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# **The Wellbeing of the Australian People: Comments on the Treasury's Framework**

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# The Wellbeing of the Australian People: Comments on the Treasury's framework

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**'The methodological principle at the basis of economic science and which distinguishes it from other sciences, is the reference which it makes to a measure, mainly money.'**  
Ian Castles (1998: 141), quoting AC Pigou, with evident approval

## 1: Introduction

The Australian Treasury has enunciated its Strategic Framework 2011-12, a central element of which is entitled 'The wellbeing of the Australian people' (TWOTAP, reproduced below). The TWOTAP framework has been around since 2004, and has not changed greatly. It provides a checklist of five dimensions that 'reinforce our conviction that trade-offs matter deeply, both between and within dimensions'.

However, by offering a checklist only, but no clues as to how Treasury deals with trade-offs, Treasury has abrogated its responsibility to provide a useful guide to its decisions and advice. Treasury signalled this dereliction of duty, back in 2004, and repeated since:

'Consistent with being primarily a descriptive tool, rather than a framework for more formal analysis, the set of dimensions are not designed to meet more formal analytic criteria, such as being comprehensive, unique or independent.'

For those outside Treasury, the checklist is almost completely useless (or worse): it does not permit outsiders to test the appropriateness of any specific Treasury recommendation or series of recommendations. For those inside Treasury, the existence and standing of the checklist should be a source of confusion and dissension. The 'Wellbeing' checklist can justify Treasury's advocacy of almost any plausible policy, because TWOTAP is a checklist, pure and simple.

A simple checklist can provide a useful guide for consistent and rigorous decisions in some instances. For example, an airplane remains on the ground unless the pilot is assured that every item on the pre-flight checklist has been ticked off: no trade-offs are permitted amongst the items. But generally, something more than a simple checklist is required. Businesses, for example, are urged to use the triple bottom line of people, planet, and profit, yet everyone knows that if profits are persistently absent or low, the business may be taken over or go kaput. Thus the profit ranks above the

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other two, in a lexicographical ordering. Also, viable businesses must be willing to consider trade-offs between the items in the 3P checklist; and that requires placing some relative valuations or ‘weights’ the various items, when used to form an index of performance.

Neither ordering nor weights is found in TWOTAP. Two defects follow. Firstly, it is impossible to show that wellbeing has improved, unless there is an improvement in every single dimension of the checklist. Otherwise, no summary statement about wellbeing can be made: when some items improve and some worsen, then TWOTAP offers a description, but no resolution. Secondly, TWOTAP provides no basis upon which to choose between alternatives that both show improvements over the status quo in every dimension, but different improvements. It is not enough to say that consideration of the dimensions ‘provides the broad context for the use of the best available economic and other analytical frameworks, evidence and measures,’ without indicating what evidence, what measures, and what overall criterion.

Moreover, the same comments apply to each of the five items in the TWOTAP checklist: without a lexicographical ordering or a set of weights, there is no way to tell if wellbeing has improved in any one of the five ‘dimensions’.

As presented, TWOTAP is incapable of providing ‘a consistent basis’ for Treasury advice about trade-offs. However, I hope that there is evidence to the contrary. I assume that Treasury presents the Treasurer with a recommendation, and not merely a summary of the completed TWOTAP checklist. Therefore, in order to give Treasury credit for consistency, it is necessary to assume that Treasury does have a lexicographical ordering of the five dimensions (and within each), or that Treasury does have a consistent set of weights for the five dimensions (and within each)—but chooses not to reveal these to the world.

## **2: TWOTAP**

For ease of reference, here is a copy from the Treasury website (emphasis and note 2 added):

### **THE WELLBEING OF THE AUSTRALIAN PEOPLE**

In undertaking its mission Treasury takes a broad view of wellbeing as primarily reflecting a person’s substantive freedom to lead a life they have reason to value.

This view encompasses more than is directly captured by commonly used measures of economic activity. It gives prominence to respecting the informed preferences of individuals, while allowing scope for broader social actions and choices. It is open to both subjective and objective notions of wellbeing, and to concerns for outcomes and consequences as well as for rights and liberties.

Treasury brings a whole-of-economy approach to providing advice to government based on an objective and thorough analysis of options.

To facilitate that analysis, we have identified five dimensions that directly or indirectly have important implications for wellbeing and are particularly relevant to Treasury.

