# THE FREEMAN

IDEAS ON LIBERTY

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JUNE
1987
VOL. 37
NO. 6

THE FREEMAN
IDEAS ON LIBERTY

Published by
The Foundation for Economic Education
Irvington-on-Hudson, NY 10533


**The Freeman** is the monthly publication of The Foundation for Economic Education, Inc., Irvington-on-Hudson, NY 10533 (914) 591-7230. FEE, founded in 1946 by Leonard E. Read, is a nonpolitical educational champion of private property, the free market, and limited government. FEE is classified as a 26 USC 501 (c) (3) tax-exempt organization. 

The costs of Foundation projects and services are met through donations. Donations are invited in any amount. Subscriptions to *The Freeman* are available to any interested person in the United States for the asking. Single copies $1.00; 10 or more, 50 cents each. For foreign delivery, a donation of $10.00 a year is required to cover direct mailing costs.



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PERSPECTIVE

# Excusing Irresponsibility

Many people are angry at the common spectacle of convicted criminals escaping punishment for their crimes, on grounds that they were "not responsible" for the social or biological conditions which allegedly "provoked" their aggression.

In recent years a new form of criminal has appeared: the international terrorist. Frequently sponsored by some collectivist regime, the terrorist commits the most heinous and bloodthirsty deeds. Inevitably, sympathetic voices in civilized nations are raised to declare that these were merely acts of desperation, in response to intractable injustices.

Then there is the related issue of aggression by communist governments, and the chronic excuse-making responses of Western individuals and governments—a phenomena vividly chronicled in such books as Jean-François Revel's *How Democracies Perish*.

What links all these issues? Each entails some form of *appeasement*—of victims rationalizing, or even abetting, the outrages of foreign and domestic aggressors.

And one other thing links them: *the assault on the philosophy of self-responsibility*. Observe that in each instance of aggression, foreign or domestic, voices of "moderation" are raised to excuse the aggressors of moral responsibility for their crimes.

Sociologists and psychologists claim that environmental or biological factors caused a career criminal to victimize others. What he needs, they say, is understanding and rehabilitation.

Diplomats and scholars argue that when the Soviet Union invades a neighboring country or subverts a distant one, it is not being aggressive; it is merely "reacting" to "historic fears of invasion" in order to "secure its borders." The cure is to reassure the Soviets that *we* mean *them* no harm, by means of increased aid, trade, and negotiation.

In each case, individual moral responsibility is obliterated, allowing causality to be inverted—with aggressors being treated as victims, and their victims treated as aggressors.

Just as the obliteration of individual responsibility encourages legalized aggression, so too does it sanction those who have no time to observe legal niceties. Therefore, it is no accident that with the decline of the philosophy of individualism and self-responsibility, we have seen the explosive increase in crime domestically, and atrocities internationally.

*—Robert James Bidinotto*

## Controls Raise Prices

A recent Canadian study provides revealing information about the effects of government regulation on prices. In 1982, Statistics Canada began to measure the rates of price increases on goods and services that are regulated by government and to compare those to the price increases on products that don't have the benefit of government regulation.

The figures show that since April, 1973, government approved or regulated prices have increased 240 per cent whereas other prices, based on what the market will bear, have increased only 167 per cent. At the present time, the annual inflation rate of products whose prices are approved is about 6 per cent while those whose prices are determined by good old supply and demand in the market place are inflating at only 3 per cent.

In other words, the unmistakable message from the Stat Can figures is that for at least the last 13 years, Canadians have gotten a better deal price-wise on those products whose prices were determined by "whatever the market will bear." The reason for this is not hard to see.

Approved or regulated prices are usually prices that are produced under monopoly or under special license from government. For example, eggs, milk, chicken, and airline travel as well as telephone calls have in common the fact that those who produce them enjoy a form of government-sponsored monopoly. The monopoly in turn is regulated by the government. The theory is that by removing the product or service from the market place and permitting a monopoly, the government will ensure that there is no duplication of facilities—e.g., telephone networks—and no oversupply—e.g., eggs and milk. By regulating the price, the government also attempts to ensure that "the price is right."

The problem is that in determining the price they will allow, regulators often have to rely on information from the regulated industry to determine the costs of production and the reasonable profit that is added. What is lacking is the pressure of entrepreneurs who want to lure away their competitors' customers. In the end, what the market will bear is determined by customers and businesses looking out for the best deal, and that is why what the market will bear serves the interest of consumers better than the well-meaning regulations of government.

*—Michael Walker*
*The Fraser Institute*
*Vancouver, British Columbia*

## Strategies for Freedom

What is the best way to attain a free society? Is it political action? Letters to the editor? The endowment of free enterprise chairs on college campuses? Mass mailings and lobbying?

I don't know. That is, I don't know the best way others should take because I don't believe there is a single best way that works for everyone. We are all different, with different strengths, weaknesses, and interests. I would no more try to tell you the best way to work for freedom than I would tell you the best way to live any other aspect of your life.

But I would like to offer an observation. Many people have become so wrapped up in developing strategies for freedom that they seem to have forgotten what freedom is all about. *Freedom is an ideal.* It refers to the absence of coercive intervention in peaceful activities. It can never be compromised because principles cannot be compromised; principles can only be broken.

