the sense of the rational-choice analysis of government practiced in economics departments (p. 1792). The tools we use below (transaction costs, bargaining, and institutional choice in the tradition of Alchian 2006a, Coase 2012, Acemoglu 2003, and Djankov et al. 2003) belong to the tradition LPE sets aside. We also note that theirs is a strange reading of legal history. Significant and sizable parts of common law emerged *outside and without* the state to create markets (Hogue, 1985; Plucknett, 2010; Hasnas, 2024). It is only later, once markets had created wealth, that states began absorbing what was essentially "stateless law" by codifying what was customary. But that critique of LPE is better left to outright jurists not mere economic historians and economists like ourselves who only listen to jurists.

[8]Kapczynski (2026, p. 443) puts it more bluntly. The law and economics movement, "though it built upon the realists, came to resemble a new kind of formalism."

of the problem: who wins and who loses, and who may do what to whom?" (p. 1798). Transaction costs and externalities supply the vocabulary. With wealth maximization, they are the "linking theories" that tie legal rules to general equilibrium theory (p. 1800), and they recast conflicts between competing interests as "a failure of accounting or pricing" (p. 1806). What is left is "an abstract but mathematically elegant account, in which questions of coercion and distribution play no formal part" (p. 1800).

That distributions depend on the rules that constitute markets is not in dispute (despite hints to the contrary in some LPE works). LPE's complaint is that economists arrive at distribution too late. Distribution enters as an outcome to be corrected through taxes and transfers, while the allocation of rights that produced it is taken as given, and so law and economics "placed questions of distribution and coercion outside the lamplight of methodology" (p. 1819). In the labor-share example of the introduction, the economist asks whether a labor share of 55 percent is efficient and how much of the resulting income to redistribute, whereas LPE asks which bargaining, property, and organizational rights produced the 55 percent in the first place. LPE even phrases the point in the economist's own vocabulary. If economics is the study of choice under constraint, then "the emphasis should fall soundly on 'constraint' and its legally constituted allocation" (p. 1820). Transaction costs cannot do that job, on this account, because what counts as one is "open-ended: push further and every impediment is revealed as the product of other background social and economic processes" (Kapczynski, 2026, p. 456, quoting Grewal).

From this diagnosis LPE derives a program, a move "from the analysis of efficiency to the analysis of power, from the pursuit of neutrality to the pursuit of equality, and from the antipolitics of the Twentieth-Century Synthesis to a candid and risky embrace of democracy" (p. 1794). That is a normative pre-commitment. Only the first of these concerns how the economy works. The other two say how it ought to be judged, by an equality "animated by a commitment to self-rule and sensitive to the importance of social subordination along intersectional lines" (p. 1824) and by whether law's creation of economic

order is accountable "to those who live in that order" (p. 1827). LPE does not present these standards as findings. "[T]he substance of these arguments," it says, "lies in political morality," and a democratic political economy "is a moral project" (p. 1832). Kapczynski (2026, p. 458) goes further, writing that LPE "contests the idea that there can be any science that will defer the ineluctably normative questions involved in ordering the political economy of today."[9] In LPE's own summing up, the realists had it right, and the emphasis belongs "on power, distribution, and the need for legitimacy as the central themes in the organization of economic life" (p. 1833). Diagnosis and moral program thus arrive together, and an unequal distribution is read, almost by definition, as a record of unequal power.[10]

2.2 What Does Inequality Mean? The Core Intuition

The first error of the LPE framework is that it assumes that all the economic information contained in an observed level of inequality can be read as describing whether a society is fair or not. Higher inequality is a bad. Lower inequality is a good. Knob to the left, good; knob to the right, bad.

But that is incorrect. What observed inequality conveys is highly complex. Consider, for example, Hirschman and Rothschild (1973), who provide one of the earliest arguments that it may depend on the context. For them, there is a "tunnel effect" whereby those who move ahead send a signal (unknowingly) to people behind them, informing them that their own prospects (or those of their children) might improve soon. This can easily be likened to the Kuznets curve logic, whereby inequality first rises with income and then declines (Kuznets, 1973). This is because, as industrialization occurs, younger individuals move to cities where

[9]Harris and Leeson (2026) conclude that the dispute between LPE and law and economics is therefore not one between realism and formalism but an ideological one between progressivism and liberalism, over whether power should be constrained no matter who wields it or placed in more democratic hands.

[10]We note that this manifesto is very much akin to putting new legalese robes on arguments made by Thorstein Veblen, Ferdinand Lasalle, Louis Blanc, Jean-Charles de Sismondi and Pierre-Joseph Proudhon (see notably the excellent treatment of Sismondi by Sowell (2006)). There may be a new tricolor flying over the barricade, but the revolutionaries underneath it are remarkably familiar. In fact, strip away any modern vocabulary and there is little here that would have confused a well-read revolutionary manning a Parisian barricade in 1848 or 1870. As such, new times, same things.

wages are higher (Williamson, 1990, 2013). This pushes up inequality since more people now earn higher urban wages relative to lower rural wages. As long as the urban population does not reach a critical mass, inequality will rise. However, once that critical mass is reached, inequality declines. The mechanism underlying the Kuznets curve is similar to Hirschman and Rothschild (1973)'s tunnel effect, since the process of industrialization through the growth of cities informs people that their living standards (or those of their children) will rise, and thus inequality is perceived quite differently.

Another example is that of the standard model of income mobility across generations developed by Becker and Tomes (1979). In that model, there can be a wide cross-sectional dispersion of wages (i.e., inequality). Some of that dispersion can be explained by the effort of individuals. Some of it might be due to intergenerational persistence, whereby parents transfer their income ranks (or even levels) to their children because they can ill afford to make "parental investments" in human capital that boost their children's later-life income. The key mechanism here is that there must be some genuine borrowing constraints (i.e., imperfect capital markets) that prevent funds from going to high-potential individuals from poor backgrounds who must rely only on funds from their families. The result is that high inequality in that context means low intergenerational income mobility. However, if that constraint is not present or is too weak to have any bite, then you could end up with high inequality *and* great intergenerational mobility. If it has no bite, the ability of parents to fund their children's human capital acquisition is not relevant because capital markets or philanthropy channel funds to them as they offer high returns. Second, if these investments fund growth in human capital, then the next generation earns more than the previous one, and that alone increases cross-sectional dispersion (i.e., inequality). Third, within each generation, there is a random element (i.e., luck, good or bad) to wages which, in standard wage regressions, can be likened to the residual term. If the younger generation is richer on average by a factor of two (for the sake of illustration), such that the entire wage distribution shifts to the right and its standard deviation scales proportionally, then

the standard deviation in dollar terms will be absolutely larger than that of the previous generation. Thus, the same relative amount of "luck" in a richer generation generates greater dispersion in dollar terms. Fourth, in the Becker-Tomes model, there is the possibility that a wider dispersion around a greater mean *incentivizes* more effort. In other words, the possibility of extremely high incomes might incentivize greater effort among some individuals. Thus, as long as there is some heterogeneity in preferences for effort, some will deploy greater effort to reach the top because the payoffs are so large. That will also increase inequality. But, in this case, the resulting inequality does not reflect the transmission of parental status to children (i.e., low mobility). In fact, in this example, the chance for *more* mobility (i.e., imagine a Horatio Alger rags-to-riches story) is actually *increasing* inequality. These insights from the work of Becker and Tomes (1979) end up pointing to something similar to Hirschman and Rothschild (1973): the context in which inequality is observed dramatically affects the meaning of whatever is measured (let's assume correctly).[11]

A closely related point to the Becker and Tomes (1979) work is that of Galor and Zeira (1993a). In the presence of imperfect capital markets, borrowing constraints are important and human capital investments must be funded to some degree from one's own savings. Inequality thus affects who is able to make human capital investments that secure upward moves and a high-inequality/low-mobility society can emerge. However, in this case, redistribution might reduce constraints. Unlike physical capital, for which collateral can be

[11]This is not a trivial point. There is a huge debate over the accuracy of inequality measurement, with Piketty and Saez (2003, 2007); Piketty et al. (2018) arguing for a pronounced U-curve pattern from the 1910s to today, with the bottom being reached in the 1950–1980 period (and thus an increase since then). In contrast, Auten and Splinter (2024), Larrimore et al. (2021), and Geloso and Magness (2023) argue that the measurements are incorrect and that there is a far more moderate increase since 1980, with no further increase after 2000. Geloso et al. (2022); Geloso and Magness (2020); Geloso and Toda (2026) show that the left-hand part (pre-1950) of the U-curve is also overestimated and that there was a decline in inequality from 1870 to 1910 that continued to 1940 (Geloso, 2027). We mention this because some LPE work simply *assumes* that one side of the measurement debate is correct and then titles its work with terms such as Accelerating Crises" to refer to rising inequality (among other things). But this means that they picked" a measurement and never discussed how their approach would change if the other group of measurers were correct. In other words, they are assuming" that accelerating crises" are a thing (Harris and Varellas, 2020). Alas, Fidel has no cigar, and this is a no-go! This point is another criticism that we think should be mentioned, but which we leave to others to expand further upon, as we prefer to focus on the more core point of interpreting inequality *assuming* measurement is accurate and not debated.

offered thus compensating through seizure the lender in the case of default, human capital is embodied in individuals and cannot be seized. Thus, poor households with few collateral have little to offer. Paradoxically, this may incentivize *too much* aggregate investment in physical capital relative to too little human capital such that the marginal returns on the latter still exceeds the marginal return on the former. In this case, redistribution is actually growth-enhancing because. The implication is not that redistribution is necessarily desirable, but that its desirability cannot be inferred from inequality alone.[12] Indeed, the *same* outcome could be generated in a low-inequality/low-mobility society. What matters is the context that jointly determines inequality, mobility, financing constraints, and the returns to human-capital investment.