These dimensions<sup>2</sup> are:

- The set of opportunities available to people. This includes not only the level of goods and services that can be consumed, but good health and environmental amenity, leisure and intangibles such as personal and social activities, community participation and political rights and freedoms.
- The distribution of those opportunities across the Australian people. In particular, that all Australians have the opportunity to lead a fulfilling life and participate meaningfully in society.
- The sustainability of those opportunities available over time. In particular, consideration of whether the productive base needed to generate opportunities (the total stock of capital, including human, physical, social and natural assets) is maintained or enhanced for current and future generations.
- The overall level and allocation of risk borne by individuals and the community. This includes a concern for the ability, and inability, of individuals to manage the level and nature of the risks they face.
- The complexity of the choices facing individuals and the community. Our concerns include the costs of dealing with unwanted complexity, the transparency of government and the ability of individuals and the community to make choices and trade-offs that better match their preferences.

These dimensions reinforce our conviction that trade-offs matter deeply, both between and within dimensions. The dimensions do not provide a simple checklist: rather their consideration provides the broad context for the use of the best available economic and other analytical frameworks, evidence and measures.

### **3: A checklist for confusion and inconsistency**

Any decision made by Treasury can be justified by TWOTAP, unless it can be shown to worsen wellbeing in all five dimensions: narrower opportunities, worse distribution, less sustainable, more risk, and more unwelcome complexity. Using only a checklist, it is logically impossible to justify the choice of one situation over another, without employing some weighting system or rank ordering (e.g., of the kind that economists call ‘lexicographic’: for example, filter first by ‘opportunity’; then by distribution; then by sustainability; and so on).

Because TWOTAP offers no ranking system or weighting system, it cannot guide Treasury consistently across time and across policy decisions. As this is my main criticism of TWOTAP, I will dwell on it further.

When an agency is charged with dealing with a series of complex decisions, it is common (and good practice) for a set of criteria or guidelines to be enunciated. Such guidelines are most valuable when they constrain otherwise unbridled and possibly capricious discretion.<sup>3</sup> Good guidelines provide the principles that inform decisions

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<sup>2</sup> For comparison, the 2004 dimensions were: ‘(i) the level of opportunity and freedom that people enjoy; (ii) the level of consumption possibilities; (iii) the distribution of those consumption possibilities; (iv) the level of risk that people are required to bear; and (v) the level of complexity that people are required to deal with.’ The reference to ‘consumption’ has been replaced with ‘opportunities’; (ii) becomes ‘sustainability’, which was one element in the original (ii); and the order has changed, with distribution coming into second place.

<sup>3</sup> Phillip Pettit has argued for the possibility of ‘group agency’, of collectives that can reasonably be attributed with minds of their own, discontinuous with the mentality of the members: see for example, ‘Groups with minds of their own’, in

and, especially, establish presumptions that clearly place the onus of proof. Take, for example, the (old) ACCC guidelines on mergers. The impact on competition was considered first, with the presumption that more competition was to be preferred over less. Thus, the onus of proof for approval of an anti-competitive merger rested with the applicants—show that the merger was in the ‘public interest’, even though competition would be reduced.

TWOTAP provides no such presumptions. ‘Opportunities’ comes first: but there is no indication that, if a proposal does not satisfy that criterion, then it is presumptively ruled out—unless a very strong or special case is made in some other dimension. There is no indication that we should place any significance on the order in which the dimensions are listed in TWOTAP.

It is one thing to assert about TWOTAP that ‘These dimensions reinforce our conviction that trade-offs matter deeply, both between and within dimensions.’ It is quite another to make those trade-offs without a lexicographical ordering, or without using weights, explicitly or implicitly.

Senior Treasury officials may plead that they exercise their informed and experienced judgment, not only in the assessment of matters that are difficult to measure (like sustainability, or unwanted complexity), but also when making an overall assessment. However, such an overall assessment can be no more than applying unannounced, unarticulated and ad hoc weights or ordering to the various items on the checklist.

It must be splendid within Treasury for those with bees in bonnets: you may lose many a battle, but never mind—eventually you will win the day, under TWOTAP. I can imagine the conversation now: ‘For today’s policy issue, the most important question is unwanted complexity of choice—in which I happen to be expert. For yesterday’s policy issue, you argued that distributional considerations were trumps; the day before, it was sustainability; and before that, it was distribution. Well, today it is complexity.’

I would rather Treasury use this checklist than that it aim, for example, to maximize the growth of GDP or GDP per head; or to improve the re-election prospects of whoever happens to be in government at the time; or to maximise the salaries, status and power of Treasury officials; or to maximize the incomes of capitalists or the incomes of members of trades union. Nonetheless, TWOTAP is unbecoming.