When we forget this—when we get so involved in forming strategies for freedom that our main concern is to "put one over" on a gullible public—we aren't fooling anyone but ourselves. For the "freedom" we attain this way will be a false freedom, with no moral conviction, ready to be turned against us by someone smarter than we are at developing a winning strategy. *—BJS*

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# The Face of a Bureaucrat

by Joe Hochderffer

As an old bureaucrat hater, I had often wondered what a real live bureaucrat looked like. Did he have horns? Spit fire? Scaly skin? Cleft foot? I didn't know.

Bureaucrats were the guys who wrote the regulations that took all the do-goodism out of the laws that Congress passed. Or they were the people in the statehouse, underpaid and overworked, who labored in dingy rooms flanking ill-lighted corridors and could hardly wait until the clock struck four. They were faceless, nameless. The unseen enemy. Waiting to pounce on an unsuspecting developer who had submitted plans for a new shopping mall. Hungry for the little old lady who dared propose corridors a mere seven-and-a-half feet wide in her nursing home wing.

Bureaucrats didn't run for office, so they didn't wage political campaigns. You never saw their pictures on a brochure or in a newspaper. They weren't interviewed by Barbara Walters, or nominated for Man of the Year.

I had grown accustomed to thinking of bureaucrats as living in Washington, D.C., or Indianapolis. But a few months ago I learned that they live in my hometown as well.

I'm CEO of a small hospital and we were about to complete a medical office building next door as a way to assure our survival. We'd long since had approval of all the state agencies required. Our community looked forward eagerly for the new young family practitioners who were moving to town to beef up our medical staff. It was a rare day in June and the contractor was right on schedule for the July 1 opening—when I had a phone call from a bureaucrat.

The local representative of the state fire marshal's office did not like the fire rating on a storeroom wall about 10 feet long. Our architect agreed to replace it.

The state fire marshal asked for one thing; the local fire inspector wanted another. It was impossible to do both. The runaround between state and local bureaucrats took several days. They juggled responsibility like a hot potato.

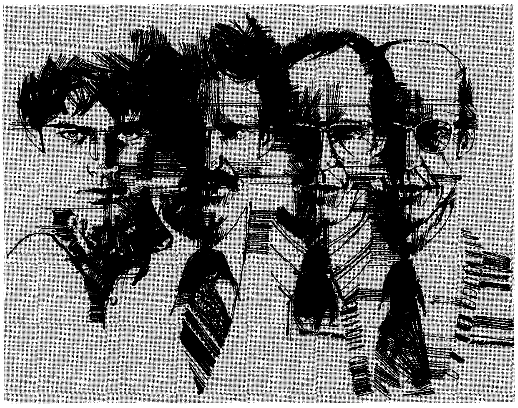
Then we found out the local building inspector didn't like our architect. Plans for a storm sewer drain, previously approved, were rejected. We started altering plans to please the locals, who kept telling us it wasn't they but the state who was holding up our project.

We finally appeased the right people at the right time and were able to open our medical office building almost on schedule. A sad story, perhaps, but at least I learned what a bureaucrat looks like.

This one had a square jaw, piercing blue eyes, and closely cropped graying hair, the latter a holdover from his days in the Marine Corps. He was medium height, medium build, and had a distinct military bearing. He was average. Bureaucrats just look average.

A few months later I had the opportunity to meet another local bureaucrat. He was the city planner, new on the job. I remembered meeting him when he first came to town. He had puppy dog eyes and a strong desire to please. He was

*Mr. Hochderffer is Administrator of Cameron Hospital, Angola, Indiana.*



polite and accommodating. That was when he first came to town.

Now he was stopping construction on our day care center, a project designed to strengthen our position to hire and retain nurses who are mothers of infants or toddlers.

We had gone through the lengthy process of getting approval of our plans from the state board of health, the public welfare department, and the state fire marshal. We had made several changes at recommendations of the state agencies—a usual process. After all the okays, our building contractor received the go-ahead from the local building commissioner, our old friend from the medical office building days.

Two weeks into the project and we received a letter from the building commissioner telling us to stop construction. If we had questions we were to call the city planner, the one with the puppy dog eyes. More responsibility dodging.

The young planner had now been on the job long enough to be too busy to return telephone calls. But we finally connected.

"I don't want to shut you down," he assured me.

"But are you going to shut us down?"

"Well, I don't want to shut you down."

Long pause.

"My hands are tied."

"Then you're shutting us down?"

"I don't want to shut you down. It's up to the board of zoning appeals."

"When can I see them?"

"They meet in three weeks."

I remembered that bureaucrats are never to blame. That had become clear a few months earlier when state bureaucrats blamed local bureaucrats and vice versa for the delays on our medical office building. Now the bureaucrat was passing the blame to a committee.

The sin we had committed was in not getting a land use variance to remodel the interior of a structure in a block that housed medical and hospital offices and residences.

"The city is considering changes in the zoning laws," the city planner told us. "If those changes were now in effect, you wouldn't need a variance," he said.

"And since they're not yet in effect," I began.

"You need the zoning variance," he finished.

So with our project half completed, our contractor had no choice but to take on other jobs. We'll get back in priority line with him when we get the decision of the board of zoning appeals. Meanwhile we've lost a few thousand dollars (nothing to a bureaucrat) and we have a newly hired director of a day care center twiddling her thumbs and wanting to get started in a new enterprise.

Now I hope you don't get the idea that I have become a hater of local bureaucrats too. I have not.

For me bureaucrats now have faces. And that's an improvement. I still like my government at the local level. I prefer the bureaucrat that I know to the faceless one.