Other insights from economic theory (and economic history) showcase that there can be contexts in which high inequality is informative of a highly desirable (for everyone) process. All of these boil down to spillovers" of sorts. Nordhaus (2004) pointed out that innovators appropriate only a small share of the social benefits of their inventions—less than 4% at best. For example, the pioneering firms producing barbed wire during the 19th century received profits from selling the good to farmers (Hornbeck, 2010). In contrast, because barbed wire helped solve the serious problem of animal trespass destroying crops (or animals being killed by predators), farmers (who were definitely near the bottom of the income ladder at the time) were able to increase the value of their land because more income (with fewer losses) was generated. The vast majority of the social gains" from barbed wire spilled over to people further down the income ladder. Thus, inequality may have increased, but everyone was better off. Now, imagine a process where innovators can appropriate *more* of the social benefits (say 5% instead of 4%—a one-quarter increase in the profitability of innovation, which is not negligible). The incentives to innovate become even stronger. If one imagines a log-normal distribution of income, multiplying breakthrough technologies shifts the entire distribution to the right but may dramatically widen the right tail (i.e., not all rightward

[12]This is also present in the work of left-leaning economists like Lindert (2022) and Boyer (2023).

shifts are of the same proportion), such that *everyone* could be better off despite a few more extreme fortunes. In that case, the spillovers from innovation make the inequality *desirable* if one cares about one's own well-being.[13]

Another spillover is even more telling. Geloso and Lindert (2020) and Geloso (2027) show that, from 1870 to 1910, the cost of living in the United States became dramatically more egalitarian. The prices of goods typically featuring in greater proportions in the budgets of the poor *fell* relative to those of goods featuring in greater proportions in the budgets of the rich. One key reason for this was that the innovative process itself was pushing up wages for unskilled workers in sectors where productivity was rising. However, in sectors with slower productivity growth, wages had to be bid up to match those in sectors to which workers could move. Without the same productivity gains, those sectors had a harder time hiring the same number of workers. These sectors with slower productivity growth were typically services. More precisely, they were service sectors that featured heavily in the baskets of the very rich (e.g., household staff, clerical and white-collar services, etc.). That meant that the "price" of these services, which featured more heavily in the baskets of the rich, rose in line with the productivity-driven wage increases of workers in manufacturing or other fast-productivity-growth sectors. This was dramatically leveling inequality. But this, too, was a spillover from innovations that shaped the interpretation of any given level of *nominal income* inequality.

All of these examples speak to the idea that one could observe two societies with the same *very high* level of inequality and still be unable to conclude much from it. One could be a hierarchical society with laws that set status in stone and transmit it across generations, with no mobility whatsoever, no innovation, no spillovers, and no new opportunities. The other

[13]Berggren (2026) provides the same insight but starts from a policy action to reduce inequality (and thus connects to optimal taxation theory). If inequality-reducing policies affect entrepreneurial entry and innovation spillovers, the inequality index loses considerable information for describing outcomes. Indeed, policies that lower inequality may simultaneously alter the productive process generating the upper tail by discouraging entrepreneurial entry or reducing entrepreneurial output (i.e., innovations). If these entrepreneurs generate positive spillovers, then the welfare gain from compressing the distribution must be weighed against the welfare loss from reduced productive activity. Inequality and entrepreneurship may therefore move together as endogenous outcomes without inequality itself being socially beneficial.

could be a society with rapid economic growth, no persistence of parental status, massive innovation, and gigantic spillovers from innovations that pull everybody up.

It is here (and why) we can incorporate the core point made by Finis Welch (1999) some years ago, whereby "inequality is destructive whenever the low-wage citizenry views society as unfair, when it views effort as not worthwhile, when upward mobility is viewed as impossible or as so unlikely that its pursuit is not worthwhile" (Welch, 1999, p. 2). This emphasizes that the process matters. The rules of the game that shape this process matter. And each set of rules has trade-offs that must be weighed! Our argument pushes that logic one step earlier: the level of inequality is also insufficient to explain the emergence of redistributive demand itself. Individuals evaluate inequality jointly with the mobility, spillovers, income opportunities, and costs of redistribution generated by the institutional environment. Simply put, the trade-offs do include aspects of distribution!

People are not idiots. They intuitively understand that not all inequalities are the same. They know that there are trade-offs facing them in designing the "process." In fact, this is where our most important criticism of LPE can be elaborated. Because they misunderstand the economic information conveyed by inequality statistics, they fail to understand that people can make rational choices over the most efficient institutional arrangements *considering* both pre- and post-redistribution inequality. In the next section, we develop the model to show that people can rationally prefer institutional arrangements that generate greater pre-redistribution inequality when those same arrangements also generate greater mobility, larger spillovers, higher average incomes, or make redistribution more costly in terms of foregone opportunities. Conversely, individuals may prefer arrangements with lower pre-redistribution inequality when the costs of redistribution are sufficiently small or when inequality is associated with low mobility and weak spillovers. The relevant choice is therefore not over inequality in isolation, but over institutional bundles that jointly determine both the distribution of income and the opportunities attached to that distribution. By developing a model that explains institutional choice, initial inequality, and post-redistribution

inequality without invoking *any* normative stance, we show that the entire LPE framework adds *nothing* whatsoever and even reduces explanatory power.

3 The Model

As our claim is that we do not require any normative pre-commitments to develop a positive analysis of institutional choice that incorporates both pre-redistribution and post-redistribution considerations, a model is necessary. The key ingredients of *any* good model where humans choose requires constraints and trade-offs and some array of items that people care to maximize.

3.1 The Inequality Possibility Frontier

Consider a society composed of N individuals distributed across n social classes indexed by $i = 1, \ldots, n$, where classes are ranked by mean income. Let p_i denote the population share of class i, y_i its mean income, π_i its income share, and G_i the Gini coefficient measuring inequality within class i. The overall Gini coefficient decomposes as

$$G = \sum_{i=1}^{n} G_i \, p_i \, \pi_i + \frac{1}{\mu} \sum_{i=1}^{n} \sum_{j=i+1}^{n} (y_j - y_i) \, p_i \, p_j + L, \tag{1}$$

where μ is overall mean income and L is an overlap term (strictly non-negative). The first term on the right-hand side of (1) captures total inequality due to inequality within classes. The second term captures total inequality due to differences in mean incomes between classes. The third term, L, captures the contribution of overlapping income ranges across classes.

To derive the maximum feasible inequality at a given level of development, we follow the approach of Milanovic et al. (2011) and make three simplifying assumptions that eliminate the within-group and overlap components. First, let $s > 0$ denote the subsistence minimum, the minimum income needed for survival.[14] Let μ denote overall mean income, and define

[14]Readers should think of s as the result of minimizing expenditures to a minimum that ensures survival

the income ratio

$$\lambda \equiv \frac{\mu}{s}, \qquad \lambda \geq 1. \tag{2}$$

Second, suppose that a fraction $\varepsilon \in (0,1)$ of the population belongs to a small upper class, while the remaining fraction $1-\varepsilon$ belongs to a lower class. This assumption of only two classes is not necessary to our model, but it is useful to gain mathematical traction in explaining the utility from any given distribution (see next subsection) and derive a simplified illustration in one graph. To find the maximum feasible Gini conditional on ε, push all members of the lower class to exactly subsistence, so that $y_L = s$. Within each class, everyone earns the same income, so $G_i = 0$ for each class and the within-group term vanishes. With only two non-overlapping groups, $L = 0$ as well. The overall Gini therefore reduces to the between-group term alone:

$$G = \frac{(1-\varepsilon)\varepsilon(y_H - s)}{\mu}. \tag{3}$$

The upper-class income is determined by the budget constraint. Total income in the economy is μN, of which the $(1-\varepsilon)N$ members of the lower class each absorb s, so the εN members of the upper class receive the remainder:

$$y_H = \frac{\mu N - s(1-\varepsilon)N}{\varepsilon N} = \frac{1}{\varepsilon}\big(\mu - s(1-\varepsilon)\big). \tag{4}$$

Substituting (4) into (3) gives the inequality possibility frontier:

$$G^*(\lambda) = (1-\varepsilon)\left(1 - \frac{1}{\lambda}\right) = \frac{(1-\varepsilon)(\lambda - 1)}{\lambda}. \tag{5}$$

The IPF gives the maximum feasible Gini coefficient at each level of average income relative to subsistence, conditional on ε. When $\lambda = 1$, every person earns exactly subsistence and no inequality is possible. As λ grows, there is more surplus above subsistence that can be

as in the earliest effort of Stigler (1945). However, nothing prevents this to be more inclusive to capture more complex aspects of the constraints associated with subsistence (Allen, 2017; Moatsos, 2025; Moatsos and de Zwart, 2025).

concentrated, and the frontier rises. For any given ε, the IPF G^* has four key properties.