Further, well-functioning agencies periodically review their guidelines (or have them reviewed). How have they worked in practice? Have they been followed? Consequently, how should they be changed? I found no evidence of such inquiries. However, the internal ‘Strategic Review of the Treasury’ (dated December 2011) suggested that the wellbeing framework was not being applied consistently across the department; and that SES staff thought that allocation of scarce Treasury resources between competing ends was ‘one of our weakest capabilities.’<sup>4</sup> Moreover, the

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FF Schmidtt, ed. *Socializing Metaphysics: The Nature of Social Reality* (Rowman and Littlefield).

<sup>4</sup> The ‘Strategic Review of the Treasury’ (December 2011), was conducted internally, with an external reference group. Apart from an Appendix

Independent Review of the Australian Government’s Regulatory Impact Analysis Process<sup>5</sup> noted that Treasury has a long list of items requiring Post Implementation Reviews (because no RIS was conducted), which suggests that TWOTAP may have been used extensively, instead of a RIS.

#### **4: The TWOTAP items themselves**

What follow are comments on each of the five dimensions of TWOTAP, focussing on measurability and trade-offs.

##### **Set of opportunities**

The set of opportunities available to people. This includes not only the level of goods and services that can be consumed, but good health and environmental amenity, leisure and intangibles such as personal and social activities, community participation and political rights and freedoms.

Let me assume that, for this dimension, Treasury mostly relies on an index; otherwise, I cannot guess how Treasury goes about its assessment of whether or not, the set of opportunities available to people has expanded or contracted.<sup>6</sup>

Conventionally, changes in the ‘set of opportunities’ are measured using an economic aggregate like Consumption, with the components valued at willingness-to-pay or cost; and with the valued bundle encompassing non-marketed as well as marketed goods and services. Every item mentioned in the second sentence quoted above, except ‘political rights and freedoms’,<sup>7</sup> can readily be accommodated within the extension of the national accounting framework offered, for example, by Tobin and Nordhaus (‘A Measure of Economic Welfare’, 1972): supplement the usual national aggregate for consumption, by accounting for leisure, for non-market activities, for health and longevity, and for externalities, including environmental damage. It is well

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reproducing the Wellbeing framework, the only relevant discussion I could find is in the Executive Summary: ‘Stakeholders generally consider that Treasury is a leader in applying rigorous economic and analytic frameworks to a variety of public and policy issues. A broad understanding of the Wellbeing Framework is an important part of Treasury culture and identity. In their responses to a survey conducted during the Review, SES considered that although the Wellbeing Framework is valued by staff, it may not be consistently applied across the department (p. v)... While the effective allocation of resources between competing priorities is seen by SES staff as one of the most important capabilities for the organisation, they regard it as currently one of our weakest capabilities’ (p. vii).

<sup>5</sup> <http://www.finance.gov.au/deregulation/docs/independent-review-of-ria-process.pdf>

<sup>6</sup> In a series of Treasury papers on TWOTAP, David Gruen (and others) have sensible things to say about the limitations of GDP (or NNI or national consumption) as a summary measure of aggregate or average wellbeing. However, the impression I got from reading them is that some national accounts aggregate—NNI or Consumption—plays a prominent part; but details are lacking.

<sup>7</sup> Note the absence of reference to economic rights and freedoms: politics is all?

known there are some difficulties of valuation of un-marketed goods and services.<sup>8</sup> Nonetheless, the approach is well understood and transparent. Unfortunately, the same cannot be said about the Treasury's TWOTAP.

In the Tobin-Nordhaus tradition, the weights given to the various items are the valuations of the individuals concerned, whether revealed in market transactions or inferred from objective evidence about subjective valuations. If there is 'market failure'—for example, if pollutants are being poured into the atmosphere without any charge or adequate charge—then the Tobin-Nordhaus approach is to include the cost of the pollution as a deduction from the aggregate of goods and services consumed. In arriving at the cost of pollution, the Tobin-Nordhaus approach is to use estimates of the values that individuals place on clearer air or on the cost of abatement. The essential aspect is that the valuations of the individuals affected are taken at face value.

In contrast, in TWOTAP, Treasury indicates that it will be 'respecting the informed preferences of individuals' and, presumably, not be respecting uninformed preferences. TWOTAP refers to things that Australians have 'reason to value'—this is to distinguish them, presumably, from things that Treasury officials believe Australians value for no good reason. Clearly, behavioural economics has had its effect on Treasury. Thaler and Sunstein used the Orwellian phrase, 'libertarian paternalism' to justify subliminal manipulation of individual choices. That would be a case of 'Treasury knows better than you what is good for you, and so knows what you would choose if only you did not suffer from weakness of will or defective time preference or whatever'. Here, in contrast, TWOTAP is a case of 'Treasury knows your mind better than you do'.