I can leave phone messages with the local bureaucrat. I can knock on his office door. I guess I could throw rocks at his house if I chose, but it hasn't come to that yet. I might even be able to get him fired—but why do that? You might trade in Dracula and get Frankenstein.

I'll stick by my hometown bureaucrat, thank you. I may learn to love him, but at least I won't have to take a long canoe trip with him. □

# Privatizing Japan's Railroads

by Donald J. Senese

Japan is one of the world's economic success stories. After suffering defeat and destruction in World War II, Japan, with American assistance, adopted the principles of free enterprise which have made it the leading economic power in Asia. Japan may once again show the world an economic lesson with its recent efforts to remove its railroad system from government control and turn the system over to private enterprise.

Railroads have played an important role in Japan's development, providing essential links for this unique nation which consists of four islands—Kyushu and Shikoku in the south and Honshu and Hokkaido in the north. In the words of the famous historian of Japan and former U.S. Ambassador Edwin O. Reischauer, a "complex and efficient railway network ties the whole country together."[1]

Japan began developing railroads in the 1870s. The first railroad constructed in 1872 linked Tokyo to Yokohama. British engineers built it and British investors financed it. A railroad in 1874 linked Osaka with the port of Kobe and another one in 1877 linked Osaka with the port of Kyoto. And while the years of World War II saw a slowdown in internal railroad construction, the trend toward rapid railroad expansion resumed after 1945.

Visitors to Japan in the last two decades have been impressed with Japan's "bullet trains" which carry passengers at speeds up to 130 miles an hour. The new Tokaido Line, linking Tokyo and Osaka, began operation in 1964 and Japan has continued to run superexpresses between these two key cities.

While the trains traveled quickly, inefficient railroad management was causing growing concern among top Japanese officials. To understand the problem, we need to focus on the role of government in the Japanese economy.

Japan has built its economic success by following the general principles of private enterprise, but the Japanese government, partly through influences of history and culture, has continued to exercise extensive controls. Japan maintained a monopoly on salt and tobacco through its Japan Monopoly Corporation. Japan's telephone and telegraph services were conducted through the Nippon Telegraph and Telephone Public Corporation. And railroads fell under a government-owned company called Japan National Railways. The JNR exercised powerful control, maintaining responsibility for two-thirds of rail transport in Japan. (The Japan government did maintain a hands-off policy on such areas as gas production and electricity generation.)

The management of Japan's railroads is along the lines of a government bureaucracy, rather than a profit-seeking firm. With no market incentives, costs have mounted. The number of government employees on the railroads has grown enormously, and this large personnel force is isolated from economic accountability by strong union pressures. At a time when Japanese government officials and economists are questioning the role of government and its rising costs, the deficit for Japan's

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railroads has continued to climb, placing an ever-growing burden on taxpayers.

Defenders of the public sector claim that such services as railway transportation and telecommunications are so important that they must be run by government for the public good. This argument proves shallow. Government bureaucrats, while professing to serve the public good, have strong incentives to expand their power and increase their own benefits, rather than serve consumers. This becomes evident when attempts are made to cut costs by reducing employees, or increase productivity by using more advanced technology. Growing evidence has demonstrated to the Japanese that railways are too important to leave to the mercy of a growing bureaucracy.

## A Better Way?

The most visible problems of the Japanese railroads have been the soaring deficit and the growing labor force. Could these problems be solved by more government controls? Or is a new approach needed? Does the private sector offer a better way?

A special blue ribbon committee was asked to examine various alternatives. The committee members opted for a private sector solution, suggesting that the gigantic Japan National Railways be split up and that management be shifted to the private sector. Japan's Prime Minister Yusuhiro Nakasone enthusiastically embraced the recommendation, and began to push it through Japan's legislative assembly, the Diet, where his Liberal Democratic Party has a strong majority, thus virtually assuring its passage.

The committee suggested that Japan National Railways be divided into six companies. There would be one separate company for each of three of Japan's four islands (Hokkaido, Shikoku, and Kyushu). The largest island, Honshu, which contains Tokyo and the bulk of Japan's population, would be served by three companies, with one each in charge of the northern, central, and southern parts of the island.