The first states that at the average income equal to pure subsistence, $G^*(1) = 0$. In other words, if the average income is equal to the cost of a subsistence basket. No inequality is feasible without pushing at least some individuals below subsistence and thereby threatening survival. Second, $G^*(\lambda)$ is strictly increasing in λ implying that societies with above subsistence level income can produce more inequality than those closer to subsistence income. Third, $G^*(\lambda)$ is strictly concave in λ which is produced by the second derivative of the function with respect to λ and conveys the intuition that subsistence becomes biologically less binding as society grows richer. Finally, $\lim_{\lambda\to\infty} G^*(\lambda) = 1 - \varepsilon$ implying that inequality cannot reach 1 in this two class setup which captures the ideas that feasible inequality has an upper bound.

3.2 Interior Valuations

In the two-dimensional space defined by average income relative to subsistence, λ, and inequality, G, the IPF defines the boundary of the feasible set. In our model, we assume that combinations such that $G \leq G^(\lambda)$ are biologically feasible, whereas combinations such that $G > G^(\lambda)$ are *biologically* infeasible. This is consistent with some early works in economic history. For example, Freudenberger and Cummins (1976) argued that the length of the workyear in the pre-Industrial Revolution period was probably shorter than most would expect. However, this may have been one aspect of an "equilibrium situation determined partly by a high prevalence of debilitating disease and by low and unpredictable supplies of food" (p. 10). Expected energy intake for workers was so scarce that, they argue, there were episodes during the year when they simply could not work long hours. Fogel (2000) later revisited that point by estimating the distribution of calories and then asking how many hours of work could be sustained on the diet implied at each centile. Looking at France in the years before people began to lose their heads, he found that the very bottom of the caloric distribution, roughly 3% of the population, lacked sufficient energy for any work at all,

whereas the bottom quintile could do, on average, 6 hours of light work per day.[15] As such, at incomes near s, we should not assume that the IPF captures "low" utility. It captures a hard boundary beyond which survival in the long run is impossible. It is *not* an arbitrary normalization. It is a pure biological limit to inequality – no institutional arrangement can fight this limit forever.[16]

However useful and economically intuitive this is, it provides *no* information about points where $G < G^{(}\lambda)$. More precisely, it provides no information about how people value inequality associated with any income level. Not only that, but it says nothing about how much inequality is "tolerated". Indeed, with only the IPF, we cannot pinpoint where any "demand" for redistribution might activate and exist. To consider any interior level, we must first be able to translate the combination (μ, G, ε) into the incomes of the lower and upper classes (x_L, x_H). At any Gini $G \leq G^{(}\lambda)$, the two-class budget constraint and Gini formula jointly determine class incomes. The budget constraint is

$$(1-\varepsilon)x_L + \varepsilon x_H = \mu, \tag{6}$$

and the two-class Gini is

$$G = \frac{\varepsilon(1-\varepsilon)(x_H - x_L)}{\mu}. \tag{7}$$

Solving (6) and (7) for class incomes yields[17]

$$x_L = \mu\left(1 - \frac{G}{1-\varepsilon}\right), \qquad x_H = \mu\left(1 + \frac{G}{\varepsilon}\right). \tag{8}$$

The term of interest to us is $x_H - x_L$ in equation (7) as it can be repurposed in terms of a Fehr-Schmidt utility function (Fehr and Schmidt, 1999) where payoffs to "others" $(j \neq i)$

[15] Similar work exists doing the same exercise for other societies at different points in time (Ogasawara et al., 2020; Medina-Albaladejo and Calatayud, 2020). See also important methodological qualifications to Fogel's distributions (Schneider, 2013).

[16] Or as one famous Roman senator once said: revolt is always three missed meals away.

[17] Note that $x_L \geq s$ is equivalent to $G \leq G^*(\lambda)$, confirming that the IPF is the boundary at which the lower class is pushed to subsistence.

creates envy for a person i and which is captured in the term α (if income is lower than for others) or guilt for that same person if one is richer than others which is captured in β:

$$u_i^0(x_i, x_j) = x_i - \alpha \max\{x_j - x_i, 0\} - \beta \max\{x_i - x_j, 0\}, \qquad 0 < \beta < \alpha < 1. \tag{9}$$

Its piecewise form is

$$u_i^0(x_i, x_j) = \begin{cases} (1+\alpha)x_i - \alpha x_j & \text{if } x_j \geq x_i, \\ \\ (1-\beta)x_i + \beta x_j & \text{if } x_i > x_j. \end{cases} \tag{10}$$

Thus, at the primitive level, disadvantageous inequality generates envy (weighted by α) and advantageous inequality generates guilt (weighted by β). Generally, when using Fehr-Schmidt utility function there is a tendency to assume that guilt is weaker than envy. It is why Fehr-Schmidt utility functions are useful tools to understand why people attribute some value to egalitarian outcomes. However, the true value of the model is its flexibility (something noted by the authors themselves and seen in textbooks such as Muñoz-Garcia (2017) who discuss it). Note that if the disutility from envy is negative ($\alpha_i \in \left(-\frac{1}{2}, 0\right]$) and the disutility from guilt is positive ($\beta_i \in \left[0, \frac{1}{2}\right)$); and the latter dominates the former in absolute value ($|\alpha_i| < |\beta_i|$) then the Fehr and Schmidt (1999) specification captures a *preference for efficiency*. This is not a trivial point. Consider that for the poorest person in our two-person setup, the utility function collapses to

$$u_L^0 = x_L - \alpha(x_H - x_L) \tag{11}$$

such that it is easy to visualize that $\alpha < 0$ generates a greater utility for the poor if the rich is richer. Intuitively, this relates to our point about the core intuition above. It should not be interpreted as the "poor is happier when the rich person is richer". Rather, it should be interpreted as being tied to the process that made the rich richer. If he invested in capital

goods, his income might boost the poor's person income or the chances at upward mobility for him. In other words, the sign in front of α and its size relative to β are our objects of interest here. The core intuition we laid out earlier is that these parameters are determined by institutions in ways that help explain *both* the initial distribution and the demand for redistribution leading to the final post-tax distribution.

To see how, let $r \in \{U, F\}$ index the institutional regime, interpreted as low-quality and high-quality (we can and will loosen this later, but it simpler here for expositional sake to allow this real-line-interval-like thinking). Let θ_r denote institutional quality, with higher θ_r associated with a society that improves in its protection of property rights and promotion of open markets.[18] To engage in our adjustment from Fehr-Schmidt, we must understand that the core intuition we laid out above implies that current inequality may have continuation value (as per Welch (1999)) in that it informs people about greater income opportunities (now and in the future) conditional on whether there are pathways to plausibly achieving those. This bears repeating: in a better institutional environment, the success of others *may* be informative about future opportunities, whether through mobility, learning, entrepreneurship, imitation, or generalized growth spillovers. Thus current inequality $x_j > x_i$ is interpreted as information about opportunity, not permanent exclusion. We capture this with an institutional continuation term:

$$\delta m_r \max\{x_j - x_i, 0\}, \qquad m_r \equiv m(\theta_r), \qquad m'(\theta_r) > 0, \tag{12}$$

where $\delta \in (0, 1)$ is the discount factor. Total utility in regime r is therefore

$$u_i^{(r)}(x_i, x_j) = x_i - \tilde{\alpha}_r \max\{x_j - x_i, 0\} - \beta \max\{x_i - x_j, 0\} \tag{13}$$

[18] We reiterate that this *does not* mean absence of regulation in full. As Hasnas (2024) points out, regulation via common law doctrines of nuisance, negligence and trespass can be superior to bureaucratic regulation but there could also be complementarity between them in helping courts find more straightforward standards (McMillan and Woodruff, 2000) or help with incomplete contract problems (Shleifer, 2012; Ash et al., 2025).

where $\tilde{\alpha}_r = \alpha - \delta m_r$ which is the effective envy parameter. This has the same functional form as the standard Fehr–Schmidt utility, but with $\tilde{\alpha}_r$ replacing α. The institutional continuation value offsets primitive envy. If institutions are sufficiently strong such that $\delta m_r > \alpha$, then $\tilde{\alpha}_r < 0$: disadvantageous inequality enters utility positively because the success of others signals future opportunity. When the continuation value of others' success more than offsets primitive envy, the relevant parameter range is $-1 < \tilde{\alpha}_r < 0$, $0 < \beta < 1$, and $|\tilde{\alpha}_r| < \beta$. The term $|\tilde{\alpha}_r| < \beta$ means that, in absolute value, the reward from being behind is smaller than the penalty from being ahead. This disciplines the asymmetry of the two branches, but it is *not* a fixed-sum equality condition.[19] As such, equation 11 can be rewritten such that inequality raises utility for the poor:

$$u_L^{(r)}(x_L, x_H) = x_L + |\tilde{\alpha}_r|(x_H - x_L) = (1 - |\tilde{\alpha}_r|)x_L + |\tilde{\alpha}_r|x_H. \tag{14}$$

because he has the understanding that his own payoff will be materially greater if the rich is richer (either now or later) since he can now expect greater future welfare through spillovers and mobility. These "later payoffs" for a low income individual in regime can be re-expressed by substituting (8) into (14) gives

$$u_L^{(r)} = \mu - \mu G \frac{\varepsilon + \tilde{\alpha}_r}{\varepsilon(1-\varepsilon)}. \tag{15}$$

Now, let $p_r \in [0, 1]$ denote the probability that a low-income individual occupies the high-income position next period[20], with $p_r = p(\theta_r)$ and $p'(\theta_r) > 0$. Expected utility is

$$\mathbb{E}_r[u_L] = (1 - p_r)\big[(1 + \tilde{\alpha}_r)x_L - \tilde{\alpha}_r x_H\big] + p_r\big[(1 - \beta)x_H + \beta x_L\big]. \tag{16}$$

[19]Note as well that the inequality $|\tilde{\alpha}_r| < \beta$ does not imply that equality is preferred when total income $x_i + x_j$ is held fixed. Along the poor branch, fixed-sum equality requires $|\tilde{\alpha}_r| < 1/2$. Along the rich branch, fixed-sum equality requires $\beta > 1/2$. We do not impose those stronger restrictions here.