However, Treasury is to be complimented for one aspect: TWOTAP makes no pretense that it is engaged in more than straight, unvarnished paternalism, with no need for a deceptive weasel word as modifier.

Treasury is the premier public service department, staffed by top-rate people, experienced in making difficult judgments on behalf of others. In this respect, the language of TWOTAP is revealing—'informed preferences'; 'reason to value'. Who better to pass judgment on the reasons of ordinary Australians—most of whom, it must be said, lack the education and experience of senior Treasury officials—who better, than senior Treasury officials? Who better to know which preferences deserve respect, because they are informed preferences—not to be mistaken for the uninformed, presumably ignorant preferences of ordinary Australians—who better to know than senior Treasury officials?

Is there not a tone of patrician superiority in TWOTAP? Public servants may well have crafted these words, but not, it seems, as servants of ordinary Australians, whose preferences are to be judged by Treasury and, if found wanting, discounted or completely disregarded as un-informed and un-reasoned. No, these are words crafted by the masters, not the servants.

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<sup>8</sup> Tony Atkinson reported extensively on this issue for the British government. His suggestion was to use (inferred) willingness to pay.

## Distribution

The distribution of those opportunities across the Australian people. In particular, that all Australians have the opportunity to lead a fulfilling life and participate meaningfully in society.

The second sentence is cant (that is, a ‘pious, sanctimonious platitude’) and, in particular, political cant. It goes well beyond Bob Hawke’s famous promise that ‘By 1990, no Australian child will be living in poverty.’

The first TWOTAP sentence on distribution implies that Treasury will modify its policy advice according to some estimate of the effects on the distribution of income or wealth or ‘opportunities’ (however these are measured).<sup>9</sup>

Surely redistribution is a matter for politicians, not Treasury. Politics involves the exercise of power over others, and elected politicians take from some and give to others. (The exercise of this power can be justified in a number of ways, including using the contractarian approach to politics favoured by James M Buchanan.) What role does Treasury have, beyond informing the politicians about the likely distributional consequences?

In a speech in 2011, focussing on how to take distribution into account, David Gruen chided the NZ Treasury for eschewing normative advice on distribution: this, he said, was an instance of ‘reticence proclaimed a virtue...[It] does not seem possible to me to simply communicate ‘what the distribution is’ without engaging in normative issues’.<sup>10</sup> But TWOTAP and Gruen both fail to let us know what the Australian Treasury means by **the** distribution. Gruen’s NZ speech had valuable things to say about distribution, but he manages never to outline what indicators he used to measure ‘improvements’ in the distribution. He said that Gini coefficients and the like seem to have a smaller impact on policy than do ‘measures of adequacy’—but he fails to tell us what measures of adequacy should be used. He lauds the addition of subsistence levels of consumption into the famous Atkinson-Stiglitz 1976 ‘separation’ theorem on taxation—but fails to tell us how ‘subsistence’ is measured. However, I suspect that the default is that more equal is better: after telling us that Konow argued that equality or egalitarianism is itself not an underlying principle, Gruen uses an example—involving a reduction in labour market regulation—in which movements away from equality seem to be a negative.<sup>11</sup>

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<sup>9</sup> For the economists in the audience, I should state that I think that the following is an empty set: policy choices that benefit all individuals. Nonetheless, I think that the concept has its normative uses.

<sup>10</sup> David Gruen, James Kelly, Stephanie Gorecki and Tim Wong, ‘Wellbeing, living standards, and their distribution’ (09 September 2011), p. 6:

[http://archive.treasury.gov.au/documents/2153/PDF/speech\\_dg\\_nz.pdf](http://archive.treasury.gov.au/documents/2153/PDF/speech_dg_nz.pdf)

This paper comes close to endorsing the use of a social welfare function.

<sup>11</sup> ‘... [M]ore deregulated labour markets...reduced income inequality by improving employment outcomes [but] widened wage inequalities at the same time...[I]f work has benefits separate from income, the calculus is much more likely to be positive.’

Gruen’s chiding of NZ Treasury for sticking with positive description is hard to

Many economists believe that efficiency and equality can clash; or, in terms of TWOTAP, that a trade-off exists between expanding the set of opportunities and making the distribution of wellbeing more ... well, more something—maybe more of what Treasury approves. Without some clear indication of what Treasury has in mind for the trade-off between these two goals, then if one goes north and the other goes south, of what use is TWOTAP?