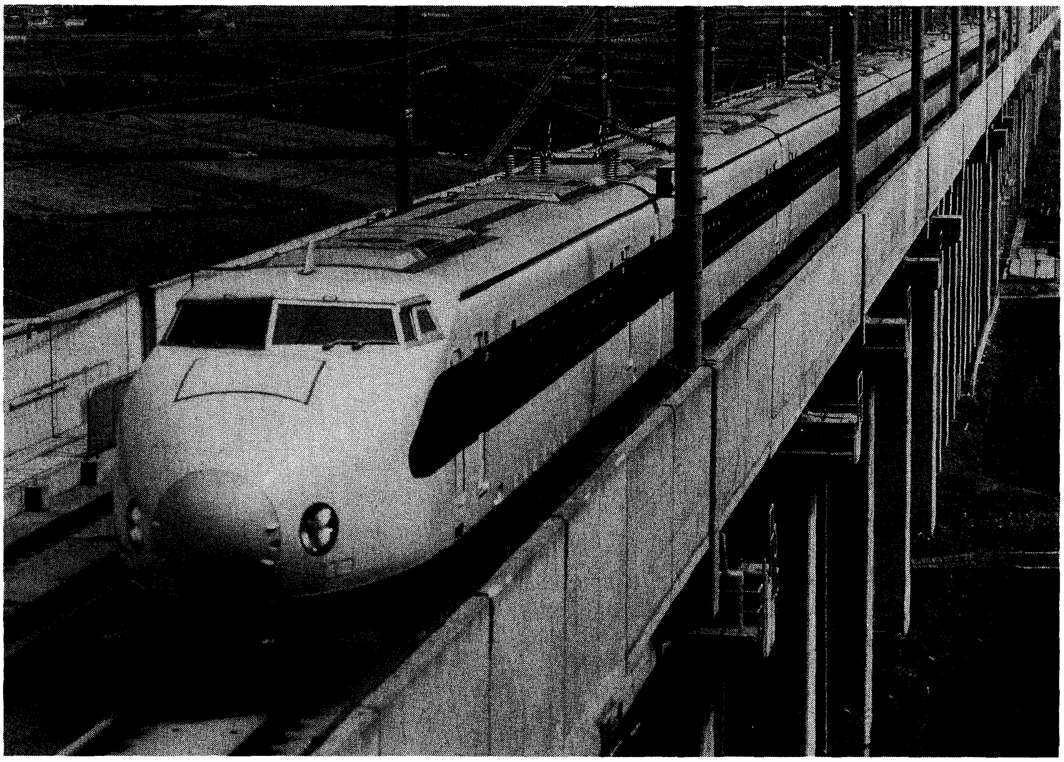
The companies operating on Honshu island would be expected to earn a profit and therefore would need to assume a part of the huge railway debt. The companies on the other islands would have more difficulty in turning a profit, but would benefit from the payment of interest from a special fund. The Shinkansen lines and the "bullet" trains which run on them would be leased to the three companies operating on Honshu island. A completely separate company would handle freight operations. The plan is scheduled to go in operation this year.

Opposition to this plan soon surfaced. Bureaucrats and their supporters argued that the railways should continue to be operated by the central government, with even greater government support, since it is in the "public interest" to have the government maintain control. Toshikazu Yamazaki, chairman of the National Workers' Union (Kokuro), largest union in the Japan National Railways work force, criticized the plan because it would reduce the number of railroad workers. A total of 61,000 workers are scheduled for transfers to central and local government agencies or the private railway companies.[2]

(The debate over the Nakasone plan demonstrates how the political debate can be shifted by advocates of freedom. The left wing of the National Railway Workers' Union strongly opposes the effort to turn the railways to the private sector. And yet possibly sensing the public mood, the Japanese Socialist Party endorsed a half-way approach which supported the idea of privatizing Japan National Railways but opposed dividing it into separate companies.)[3]

The argument that the "public interest" is being served by the government-run railways is refuted by the growing inefficiencies in the system and by the bureaucracy's failure to correct them. For example, trains have not been permitted to run 100 kilometers and back without permission from the central office. Another example involves schedule changes, which often result in simultaneous departures for connecting trains. Engineers must delay trains so that passengers can make the connections, thus causing trains to run late. Even such simple schedule changes get bogged down in the government bureaucracy.

As with other national monopolies, Japan National Railways has been responsible for the decline and disappearance of local railway lines which have difficulty competing with the gov-




**Tohoku Shinkansen train**

ernment-subsidized national system. Hiroshi Kato, a member of the blue ribbon panel which recommended turning the railways to the private sector, addressed the importance of this change:

> After reviewing why the JNR (Japan National Railways) is no longer working for the public benefit, we concluded that more efforts must be devoted to bringing efficiency levels up again. If the railways are efficient and competitive, they can protect even local lines. As things are now, all the JNR can think of to solve its troubles is to abolish local lines. And that's exactly what it's been doing. If the JNR had been denationalized a decade ago, I'm sure we could have saved a lot of local lines.[4]

Observers of the Japanese system recognize that transferring the railways to private hands will be a major undertaking. The inefficiency of the present system, the burden of the growing debt which the taxpayers of Japan must bear, the stagnant bureaucracy, and excessive workers are readily apparent. However, can the private sector do a better job? Despite the cries of alarm from advocates of the public sector, there is firm evidence that the private sector can succeed.

## Telephones: A Shift to the Private Sector

One can look to the Japanese experience with telecommunications as a guide. The government of Japan, through the Nippon Telegraph and Telephone Corporation (NTT), dominated communications for over a century, creating the second largest telecommunications system in the world. Government exercised monopoly control over this enterprise, and few suggested that the private sector could do a better job.

However, the government of Japan established an Ad Hoc Commission for Administrative Reform which recommended that the company's operation be turned over to the private sector so that it could efficiently meet the changing and diverse needs of the public. An historic event took place in December 1984 with the adoption of three pieces of legislation which shattered the government monopoly and permitted any firm to enter the telecommunications business. In April 1985, telecommunications shifted to the private sector with the renaming of the operating group as the NTT Corporation. The NTT Corporation, with its 380,000 employees, is Japan's largest private corporation.

A number of moves were made to increase telecommunications efficiency. The NTT was reorganized along the lines of a modern company, rather than a government bureau. Almost 25 thousand tons of documents and data were thrown away and the new corporation kept only those which were vital for operations. The company through its employees began promoting the sale of telephones and telephone cards, providing greater contact with the customers so as to better ascertain their needs. Research and development efforts, opened to competition, have gone forward with a number of companies seeking new technologies to improve telecommunications.