[20]Here, we can think of the possibility as well that the income of the poor rises tomorrow to the level of the rich today as well.

Define

$$\tilde{\Delta}_r \equiv 1 + \tilde{\alpha}_r - \beta. \tag{17}$$

such that equation (16) simplifies to

$$\mathbb{E}_r[u_L] = \mu - \mu G \frac{d_r}{\varepsilon(1-\varepsilon)}, \qquad d_r \equiv \varepsilon + \tilde{\alpha}_r - p_r \tilde{\Delta}_r. \tag{18}$$

This means that the parameter d_r is the effective slope of expected utility with respect to inequality. Better institutions lower d_r by making current inequality more tolerable through both opportunity and mobility. We impose only one set of assumption whereby $d_r > 0$ and $\tilde{\Delta}_r > 0$. This is because if we allow $d_r < 0$, a low-income person would want *more* inequality all else equal. While we think this assumption is realistic, we do not believe it to be crucial. In fact, it works against our claim. Indeed, we say that if people are presented with an institutional choice that would raise inequality dramatically but also raise their living standards more than alternative arrangements, they could choose it. However, we believe that most would find to be stretching imaginations and might accuse us of letting the parameter do the dirty work in the assumption. By forcing non-negativity, we simply assume that people do not like inequality in and of itself.[21] The second restriction, $\tilde{\Delta}_r > 0$, ensures that greater upward mobility lowers d_r and therefore makes current inequality more tolerable, since $\partial d_r / \partial p_r = -\tilde{\Delta}_r < 0$.

Overall, equation (18) simply expresses that expected welfare is the value of having a larger pie size minus the cost of inequality. The second term being the cost. Our argument here is that d_r is itself a function of an initial institutional choice.

[21] We note that this matters in generating a concave-shaped IIF in the next section. Indeed, a $d_r < 0$ would open the door to convex-shaped floor or maybe quasi-linear or even piecewise defined sections where the IPF could dominate the IIF in some ranges and which would in turn allow for large institutional shifts past certain income levels.

3.3 The Intolerable Inequality Floor (IIF)

The feasibility threshold is determined by subsistence in the IPF. But there is a political threshold which is determined by the attractiveness of redistribution relative to the status quo. This is our ceiling for tolerating inequality or, phrased backwards, it the floor at which inequalities start to be intolerable (our intolerable inequality floor or IIF).

The key issue here is some might expect to ask why people would ask for redistribution. All we have done up to this point is define a boundary and the valuation of interior points. But how do people trade-offs between those points? Or more precisely, what constraints exist to explain the choices.

Indeed, if there were redistributive schemes that grew the pie's size and all members were better off, why refuse? This is notably what we indicated above when discussing Galor and Zeira (1993a). However, saying this implies that individuals will consider trade-offs on growing between absolute levels of income, income mobility and income distribution. This means that our term d_r from above and a new term κ are not going to be independently influenced parameters but rather jointly/simultaneously determined with the selection of rules/institutions. In this, we respect the tradition that institutions should be understood as bundles of rules selected and adapted according to the joint consequences they generate rather than as independently chosen policy instruments. In the Alchian-style efficiency view (Alchian and Demsetz, 1973; Alchian, 2006a,b,c) (we will return to this below in the discussion section), institutional arrangements survive and evolve insofar as they facilitate higher-valued uses of resources under the relevant constraints. Rules that better facilitate mutually beneficial exchanges, economize on transaction costs, and direct resources toward higher-valued uses may emerge and persist precisely because of the surplus they generate. Consequently, the institutional environment simultaneously determines both the content individuals attach to a given distribution, summarized by d_r, and the output consequences of altering that distribution, summarized below by κ_r. Neither should therefore be interpreted as an independently selected parameter.

To see this, suppose that *some* redistribution is demanded. The degree to which it compresses inequality is given by $\tau \in (0, 1]$ such that post-redistribution inequality is

$$G^{\tau} = (1 - \tau)G. \tag{19}$$

However, that redistribution is not costless. Compression may destroy part of the opportunity-generating process by weakening contestability, learning, investment, or entrepreneurial return.[22] Let $\kappa_r \in [0, 1)$ denote the regime-specific efficiency cost of redistribution, measured as the fraction of the surplus above subsistence destroyed by a unit of redistribution intensity.[23] Post-redistribution mean income is therefore

$$\mu_r^{\tau} = \mu - \kappa_r \tau(\mu - s). \tag{20}$$

Given equations (19) and (20), post-redistribution class incomes are

$$x_L^{\tau} = \mu_r^{\tau}\left(1 - \frac{(1-\tau)G}{1-\varepsilon}\right), \qquad x_H^{\tau} = \mu_r^{\tau}\left(1 + \frac{(1-\tau)G}{\varepsilon}\right). \tag{21}$$

Evaluated with the same effective social preferences, expected utility under redistribution is

$$\mathbb{E}_r^{\tau}[u_L] = \mu_r^{\tau} - \mu_r^{\tau}(1-\tau)G\frac{d_r}{\varepsilon(1-\varepsilon)}. \tag{22}$$

In so doing, we incorporate the idea that a particular institutional choice entails choosing among bundles of jointly determined outcomes. Some institutional arrangements may generate high pre-redistribution inequality together with rapid growth, substantial mobility, and large spillovers; others may generate low pre-redistribution inequality while nevertheless pro-

[22] We note the example of Berggren (2026) when policies that reduce inequality may (not always) also reduce entrepreneurial entry and reduce positive spillovers.

[23] We want to be very clear that the restriction is not something implied to the theory we develop. For simplicity of exposition, we force the κ to be $\in [0, 1)$ but it could be allowed to be $(-1, 1)$ to reflect the possibility that redistribution is on net growth enhancing (see examples from Galor and Zeira (1993a) and Lindert (2022). In the discussion section below, we will elaborate on this possibility relying on how redistribution might be desired in fast-growth regimes where credit market imperfections exist.

ducing rapid growth, substantial mobility, and large spillovers. In those instances, there is not much trade-offs. However, others may generate high pre-redistribution inequality but insufficient growth, mobility, or spillovers to make that inequality tolerable, thereby generating demand for redistribution and producing a different post-redistribution distribution. Thus, there is no necessary mapping from the degree of pre-redistribution inequality to the attractiveness of an institutional arrangement. What matters is the entire bundle of inequality, growth, mobility, spillovers, and the consequences of redistribution generated by the rules under consideration.

For analytical convenience, let us define, for each regime r, an indifference threshold corresponding to the level of inequality beyond which the low-income individual finds redistribution preferable. This threshold is implicitly defined by

$$\mathbb{E}_r[u_L] = \mathbb{E}_r^{\tau}[u_L] \tag{23}$$

Let $G_{\mathrm{IIF},r}(\lambda)$ denote the corresponding inequality floor. For $G > G_{\mathrm{IIF},r}(\lambda)$, redistribution is demanded, whereas for $G \leq G_{\mathrm{IIF},r}(\lambda)$, it is not. Thus the floor is the level of inequality at which the low-income group is indifferent between tolerating the status quo and supporting a compressive policy that reduces the market-produced level of inequality but weakens the opportunity-generating process. Below that floor, the opportunity-generating process dominates redistribution and thus there is no demand for the latter. Using (18) and (22), the condition $\mathbb{E}_r[u_L] = \mathbb{E}_r^{\tau}[u_L]$ becomes

$$\mu - \mu G \frac{d_r}{\varepsilon(1-\varepsilon)} = \mu_r^{\tau} - \mu_r^{\tau}(1-\tau) G \frac{d_r}{\varepsilon(1-\varepsilon)} \tag{24}$$

Substituting (20) and solving for G yields

$$G_{\mathrm{IIF},r}(\lambda) = \frac{\kappa_r(\lambda-1)\varepsilon(1-\varepsilon)}{d_r\left[\lambda + (1-\tau)\kappa_r(\lambda-1)\right]}. \tag{25}$$

Using (5), this can be written as

$$G_{\mathrm{IIF},r}(\lambda) = \frac{\kappa_r \varepsilon \lambda}{d_r\left[\lambda + (1-\tau)\kappa_r(\lambda - 1)\right]} G^*(\lambda). \tag{26}$$

This produces the comparative statics that follows. First, for fixed λ and τ, the inequality floor $G_{\mathrm{IIF},r}(\lambda)$ is increasing in κ_r and decreasing in d_r. Second, an increase in m_r lowers $\tilde{\alpha}_r$, which lowers d_r and therefore raises the floor. Likewise, an increase in p_r lowers d_r and raises the floor, provided that $\tilde{\Delta}_r > 0$.