Australians have preferences about distribution of opportunities, income, wealth and power. While they may want improved wellbeing for themselves, and for their families, friends and communities, most Australians do not want to live in a country in which some people have no opportunity to enjoy a reasonable standard of wellbeing; or worse, a country in which some people have a miserable level of wellbeing. Many Australians are offended by extremes of income and wealth and power and opportunities. In the Tobin-Nordhaus approach to index numbers for aggregate wellbeing, the values that ordinary Australians place on these matters can be taken into account (with difficulty). Otherwise, leave distribution to the politicians.

A final remark: the Australian Constitution has a Lockean clause requiring just compensation for property taken by the Commonwealth. This requirement—absent or ignored in non-democratic countries—reflects a concern with the arbitrary use of power, and a respect for private property rights—that is, respect for the distributional status quo ante. Max Corden coined the memorable phrase ‘conservative social welfare function’ to capture this latter aspect. It clashes with the assumption that all incomes and assets are ‘the community’s’: if something is left in private hands, then it is only by the grace of government or government’s incapacity to devise mechanisms that better achieve its goals.<sup>12</sup>

## **Sustainability**

The sustainability of those opportunities available over time. In particular, consideration of whether the productive base needed to generate opportunities (the total stock of capital, including human, physical, social and natural assets) is maintained or enhanced for current and future generations.

There is an old saying, with some truth-value: if you cannot measure it, you cannot manage it.

Specific attention was given to sustainability by Stephanie Gorecki, David Gruen and Shane Johnson, in their September 2011 paper cited earlier, from which I quote:

[F]or many stocks, particularly environmental and social capital, placing a monetary value ... is very difficult. Stiglitz et al (2009) ... recommended that a monetary index of sustainability be complemented by a limited set of physical indicators to monitor the environment — particularly in the case of irreversible or discontinuous

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reconcile with the Australian Treasury’s insistence in 2004 that TWOTAP is ‘primarily a descriptive tool’.

<sup>12</sup> In his NZ speech, David Gruen remarked that ‘We [Treasury] of course see rewarding effort and risk as important from an efficiency perspective, but for that reason only’. Maybe there is a typo, and the last phrase should read ‘...but not for that reason only’.

alterations. Such an approach seems entirely sensible as we determine better ways to value the environment (p. 27).

However, Treasury will not adopt Stiglitz' recommendation<sup>13</sup>:

We have not yet developed any single measure to summarise all that wellbeing and progress encompass, and it is fair to say that we are unlikely to. It follows, that we — policy makers, commentators and the public — ought not to rely on any single measure to provide us with an assessment of the quality of individual lives or the cohesion of society (p. 31).<sup>14</sup>

Say that the 'productive base' is enhanced for future generations, but damaged for current. When does that enhance wellbeing, or damage it? Once again, trade-offs come into play—but once again, a checklist does not encourage consistency and transparency.

### **Overall level of risk**

The overall level and allocation of risk borne by individuals and the community. This includes a concern for the ability, and inability, of individuals to manage the level and nature of the risks they face.

A worthy matter: but how to make it operational? And I do note the post-modernist touch—'concern for the ability, and inability...' At least Treasury did not disavow the law of the excluded middle.

### **Complexity of choices**

The complexity of the choices facing individuals and the community. Our concerns include the costs of dealing with unwanted complexity, the transparency of government and the ability of individuals and the community to make choices and trade-offs that better match their preferences.

How many are there, in the behavioural economics group in Treasury, that they can not only delineate unwanted complexity in the world of choice, but also estimate the costs of dealing with it. Thaler and Sunstein should be envious.

## **5: Conclusion**

A checklist gives great scope for Treasury officials to exercise their expert judgments about complex matters. Whereas all the items in an index must be quantifiable, for items in the TWOTAP checklist, Treasury find no such need. Moreover, TWOTAP calls on Treasury to reject some quantifiable evidence of the valuations that ordinary Australians place on items in the checklist.

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<sup>13</sup> Presumably, one reason for reticence is that Treasury knows that even when markets for assets do exist, market prices may well be distorted by defective time preferences and the like: shadow prices everywhere, cast by the behaviourist's lamp.

<sup>14</sup> Presumably the first 'We' refers to the Treasury, which seem to compromise the disclaimer about these being "the views of the authors and not necessarily those of Treasury."

However, my main criticism is that TWOTAP consciously avoids lexicographically ranking the items in the checklist, and eschews announcing the relative importance or weights of the various items, which normally would guide decisions about trade-offs.

Others may be able to explain Treasury's abrogation of responsibility for its advice, in resorting to a checklist. A lexicographical order commits Treasury, as does a set of weights for an index or sub-indices. It is easy to find philosophical and ideological objections to ranking one dimension of wellbeing higher than another, or the use of summary indices of wellbeing. But whatever reservations one may reasonably hold about these, they do not provide sufficient justification for choosing something worse.