The almost two years of private sector telecommunications demonstrate that the public interest is better served by the new system. Hisashi Shinto, who headed up the old Nippon Telegraph and Telephone Public Corporation and became president of the privately owned NTT Corporation, emphasizes the change in spirit and approach with the new ownership of telecommunications: "When I became the head of the 'old' NTT, there was no concept of the customer. But now I see the word 'customer' used instead of 'subscriber' even in formal documents. In other words, people at NTT have readily begun to understand that they earn their living because customers use their services."[5]

Fortunately, the change in telecommunications was made when even the government-run operation was making a profit. The new NTT Corporation has produced a larger profit, up 30 per cent in its first year of operation. In addition, any profits in excess of a 10 per cent dividend will go to reduce customer charges. On the other hand, Japan National Railways has experienced tremendous losses and carries a heavy debt. The record of losses will have to be reversed as the new companies work to turn the railways into profit-making operations.

The decision by Japanese political leaders to turn the debt-ridden and inefficient Japan National Railways over to private corporations is an important one with significant consequences for the Japanese public and the expansion of the private sector in Japan. As the telecommunications experience has already shown, government can divest itself of long-time monopoly operations, with consumers reaping important gains.

However, in the long run, the real beneficiary is the cause of freedom. A new avenue for competition, creativity, efficiency, technological innovation, and service is opened up compared to the rigid regulations and productivity disincentives built into government monopolies.

The privatization of Japanese railways will likely signal another great economic and political advance for Japan. One of the most powerful economies in the world is demonstrating that individuals operating in an atmosphere of economic freedom can greatly benefit the public in providing essential services. ☐

1. Edwin O. Reischauer, *The Japanese* (Cambridge, Massachusetts and London, England: The Belknap Press of Harvard University Press, 1977), p. 28.
2. Hiroshi Kato and Shun'ichi Yamazaki, "The Plan to Privatize the National Railways," *Economic Eye*, December 6, 1985, No. 4, pp. 24-25.
3. "Socialists' Plan for JNR Backed by Biggest Union," *The Japan Times*, March 18, 1986, p. 2.
4. Kato and Yamazaki, "The Plan to Privatize the National Railways," p. 26.
5. "Science and Technology: One Year Later—Improved Services in the Wake of NTT's Privatization," *Look Japan*, May 10, 1986, p. 13.

# William Graham Sumner

**IDEAS ON LIBERTY**

Competition can no more be done away with than gravitation. Its incidence can be changed. We can adopt as a social policy, "Woe to the successful!" We can take the prizes away from the successful and give them to the unsuccessful. It seems clear that there would soon be no prizes at all . . .

# Planning Threatens Freedom

by C. Brandon Crocker

Is the American economy too free? Many people think so. Socialists have long advocated central economic planning, and, under the guise of "national economic policy," the idea is working its way into the programs of the major political parties.

The persistent appeal of central planning is anomalous, given the poor relative performance of planned economies versus free economies. But economic efficiency is not the only, or necessarily the most compelling, argument against central planning. Economic planning threatens all individual freedoms, and must be analyzed in terms of these threats.

How does central planning threaten individual liberty? To find the answer, we must consider what central planning is and how it works. The goals of central planning are to create high growth, minimize unemployment, and sometimes to provide an "equitable" income distribution, or to protect the environment. Proponents believe these goals can be achieved by using government to intercede in the "chaos" of the free market so as to redirect the nation's resources and design an "optimal" mix of industries.

The losses to individual freedom from this type of system are obvious. To make sure the economic plan is followed, government must interfere with the freedom of individuals to start businesses, to invest and work where they choose, and even to consume certain goods and services.

A nation's economy is nothing more than the decisions of individuals as to what to produce and consume. Therefore, a government-controlled economy means government-controlled people. If government is to enforce an economic plan, it cannot have people starting whatever businesses they like or investing capital wherever they wish. Certain fields of employment will have to be forcibly curtailed and certain goods and services (either already available or which could be made available) will have to be prevented from reaching the population—because control of what is produced is necessarily control of what is consumed.

These are not insignificant losses of freedom. Proponents of central planning, however, deny that there is any major restriction of occupational choice under economic planning. To be sure, some restriction will take place in "undesirable" industries targeted to be phased out, curtailed, or not allowed to start up, but this will be done for the "social good." Furthermore, central planning in practice often saves jobs, they claim, in industries which would be abandoned in a free market, thus preserving the freedom of many people to pursue the occupations of their choice.

These arguments, however, are invalid. First, whether jobs are taken away for the "social good" or not doesn't alter the fact that freedom of choice, in terms of available options, has been diminished. Second, while the free operation of the market does cause some people to leave their chosen occupations when industries become obsolete, there is a great difference between not being able to follow one's chosen occupation because no one is willing to pay for a particular product or service, and not being able to follow one's chosen occupation

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because of government edict. In the first instance freedom of action is not being denied and the freedom of people to make (or not make) contracts is preserved. In the second instance, the opposite is true.

Is the loss of individual freedom so onerous as to outweigh such professed benefits as security against involuntary unemployment and destitution? An acquaintance from Norway, living under a semi-socialist system, thinks not. He likes the feeling of security. He even asserts, as do many Norwegians, that government should tell people what they should and should not do because most people do not know how best to take care of themselves (and the government does).

This is security at a price, certainly. But in addition to the individual freedoms already lost by such a scheme, this brand of security comes at the expense of something of far greater value—security against arbitrary power and despotism—in a word, security against totalitarianism.