The only necessary to arrive at non-empty feasible redistribution is that $d_r > \kappa_r \varepsilon$. This prevents that *every* biologically feasible inequality level becomes tolerable. In other words, there are *some* allocations wherein redistribution is attractive enough to warrant some alterations to initial distributions well before the biological ceiling of the IPF is reached. As such, within the ordering, $0 < G_{IIF} < G^*(\lambda)$, there are *some* allocations that are not tolerated. Thus, we can partition the space below $G^*(\lambda)$ in two:

$$\mathrm{Region}_r(G;\lambda) = \begin{cases} \mathcal{T}_r(\lambda) \text{ (Tolerated region)}, & 0 \le G \le G_{\mathrm{IIF},r}(\lambda), \\ \mathcal{R}_r(\lambda) \text{ (Redistribution region)}, & G_{\mathrm{IIF},r}(\lambda) < G \le G^*(\lambda). \end{cases} \tag{27}$$

Which gives us the demand for redistribution in regime r be

$$D_r(G,\lambda) = \begin{cases} 0 & \text{if } G \le G_{\mathrm{IIF},r}(\lambda), \\ h(G - G_{\mathrm{IIF},r}(\lambda)) & \text{if } G_{\mathrm{IIF},r}(\lambda) < G \le G^*(\lambda), \end{cases} \tag{28}$$

where $h : \mathbb{R}_+ \to \mathbb{R}_+$ is continuous, strictly increasing, and satisfies $h(0) = 0$.

3.4 Institutional Choice

Figure 1 illustrates the model we derived above. For simplicity, we will first start with "low" and "high" quality institutions to distinguish between regime types in order to showcase

what unambiguous trade-offs would look like. High-quality institutions yield terms m, p and κ that are greater than for low-quality institutions. This implies $d_F < d_U$ (where F is high-quality and U is low-quality) which in turn implies $\tilde{\alpha}_F < \tilde{\alpha}_U < 0$. In other words, we assume that "high quality" simply dominates in all instances (making the trade-offs we will explain below easier to introduce). Ultimately, given these assumptions,

$$G_{\text{IIF},F}(\lambda) > G_{\text{IIF},U}(\lambda), \forall \lambda > 1 \implies W_F^T(\lambda) > W_U^T(\lambda) \qquad \text{and} \qquad W_F^R(\lambda) < W_U^R(\lambda) \quad (29)$$

Thus higher-quality institutions raise the floor through two channels. First, higher m_F and p_F reduce the effective slope d_F, making inequality less objectionable. Second, higher κ_F means redistribution destroys more of the opportunity-generating process, so compression is tolerated only at higher levels of inequality. In Figure 1, this is illustrated as two different activation marks. The core idea to extract is that for a given λ and ε there will be greater toleration for inequality in the high-institutional quality society. If both the societies pick policies that generate the same average income but the lower institutional quality one is more predatory, people will demand more redistribution in it.

While this is particularly evident now that we have exposed our model, what is less evident but far more important are the implications for the choice of institutions. Indeed, what our model does is set the mapping of preferences, constraints and trade-offs facing individuals. From this core, we can return to conventional analysis of institutional choice (and comparative institutional analysis which LPE rejects as being "law and economics").

To see this, one should be even more agnostic about the sub-indices F and U above. Rather, let us shift to i as sub-indices to remove any connotations of "good" or "bad" institutions. This allows trade-offs to be those that agents inside the model prefer. Any institutional arrangement becomes a particular bundle of d, κ, μ, and p that generate simultaneously G_{IIF} and G. But here, we assume bundles cannot be linear combinations of characteristics. There is lumpiness. This reflects the idea that institutional choices are more

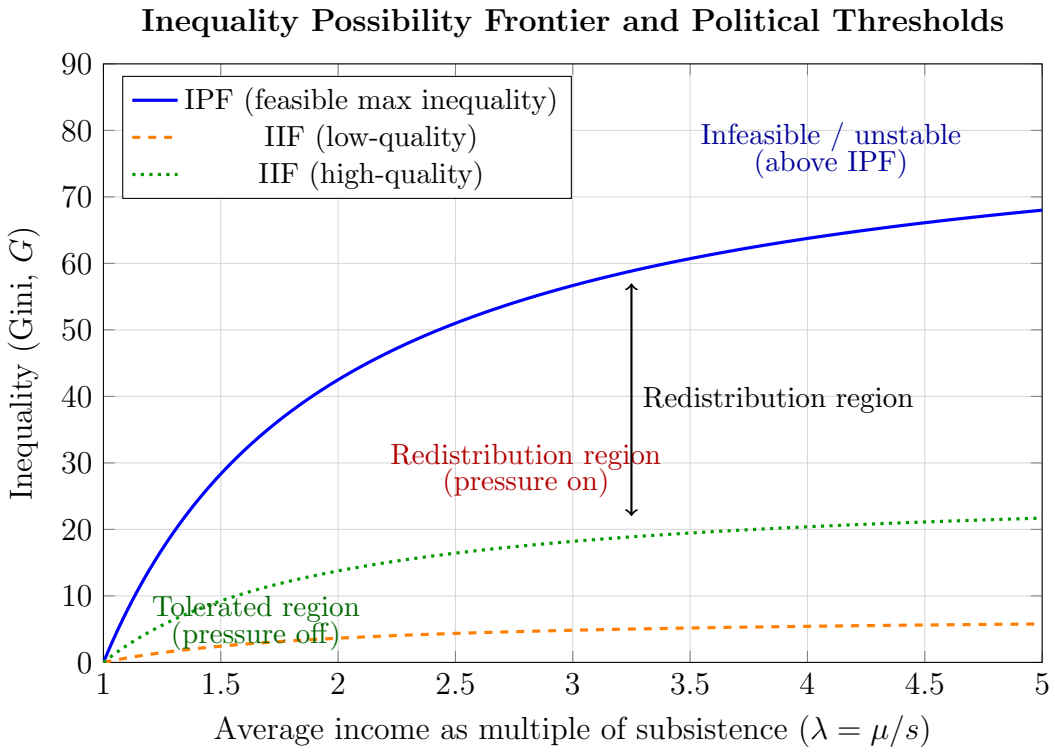


Figure 1: The solid curve is the inequality possibility frontier. The dashed orange curve is the intolerable inequality floor in the low institutional quality regime, and the dotted green curve is the floor in the high-quality regime. The high-quality regime has the higher floor. Therefore, more inequality is tolerated before redistribution turns on, and the region with active redistribution pressure is narrower. Calibration: $\varepsilon = 0.15$, $\tau = 0.50$, $\beta = 0.30$, $(\tilde{\alpha}_U, p_U, \kappa_U) = (-0.04, 0.01, 0.06)$, and $(\tilde{\alpha}_F, p_F, \kappa_F) = (-0.08, 0.04, 0.10)$. These imply $d_U = 0.1034$ and $d_F = 0.0452$, both of which satisfy $d_r > \kappa_r \varepsilon$.

often discrete than continuous such that it is impossible to mix and match the best *from* all worlds and one is forced to take the best *of* all *feasible* worlds even if it is imperfect and implies trade-offs.[24] Because all of these features are simultaneously chosen, the trade-offs must be weighed. In other words, the following implication emerges

$$\underbrace{\theta_i}_{\text{rules/institutions}} \longrightarrow \underbrace{(G_i, \mu_i, m_i, p_i, \kappa_i)}_{\text{economic consequences of rules/institutions}} \longrightarrow \underbrace{(d_i, G_{\text{IIF},i})}_{\text{evaluation/tolerance}} \longrightarrow \underbrace{D_i}_{\text{redistributive demand}}$$

The key linchpin of this simultaneous choice over institutions is that it means that *each* institutional bundle produces its own $G_{\text{IIF},i}$ as well as its own G_i (we cannot stress this enough). Recall that what defines G_{IIF} is $\mathbb{E}_r[u_L] = \mathbb{E}_r^{\tau}[u_L]$. This asks, given the opportunities, mobility, income, and consequences of redistribution generated by institution i, how much inequality can exist before the demand for redistribution activates. To see how, a small example of a discrete choice between the only two feasible institutional alternatives (A and B) will suffice. Choice A has the same inequality as B, but also higher income mobility ($p_A > p_B$) and larger spillovers to low-income classes ($m_A > m_B$), such that $d_A < d_B$. In this case, B has a larger utility cost of inequality and must have a lower IIF than A. This conclusion is only reinforced if A is a set of rules under which redistribution damages the process producing income (the cost κ_A). Individuals then require a fairly large inequality problem before accepting that sacrifice under A. Then $G_{\text{IIF},A} > G_{\text{IIF},B}$. But this can be reversed dramatically if a redistributive policy in A is relatively inexpensive. In this case, the floor for redistribution might even be lower than in B despite generating more mobility and spillovers.

Because of this setup, there is not automatic equivalence such that $G_{\text{IIF},A} > G_{\text{IIF},B} \not\Rightarrow A \succ B$. Treated as bundles, each arrangement jointly determines the level of inequality, the economic consequences attached to that inequality, and the cost of compressing it. The trade-offs between A and B are thus so multidimensional that people weigh their future (or

[24] See Geloso et al. (2026a) for such an application to public health outcomes and institutional choice.

children's) well-being resulting from the wealth of others *now* accounting for the costs of redistribution. Ultimately, what matters is the expected utility generated by the complete feasible bundle. It is thus entirely possible to see a high-income mobility society with high-inequality and a large welfare state (e.g., the United States) and a low-inequality society with low mobility and a larger still welfare state could also exist and both – given their respective alternatives – be deemed the best of all feasible choices. In other words, inequality itself offers little to nothing in and of itself in terms of economic information. Its "content" to people depends on all the institutional settings that generate it.

4 Discussion

We believe that this model offers considerable traction. Far more than any traction LPE can claim to have. First, it provides a rational choice analysis of institutions in relation to distribution and anchors the origins of redistribution in rational choice as well. No need for normative pre-commitments. Second, it squares quite well with empirical patterns that exist in the literature regarding inequality, income mobility, and institutions. We break our discussion into both sets of ramifications.

4.1 Efficiency, Distribution and Institutional Choice

It is useful here to reiterate the LPE framework to showcase the relevance and superiority of our model. The LPE critique is that efficiency is the only object of consideration in the paradigm of neoclassical/mainstream economics they wish to depart from. But that misses the point that efficiency choices *do* incorporate considerations over distribution and redistribution. Indeed, our model does exactly that whilst using an entirely positive framework that imposes none of our normative priors into the analysis.

If institutional choices are not continuous (i.e., not *à la carte*)[25] but rather discrete,

[25]Institutional reform regarding is not frequently *à la carte*. The French learned this when a modest and reasonable request for fiscal reform somehow came bundled with a republic, a new calendar, and a

then there is a finite set of choices: $\mathcal{I} = \{I_1, I_2, \ldots, I_N\}$ with $I_i \longrightarrow (\mu_i, G_i, m_i, p_i, \kappa_i) \longrightarrow (d_i, G_{\text{IIF},i})$. This discreteness reflects the logic of efficiency when transaction costs are accounted for. Any element I_i requires rules, and they must be defined, enforced, and policed/monitored such that a stable framework of exchange is secured – all of which fall under the logic of transaction costs. A common saying in the "efficiency" view criticized by LPE is that the institutions ultimately chosen maximize wealth *net of transaction costs* (Allen, 2011, 2013). Here, we merely tweak that expression to replace "wealth" with "living standards" to be more encompassing.

For example, an institutional choice that generates exceptional mobility and considerable positive spillovers onto the poor may rely on a system of property rights with little room for any transgression and which may also generate high inequality. One could of a Schumpeterian growth model as analogous to this. Innovators need to appropriate substantial shares of temporary monopoly profits to engage in innovative endeavors. While pre-redistribution inequality would be high, the arrangement might come with fast growth for all, very high inter-generational and intra-generational mobility in living standards. The key condition is that they must appropriate monopoly profits. For this choice to be made, rules must first be chosen to define property rights, second to secure the enforcement of those rights, and third to define punishments for their transgression.

All this requires *some* costs to be incurred. For our Schumpeterian economy, the analogy would be that business owners must have incredibly wide abilities to reconfigure their properties to appropriate the rents of innovation, and this could be thought of as the absence of antitrust legislation, for example, and also very low tax rates.[26] These rents may generate a desire by some parties to lobby politicians to ask for some redistribution which, if acquiesced to, would eliminate the drive to innovation. Thus, enforcement is necessary for this bundle to be chosen. The question becomes how costly it is to transact between parties (the L and H in our setup) to arrive at a mutually beneficial arrangement. If there is an alternative

considerably smaller elite ε. The choice was thus more discrete than continuous.

[26]This is consistent with economic history work by Smythe (2010).

bundle available that offers *some* redistribution scheme but stronger property rights such that transaction costs are lower than in our "Schumpeterian" example, then that bundle is superior *because* it maximizes living standards *net of transaction costs*. If there is an alternative bundle that offers the "Schumpeterian" example with lower inequality but it cannot be enforced because transaction costs are too high, then it cannot be chosen.

This is more powerful than it may appear at first sight. Since we are stating that you cannot modify *only* an undesirable characteristic such as G_i without changing the *whole* set of institutions, changing one characteristic requires redefining rights, identifying what is subject to redistribution, establishing systems for monitoring compliance, adjudicating disputes, and preventing avoidance. The bargain that emerges is a series of political exchanges to secure an agreement that maximizes living standards net of transaction costs. This means that both the IIF and the observed level of inequality are products of the institutional bundle. Actors negotiate between arrangements based on the standard transaction costs analysis. This is the standard analysis but made richer with considerations of distributions (post and pre). Thus, the claim by LPE scholars that the "efficiency" view fails to consider distribution and redistribution is patently incorrect.

In fact, we can go one step further in the conceptual analysis here. A joke allows us to convey the point by way of analogy: Louis XVI might have had preferences over institutional arrangements too, but Maximilien Robespierre and company did come into possession of a rather effective and sharp veto. The consideration of inequality is easily extendable to inequality in the ability to produce violence (which we see as synonymous with power and so LPE scholars). Suppose that there are three choices of institutional bundles: A, B, and C. Let us also assume that the population ε is small such that there is a small elite and a large lower class. In the aggregate, it could be that the expected utility of each arrangement is such that: $A \succ B \succ C$. However, the small elite has the following preference order: $C \succ B \succ A$. If the elite has sufficient coercive power to enforce its preferences by sending troops against mobs and the costs of resisting the elite are too high for the lower classes, then the latter

will implicitly acquiesce to C. This becomes a transaction cost problem since the elites have the *lowest* transaction costs to make choice C stable by credibly menacing the lower classes. Thus, because the cost organizing, coordinating, resisting, and enforcing A are sufficiently high for the non-elite, their preferred institutional arrangement is not implementable. The implicatinon is that C is the stable equilibrium because no coalition is capable to form to replace it (Telser, 1987). To stress the point further, imagine that the lower classes see a lowered cost of organizing their own movements. The reductions makes them able to credibly threaten to hang elite members from street lanterns with hay in their mouths[27] unless an alternative arrangement is reached. This might shift the choice to B rather than C such that no one gets their first choice. But this is the same as saying that we should factor in transaction costs of forming coalitions when considering institutional choices.[28]

This is nothing more than conventional economic analysis of institutional choice in the presence of transaction costs. We only reshaped it to incorporate considerations of distribution. To belabor the point, everything that was described above can be read in terms of transaction costs. An elite possessing substantial coercive capacity can lower the private cost of enforcing rules favorable to itself while simultaneously raising the cost to other groups of resisting, renegotiating, or replacing those rules. Thus, while the bundled in the set $\mathcal{I}$ come with their respective outcomes, the choice of which element is selected can be 100% explained with the conventional rational choice analysis of institutional design. It is just that parties are now allowed to factor in considerations about distributions (post and pre).

This is where we can judge the LPE framework to be wholly worthy of dismissal. In their framework, an observed undesirable institutional characteristic (e.g., high inequality) is immediately judged as a sign of poor performance that mainstream economics cannot explain. To them, the initial distribution of rights cannot be analyzed by standard economics. The question of why A and B bundles possess their respective power positions for members cannot

[27]This is a reference to French revolutionary practices.

[28]This is closely related to the political-power distinction in Acemoglu and Robinson (2008): institutions are determined through the exercise of de jure and de facto political power, and de facto power can include coercive capacity. Their models explicitly consider labor repression and elite use of paramilitary force.

be answered within conventional economic analysis. Britton-Purdy et al. (2020) explicitly say that the traditional focus on transaction costs and externalities displaced questions about how law creates unequal bargaining positions. But that is wholly untrue, and it is based on either a misunderstanding or a shallow reading of what is being critiqued. Our point is that the transaction-cost approach can incorporate precisely that question, and this is what our model does. Because if $I_i \rightarrow (\mu_i, G_i, m_i, p_i, \kappa_i)$, then the distribution of income and bargaining opportunities is itself an endogenous characteristic of the institutional arrangement. Nothing in rational-choice institutional analysis requires taking the initial distribution as fixed via law.