The serious implementation of any significant economic plan will lead to increasing governmental dominance in the running of industry and make possible the easy abduction of most political and economic freedoms. There will be an inevitable conflict between business and the economic planners. To regulate millions of individual businesses in such a complete way (output, number of employees, use of raw materials, etc.) without the cooperation of those businesses will be impossible—especially considering that business will feel that policy may change with the next election. The solution to an uncooperative private sector will be to make individual companies better serve the "public interest" through measures such as nationalization and government controlled syndicates.

Government control of the economy leads not only to power over production, but also to power over consumption and distribution. Displacing the price system with government edicts takes the distribution of goods and services out of the hands of individual buyers and sellers, and places it into the hands of a central authority. With this power the central authority can wield great control over the populace.

George Orwell, commenting on Friedrich Hayek's classic book, *The Road to Serfdom,* remarked, "It cannot be said too often—at any rate it is not being said nearly enough—that collectivism is not inherently democratic, but, on the contrary, gives to a tyrannical minority such powers as the Spanish Inquisition never dreamt of." To believe that such a vast concentration of power will not be used at some point to oppress the population is to deny the history of mankind. The world is full of maniacs and coercive utopians—many of whom are interested in exercising political power, as history well shows.

All totalitarian regimes rely heavily on economic controls to coerce their subjects. The efforts of Hitler's National Socialists to oppress Jews and other minority groups were greatly facilitated by the Nazi government's control of employment and the distribution of goods. The Soviets use economic controls to pressure dissidents, and they even use their system of rationing to create high voter turnouts for their one-candidate elections—if you don't vote, you don't receive your ration cards. Those not rigidly conforming to Maoist doctrine during the Cultural Revolution often lost their jobs, no matter how valuable their skills. China's current one-child policy is enforced through the control of a series of economic "benefits" which include jobs, salaries, and rations. The success of the Chinese central planners in enforcing such an unpopular policy which meets the resistance of centuries of Chinese tradition shows how great the power a government can wield over its people when it controls the economy.

Neither Germany in 1933, nor Russia in 1917, nor China in 1949 had long traditions of democracy and political and economic freedom. The United States, in contrast, has a long and deeply ingrained tradition of democracy and freedom, as well as constitutional arrangements which make quickly installed tyranny unlikely. This is no reason, however, to feel safe in taking steps to weaken that tradition and to make possible great abrogation of individual freedom. Free societies have been, and still are, very rare and fragile. Freedoms taken for granted and not carefully safeguarded do not last long. The loss of economic freedom is a major crack in the foundation of any free society. □

# Socialism Succeeds by Failing

by Allan Levite

There has never been any shortage of proof—both theoretical and empirical—that socialism is a practical failure. Or, to put it another way, it has proven itself to be an economically inefficient system. Yet in spite of its major flaws, socialism continues to attract and often hold many of the best minds.

In our effort to understand this phenomenon, it seems to me that we have also erred, in that we have always analyzed socialism using an assumption that we never questioned because its truth seemed so obvious. This proposition is that socialists define economic "success" the same way we do, as a condition of greater general prosperity—in short, increased living standards for most people, compared with alternative economic systems. As I will show, however, this is a false assumption, and the misplaced emphasis it causes on our part accounts, in large measure, for our failure to understand why socialism keeps thriving in theory despite performing so poorly in practice.

Our first clue should come from the history of socialism and communism, a history permeated with examples of fervent disciples living austere, spartan lives. Almost invariably, the more wholeheartedly a socialist or communist believes in his credo, the more ascetic an existence he maintains. This point is all too often overlooked as we allow our attention to be diverted by the many well-known examples of wealthy or cultured socialists who do not eschew their hedonistic surroundings. We should instead focus on those who are the most loyal to both the letter and the spirit of socialism—namely, those who shun material wealth even though it would be available to them with a little effort. And it is here that we find the essence of the socialist creed.

Any biography of Karl Marx will note that he lived in self-imposed poverty, even though he could have used his educational credentials to obtain well-paying work.[1] His friend, Engels, similarly wrote with great admiration of the ascetic renunciation that he (Engels) believed was necessary for revolution, stating that workers "must deny themselves even the smallest enjoyment" in order to steel themselves for the class struggle.[2] Bruce Mazlish, in his appropriately titled *The Revolutionary Ascetic,* quoted Gorky describing Lenin as a puritan who had "renounced all the joys of earth . . ."[3] Mao Tse-tung, who like Engels had a wealthy father, lived his life in much the same way; stories of his economic self-abnegation abound.[4] Fidel Castro, another scion of wealthy parents, lives quite frugally and, like Mao, prefers to dress in plain army fatigues, a sharp contrast with the sartorial habits of genuine working people whenever they can afford more expressive apparel.

With this evidence, let us construct an imaginary Socratic dialogue that will illustrate the point I have in mind.

"You socialists assume, I take it, that people like Marx, Mao, and Castro are 'men of good will'?"

*"Of course."*

"Which means that they wish only good for others?"

*"Certainly."*

*Mr. Levite is a computer salesman and a free-lance writer, residing in Dallas, Texas.*

"So if anything bad happened to them, they would not want anything similar to happen to others, especially the poor?"

*"Correct."*

"And if they believed something to be good or beneficial, they would want that also for others, particularly the poor?"