What is more, *none* of the LPE framework is required, as it adds absolutely nothing that the rational-choice framework cannot. For example, Grewal and Purdy (2014) say that markets are products of legal choices. For them, the law mediates conflicts between "market imperatives" (p. 1) and "democratic demands" (p. 2) for redistribution, fairness, and justice. That markets are the product of "law" (in the broadest sense possible, to include norms, self-regulation, private governance, and legislation by government—see Hasnas (2024)) is not disputed. Indeed, Ronald Coase stated that "the provision of markets is an entrepreneurial activity and has a long history," and it is what the "law" tries to allow for—the provision of markets. In fact, the entire analysis of institutional choice is about this task (Greif, 2000). Thus, the first part of the LPE claim is entirely redundant with standard economics. But the second part is *ad hoc* and only the result of the normative commitments LPE scholars want to make. Theirs is a creation (assumption even?) of people's preferences[29] within a system with no trade-offs and no constraints. In doing so, the answer they provide to how institutions determine who gets what and who has power over whom is baked into assumptions about preferences that are exogenously imposed by them. This supports their

[29]We could be ungenerous and make the argument that these are rarely documented empirically in their work and are more often taken in ways that fit their priors. They ignore findings at odds with their framework. But that would be too easy. Way too easy. We prefer to point out that not one part of their framework adds anything to the study of inequality in relation to institutions. It is either superfluous, *ad hoc*, unnecessary, or ends up explaining *less* rather than more.

entire normative framework and allows them eventually to eschew a positive framework.

But then the puzzle emerges: why does person L demand redistribution (and obtain it) under choice I_A but tolerate greater inequality under choice I_B? Thus, while it does offer normative objections to inequality, it fails to provide any positive explanation for distribution and redistribution. In contrast, our extension of standard economic models to considerations of distribution allows us to answer all of their questions about the initial distribution, the existence of markets (as per the Coase quote above), and the demand for redistribution (i.e., not preferences, but actual demand), while remaining within the framework of transaction-cost analysis.

In fact, our positive framework offers far richer normative implications without having them drive the results. The first is that someone with the same *normative* commitments as LPE scholars could use our model. For example, Britton-Purdy et al. (2020) are very open about wanting to orient legal analysis toward equality, self-rule, and anti-subordination. But, in our example above, the ability of the lower classes to resist oppression by organizing more cheaply against subordination is the key determinant of securing such outcomes. One of the authors of the present paper showed, for example, that market integration in Lower Canada (modern-day Quebec) from the 1810s to the 1830s allowed a rich commercial infrastructure (physical and network-based) to emerge in opposition to well-established legal regimes of land tenure. This infrastructure could be repurposed for rebellious activities against British rule in the colony and the landed elite allied with British authorities. In practice, this was an instance in which lower transaction costs outside the elites facilitated a challenge to the established institutional order. This infrastructure (measured by the depth of market integration) explained anti-regime activities in the 1837–38 rebellions (Geloso and Kufenko, 2019). While the rebellions themselves were ultimately unsuccessful, they did pave the way for a wave of political reforms that included the abolition of the landed elite's land-tenure regime, which gave it strong monopoly and monopsony rights on its estates (Geloso and Lacombe, 2016; Geloso, 2020; Geloso et al., 2023). Here, an anti-subordination effort *is* made

possible because the cost of challenging the existing order falls, and this can be explained within our framework. One could easily make the claim that the resulting outcome was normatively superior to the one that existed before. However, that normative judgment is made independently of the positive explanation of why institutional change occurred (and greater equality was produced), rather than being embedded in the assumptions used to generate that change.

This criticism of the LPE framework connects with other criticisms of LPE contained in papers for this special issue. Most notably that of Harris and Leeson (2026) who argue that LPE makes a normative pre-commitment to ideals (which the present authors here actually share) regarding constraining power in order to make a neutral claim and that those pre-commitments are not necessary. Indeed, it is *exactly* because law involves power and discretion that we need rational choice analysis to understand how it is designed. The pre-commitment is not necessary. Our framework is able to make sense of the fact that institutions are neither neutral nor exogenous, but are themselves objects of choice among agents with heterogeneous interests, unequal capacities for organization, and different costs of enforcing or challenging alternative rules. And this makes it possible to ask normative questions about the value of constraining political power (and its wielders) thanks to impersonal and general rules that are predictable. Indeed, if power implies discretion over rules if one group can use its coercive power (i.e., lower transaction costs of exerting violence) against another, then our model explains what one could try to do to change the equilibrium. The ability to rebel against rulers is one way (Leeson and Suarez, 2016; Geloso and Kufenko, 2019)[30], the ability to move elsewhere and escape bad elites (Vahabi, 2016a,b; Weingast, 1995), the ability to hide resources from rulers (Desierto and Koyama, 2026), and the ability to barter more cheaply between parties to rearrange property rights[31] (Alchian, 2006a,b,c;

[30]In sufficiently extreme cases, this may force elites to re-bargain to improve outcomes for the lower classes either through more income mobility or through redistributive schemes. The French experience suggests that this might happen when lower classes can remind the upper classes that lamp posts and cords are also a form of public infrastructure.

[31]One might even go as far to say that when the transaction costs of renegotiating the institutional order fall sufficiently far, the bargaining table can begin to resemble the Place de la Révolution.

Geloso et al., 2026c) are all ways that normatively superior bundles could be secured. Indeed, even theorists like Leeson (2020), who are presented as "efficiency, always" apostles, accept the point that arriving at normatively more desirable outcomes only entails finding ways to change the constraints.[32] This can occur through any of the channels discussed above, and it is here that we can move to the empirical connections that can be made.

4.2 Empirical Connections

Indeed, if our positive framework for thinking about institutions and distributional concerns is superior because it is more economical—requiring fewer assumptions—while also offering greater explanatory power—allowing more phenomena to be explained within the same framework—then what normative implications emerge from it in the process?

Our framework suggests that people might trade off higher inequality now for greater income mobility over time. Inside the Becker and Tomes (1979) framework for income mobility, especially if there is fast economic growth, high inequality could be tolerated when it generates growth and greater opportunity. This is consistent with three sets of findings in the literature. The first is that income mobility *is* associated with tolerance for inequality. Shariff et al. (2016) find a "cross-national comparison showing that income mobility is associated with tolerance for inequality and experimental work demonstrating that perceptions of higher mobility directly affect attitudes toward inequality" (p. 373). Alesina and La Ferrara (2005) made a similar finding some years earlier and revisited it later with cross-country and experimental evidence (Alesina et al., 2018). Second, there is a smaller corpus of empirical literature that associates faster economic growth in general with lower demand for redistribution (Blekesaune, 2007; Jæger, 2013; Martén, 2019). Both patterns are consistent with our model. People may accept the level of inequality as being part of the bargain for greater mobility or greater economic growth (via spillovers, for example), which then affects their demand for redistribution.

[32] And scholars less inclined towards this efficiency-always view would agree with the claim (Chenoweth, 2023).

Another important connection to empirical findings is the growing literature connecting economic freedom (i.e., how open markets are and how secure property rights are) and income mobility (Dean and Geloso, 2022, 2024; Callais and Geloso, 2023; Callais et al., 2025, 2024a,b; Geloso et al., 2026b). These studies find that economic freedom promotes greater income mobility—both in terms of moves along the ladder and in terms of increases in absolute living standards across and within generations. They also look at setups that are more causal to see if large reforms that liberalize the economy lead to greater mobility and conclude in the affirmative (albeit with intragenerational mobility figures as the dependent variable). They also find that it changes poverty dynamics by reducing cases of persistent poverty (multiple years below the line) and resistance to poverty (never falling below the line). But most importantly, they find that economic freedom generally has a stronger positive association with income mobility than inequality's negative association. Bear in mind that, inside the Becker and Tomes (1979) model and corollaries such as Galor and Zeira (1993b), inequality *must* reduce mobility when there are strong borrowing constraints such that the poor cannot seize opportunities. That finding suggests that where markets are more open and property rights are more secure, the constraint-associated effects of inequality are being minimized and overpowered such that, on net, there is more mobility than if inequality were reduced to limit the borrowing-constraint issues. The important implication is that the mobility consequences of inequality are themselves institution-dependent. Where markets are more open and property rights are more secure, the mechanisms through which inequality generates persistence—such as restricted access to credit, investment, entry, or other opportunities—appear substantially weaker. The institutional effect can therefore dominate the negative association between inequality and mobility, precisely as our model allows.

All three findings connect with our claim that LPE imports normative considerations to make positive descriptions (with a critique of an alternative they did not fully understand) that are actually *less* descriptive than our model. Inside their framework, inequality is

primarily interpreted through the institutional allocation of resources, bargaining power, and political power. What is missing is a positive mechanism explaining why individuals facing the same observed inequality may evaluate it differently depending on the mobility, growth, and spillovers generated by the institutional order. In other words, their framework can explain why rules produce different distributions, but it does not explain why the same distribution can generate radically different demands for redistribution across institutional environments. Our model does precisely this through p_i, m_i, and ultimately d_i and $G_{\text{IIF},i}$.

In fact, their model is even less able to deal with some extreme cases and cannot make sense of them because they contradict it. For example, despite decades of growing income, people in the former East German Republic are still more supportive of redistribution and state intervention than West Germans, even after controlling for individual characteristics (e.g., income) (Alesina and Fuchs-Schündeln, 2007; Bondar and Fuchs-Schündeln, 2023). Similar evidence exists for Central Europe in general following the collapse of the USSR (Libman and Popova, 2023). Measuring redistribution as the reduction in the Gini coefficient produced by taxes and cash transfers for 146 countries since 1960, Kammas and Sarantides (2019) find that dictatorships appear to engage in more direct fiscal redistribution than democracies (i.e., relying heavily on outright cash transfers).[33] This is true *after* controlling for income (i.e., λ being held constant). Why would dictatorships redistribute more? Under our framework, dictators understand that, to remain in power, they must sacrifice some of their rents to stave off alternative coalitions. In practice, this means that the trade-off incorporates a lower inequality tolerance floor (i.e., IIF). This is consistent with the fact that while dictatorships have more redistribution, they also exhibit less income mobility across generations, as our model's trade-off implies. The difficulty for LPE is not that authoritarian redistribution is impossible to rationalize ex post. Almost any observed policy can be redescribed as reproducing, legitimating, or contesting power. The difficulty is that the framework provides no positive mechanism generating a prediction about when

[33] In contrast, they find that democracies redistribute through public services such as health care and schooling.

an unequal and hierarchical institutional order redistributes more rather than less. Our framework does.

Our model also has one important feature that helps connect it to the empirical literature. By creating the IIF, we incorporate the idea that inequality may generate costs. Some might be tempted to conclude that this is because it generates disutility for the poor, but it need not be. It can also generate disutility for the elites. If the rich exert power in the institutional arrangements and the transaction costs of the poor organizing are too high to make other arrangements feasible, it does not mean that the rich do not pay a cost. Discontent with an arrangement may require the rich to hire resources to guard against defection. Samuel Bowles (2012) pointed out that this may take the form of the rich hiring more security guards and supervisory labor because it comes with distrust. There is a genuine cost to using resources to nullify threats, as they could be used to produce *other* things. Bowles and Jayadev (2006) showed that inequality correlates with guard labor in ways that exemplify these extra costs.[34] Our model can be thought of as connecting to the empirical findings of Bowles (2012) and Bowles and Jayadev (2006).[35]

And finally, all these connections to empirical findings give us our normative considerations without, as LPE scholars do, starting from them. If one sets as his standard the improvement of the living conditions of the poorest, then one should look at ways to alter constraints on political bargaining to open up options that generate combinations that increase their living standards the most. That could mean combinations that have a bit more inequality but far more mobility and far faster year-to-year growth. It could also mean combinations that reduce inequality (to alleviate borrowing constraints such as in the Galor

[34]We note that Geloso and Kufenko (2017) disagreed with whether this was empirically correct in this case. However, Geloso (2019) later explained elsewhere that he thinks the essence of Bowles' theoretical insights is correct and that the argument is probably empirically relevant, which highlighted a narrower disagreement with Bowles and Jayadev (2006).

[35]As a further sidenote of interest, the authors of the present paper are definitely inside what could be dubbed the classical liberal family, whereas Bowles is far closer to the progressive left family. Yet, as if to illustrate the attachment to a positive framework first, from which we can later read normative desires, we agree with *all* of the positive framework of Bowles. In fact, the idea for this paper began *with* reading Bowles and being amazed at a non-normative theory of why people find trade-offs in inequality levels.

and Zeira (1993b) model) and increase mobility and growth a bit less. In fact, one of the authors in the literature connecting economic freedom to income mobility finds that some components of economic freedom matter far more than others. Secure property rights and limited regulation were generally highly important to income mobility. However, government spending to individuals did not seem to generate any significant association (Callais and Geloso, 2023). Now, this could be because transfers help by pushing people up while the taxes needed to fund them discourage effort, which cancels out the effect. But it is pointed out that these results were based on *all* government spending (inclusive of government procurement contracts) rather than individual programs (Dean and Geloso, 2024). Some work, such as that of Lindert (2022), suggests that many types of social transfers are not inimical to growth in general and are definitely positive in pushing the poor up. Thus, there could be institutional bundles that rely on highly secure property rights, limited regulation, and open trade with a particular welfare state (Friedman et al., 1962; Boyer, 2023). Andreas Bergh (2020) argues that Sweden has such a type of institutional arrangement, which he calls a "Hayekian welfare state." But why don't countries like Canada or the United States have that too? Because the political constraints make it so that this configuration is unfeasible without a wholesale reform of the entire set of institutions. If a Canadian or American were to believe that Bergh's description of a Hayekian welfare state offers the normatively superior outcome, then he would have to work to alter constraints in ways that make it feasible as a bargain. Now notice that, unlike LPE, the normative consideration came last, not first.

5 Conclusion

The Law and Political Economy (LPE) project argues that we should consider how institutions (and law) shape markets in ways that affect distributions of wealth and income. That distributions cannot be understood independently of the rules that shape markets is so true that it borders on a triviality that we see no point in contesting. However, from that

entirely reasonable statement, they see a justification for departing from conventional economic analysis because it "fails" to explain power structures and the reproduction of existing distributions. We see no reason for this. Rational-choice institutional analysis already allows rights, bargaining positions, income distributions, mobility, and redistributive policies to be endogenous to the institutional environment. However, unlike LPE, it requires no normative pre-commitments to equality, anti-subordination, and democratic control *before* producing positive analyses.

Two mistakes happen. The first is that positive explanation and normative evaluation are collapsed into one another. The framework predicts little because the answer is effectively contained in the premises: institutions that generate unequal power are objectionable because unequal power is taken to be objectionable. The second is that it fails to understand in depth what it criticizes and thus misses the target.

These two mistakes end up costing a lot. By folding the normative priors into positive explanation, the answer is contained within the premises: institutions that generate unequal power are objectionable because unequal power is objectionable. A platitude of little meaning that is unable to explain what content individuals attach to a given distribution. In the LPE framework, a more income-egalitarian society is preferable to a less egalitarian one because of the unequal power it supposedly reveals. However, if the less egalitarian one offers more growth, more income mobility, is democratic with strong anti-subordination norms, and has little status based on wealth, then the LPE framework is unable to explain this. If two equally (and highly) democratic societies, with equally strong anti-subordination norms and little wealth status, show different levels of mobility, growth, and inequality, LPE again fails to explain.

Our framework suffers from no such flaws and requires no normative pre-commitment. It shows that the trivial statement that distribution cannot be evaluated independently of the process generating it is indeed correct. However, it also shows that economic analysis along very standard lines can show that institutional arrangements jointly determine inequality,

average income, mobility, spillovers, and the costs of redistribution. They therefore determine not only G_i, but also $G_{\text{IIF},i}$: the amount of inequality individuals are willing to tolerate before demanding redistribution. From this, potent ramifications exist for why and when variations in redistribution by governments would exist. As such, the same observed inequality can consequently have very different welfare and political meanings under different institutional arrangements.

Once this map of trade-offs over institutions is introduced to consider distributions, standard transaction-cost analysis can explain why certain institutional choices are picked over others and what would cause shifts to alternative institutional choices. The normative points that one cares to make emerge out of an entirely positive analysis. No need to pre-import them.

At this point, let us state our own normative preference. We like institutions that are impersonal and treat the poor with dignity by giving them the same rights as the wealthy and giving the latter no privileges. Our standard of choice in judging which ones we deem preferable is whether they generate mobility such that rags-to-riches stories occur, the entire ladder grows, vulnerability to shocks (being thrown back into poverty) falls, there are spillovers such that the success of some feeds the success of others, and there is economic growth for all. In a way, what we want is a "lean and mean egalitarian growth machine" (Geloso, 2027). To get that machine, our framework says that "what ought to be done" (to quote the favorite author of early 20th-century Russian socialists) is to influence the constraints tied to political exchange to allow for bargains over rules that generate these outcomes.

In a way, and this is where we allow ourselves to be rough, LPE offers one of the most condescending explanations of what the poor should want. It tells them that what they ought to care about is what follows from the theorist's own normative priors regarding inequality, hierarchy, and power. Suppose that the poor willingly accept greater inequality—that is, a greater distance between themselves and the rich—because the institutional arrangement

generating that inequality also produces larger spillovers for them, greater mobility possibilities for themselves and their children, and faster improvements in their absolute living standards. Indeed, even if they fail to move up the ladder, sufficiently rapid growth may continuously raise the floor to which they can fall, making failure less damaging over time. In such a case, the LPE response amounts to telling them: stuff it, like what we say you should like. The theorists know better than they do what dimensions of their economic condition they ought to value. The uncomfortable analogy here is with what William Easterly (2025) criticizes as the "violent savior" mentality. The violent savior does not merely claim to want to improve the condition of poorer people. He claims the right to substitute his own conception of what constitutes improvement for theirs, treating the supposed beneficiaries as objects to be improved rather than as agents capable of evaluating trade-offs for themselves. The poor are assumed to have no right to consent to the outcomes they have (Easterly, 2021). Their own preferences, choices, and willingness to accept trade-offs cease to matter whenever these conflict with the savior's prior conception of the good outcome.

By relying on a model constructed on *their* normative pre-commitments, LPE scholars are being "violent saviors" who say that the poor have no right to consent to their development. Ironically, they reproduce the very structure of power they so despise. In contrast, our framework makes no claim about what the poor should want. Our framework says how, if the poor want a new option to consent to, they should go about altering the game of political exchanges. We do not claim to know, nor would we be so morally presumptuous as to say anything more than that.

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