*"Naturally."*

"So if such a socialist leader were blessed with good health all his life, he would want the masses to enjoy the same advantage?"

*"Positively."*

"Now, do the socialist leaders who believe in this doctrine the most completely, like Mao Tse-tung, tend to live ascetically or in self-imposed poverty?"

*"Most of them, without a doubt, particularly those whose faith in socialism has not become corrupted by greed or pragmatism, like that of the current Soviet and Chinese leaders."*

"Yes. Now mustn't we assume that the 'purest' of the socialists, like Mao, lived ascetically because they believed it to be good and proper to do so? Obviously, since they are men of good will, they would not have lived this way had they believed it to be morally objectionable, but only if they thought it was right."

*"So it would seem."*

"And we have already agreed that whatever they deem good for themselves, they also wish for others?"

*"Yes, we did."*

"Then since they deem poverty good and affluence bad for *themselves,* they must also consider poverty good and affluence bad for others, especially the poor, with whom they so strongly identify. And they must therefore want the poverty of the poor to be continued, not eliminated."

From here on it should be understandable why socialism continues to attract followers despite its economic failures whenever tried. It was never *intended* to "work," as we understand the term. If it did "work," using our own definition, prosperity would soon emerge, which is the *last* thing that the most passionate of the socialists want. How could they want for others what they believe is morally objectionable for themselves? Abundance, for them, means not only that materialism will erode ideological zealousness, but also that enjoyment of life will manifest itself, which for them is an undesired goal. Nothing can make an ascetic feel lonelier and more betrayed than the sight of multitudes busying themselves with the pursuit of life's pleasures. And even those socialists who decline the spartan life still hold such self-sacrifice to be a fine ideal even if they cannot bring themselves to practice it. So they can never truly accept prosperity for what it is. They hate capitalism not for its failures but precisely for its successes, because it engenders markedly higher living standards for the majority.

Not surprisingly, then, as Ludwig von Mises pointed out, we learn that the concept of socialism was not a product of proletarians, but of the children of wealth and of the bourgeois intelligentsia.[5] Working people cannot be so easily convinced to give up their quest for a more comfortable life, not having been jaded by a superfluity of comforts. As rare as a snowball in Tahiti is the poor person who wants to remain poor. Such notions, where they exist at all, are almost exclusively the property of those who disdain wealth, due perhaps to guilt. "Imagine no possessions," said Beatle John Lennon in his song "Imagine." It is no coincidence that this was not one of the songs he wrote when he was poor, struggling to earn a living playing rock and roll in gritty nightclubs —he wrote it after having amassed great wealth. Anyone wanting to imagine something truly fantastic should try to conceive of *poor* people giving up their dreams of having more possessions.

## The Power of the State

Socialism's most extreme form, communism, absolutely depends on making the poor abandon their materialistic dreams. This explains why communism proposes to give such awesome power to the state. No other institution, and no amount of propaganda, could induce the masses to abjure wanting to enjoy life. Only the *state* has the naked power needed to *enforce* asceticism. A future condition of abundance is promised only because it is counterproductive to advertise what people don't want, and much more practical to promise something they do want.

Can generations of "re-education" ever make the common people renounce their urge to enjoy life and its material benefits? Fortunately, no. In December 1986, many thousands of students in China demonstrated for democratic reforms, complementing the millions of their brethren who wanted and finally received greater economic freedoms in the post-Mao era. These youngsters had never seen capitalism nor known anything but the Marxist dogma they had been exclusively taught; they were all born after the Communists took power in China. Yet their profoundly human strivings to live freer and fuller lives could not long be suppressed. No amount of propagandizing could ever make them or any other mass of people stop wanting to be human. And in this we can rejoice, for true hope comes from this simple observation.

We must not, however, conclude that socialists will see in this evidence proof of the error of their dictum that people can be taught to seek monastic, self-sacrificing existences. Facts cannot make the socialists stop wanting a spartan world, and, as I have shown, trying to convince them that capitalism produces high living standards is largely useless, especially if they already believe it. Even the best salesperson would have a hard time trying to sell something the customer does not want at all.

We will be able to convert the most zealous of the socialists only by convincing them that enjoyment of life is not wicked. Our occasional successes in converting socialists to capitalism with economic facts should not obscure the larger truth that those who take socialism truly to heart cannot be swayed by statistics on higher living standards under capitalism if they seek ascetic conformity instead. This is why no number of economic failures, no matter how high, ever demoralizes socialism's most devoted partisans. If anything, such debacles only *strengthen* their convictions. This is not to say that we should abandon our factual approach to promoting free enterprise; far from it. But we must temper it with the knowledge that only those who have no objection to enjoying life will find capitalism appealing. There are those who have such objections, and so our first goal must be to overcome them before moving on to economic or political theory and practice. □

1. Thomas Sowell, *Marxism* (New York: William Morrow and Co., Inc., 1985), p. 174.
2. Edmund Wilson, *To the Finland Station* (Garden City, N.Y.: Doubleday and Co., Inc., 1940), p. 210.
3. Bruce Mazlish, *The Revolutionary Ascetic* (New York: McGraw-Hill Book Co., Inc., 1976), p. 152.
4. Edgar Snow, *Red Star Over China* (New York: Bantam Books, 1972), pp. 68-72.
5. Ludwig von Mises, *Theory and History* (New Rochelle, N.Y.: Arlington House, 1969), p. 121.

## In Future Issues . . .

### July

- ''World Resources and Economic Exploitation'' by M. W. Sinnett
- ''Lessons in Liberty: The Dutch Republic, 1579-1750'' by Robert A. Peterson
- ''Amelioration'' by Philip J. Bowers

### August

- ''Which Liberalism?'' by Tyler Cowen
- ''Take Back the Environment'' by Jorge E. Amador
- ''One Complaint per Customer, Please'' by Jane M. Orient

# Houston's Laissez-Faire Housing Policy

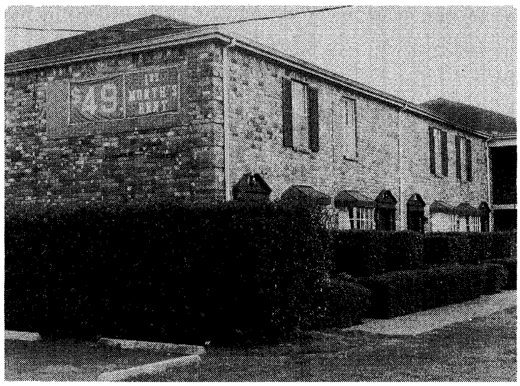
by J. Brian Phillips

During the 1970s Houston's population grew by an average of 36,000 per year. This pace accelerated during the early 1980s as oil prices skyrocketed and Houston's economy boomed. Jobs and opportunities were plentiful, which combined with the subtropical climate to create a virtual paradise for unemployed, winter-weary Northerners.

This huge influx of people created a tremendous need for housing. New home and apartment construction proceeded at an unprecedented rate. Over 25,000 apartment units were built each year from 1977 through 1983. What had been cow pastures and rice paddies only ten years before were transformed into sprawling apartment complexes in a matter of months as developers raced to meet the growing demand for housing.

In 1982 Houston's economy began to slow. Unemployment rose and the stream of new arrivals dwindled to a trickle as recession gripped the city. Throughout this period of economic volatility, Houston continued to have an adequate supply of rental housing at reasonable rates. Unlike cities which have turned to rent control in a futile attempt to provide affordable housing, Houston has remained committed to a laissez-faire housing policy. The results speak for themselves.

The most striking fact about cities with rent control is their perpetual shortage of rental housing. Vacancy rates usually run under 5 per cent, which gives renters few, if any, housing options. Rent control, in fact, is price control.



As has been demonstrated repeatedly, in theory and in practice, price controls always result in shortages.

But Houston did not experience a housing shortage. The lowest vacancy rate reached in Houston was 4 per cent in June 1982. During the 1970s the average vacancy rate was 7 per cent. And this was in spite of the fact that the population was growing by an average of nearly 700 people a week.

The 4 per cent vacancy rate of June 1982 did not last long. By April 1983 the rate had reached a record high of 24 per cent. This abrupt shift was primarily caused by two factors: the downturn in the economy and an overbuilt market. Because housing construction is a relatively long-term project, developers were unable to respond immediately to market conditions. Despite the high vacancy rate in 1983, over 28,000 new units were built that year. However, the next year that number fell by over 50 per cent, reflecting the oversupplied market.

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As occupancy rates decreased, apartment owners were hard pressed to continue operating profitably. In an effort to attract tenants, apartment owners began offering a myriad of gifts and other special promotions. Televisions, video recorders, memberships in health clubs, holiday turkeys, life insurance policies, and cable television were among the free gifts used to entice renters into signing leases. Many apartment owners waived security deposits, and more than one even paid the moving expenses of new tenants.

## Owners Compete, Too

In rent-controlled cities, renters often pay apartment "locators" hundreds of dollars to find housing. In Houston, apartment locators offer similar services; however, their fees are paid by the apartment owner rather than the renter. Just as the recession has hurt the apartment industry, it has hurt the apartment locators also. Most now offer gifts to renters who find an apartment through their services. This illustrates the fundamental difference between cities with rent control and those which allow the market to operate freely: *In the former, renters engage in one-sided competition for housing space, while in the latter, there is also competition among apartment owners.*

These competitive forces are readily apparent in the Houston rental market. When the economy slipped into recession, the number of renters stabilized as new arrivals dramatically decreased, while developers continued to build new apartments, though at a greatly reduced rate. Since April 1983, the vacancy rate has stayed near 17 per cent, keeping apartment owners in intense competition to attract and retain tenants.

In rent-controlled cities, tenants often stay in the same apartment for decades. There are two good reasons for this: one is the general lack of housing options, the other is the obvious benefit of paying a rent established 20, 30, or even 40 years ago.

In Houston, however, most leases run six months. The average renter is young and mobile, and with an oversupplied market from which to choose, renters are quite willing and able to move with ease. The fact that renters can move so easily places more competitive pressure on an already intensely competitive industry.

One of the stated purposes of rent control is to insure a sufficient quantity of affordable rental housing. But in city after city, rent control has resulted in housing shortages. In Houston, in contrast, where apartment owners are governed by the market, there has always been a sufficient supply of rental housing.

The real victims of rent control are property owners who must accept less than market rates for their properties. Rents are established by a central board, and annual rent increases are generally meager, if allowed at all. In New York City, some renters still are paying 1940s rates for their apartments. It is little wonder that developers are reluctant to build new rental housing in such cities.

Even the most radical rent control advocates eventually recognize the discouragement to new construction that rent control creates. Consequently, like most statist policies, exceptions are made as those in power seek to gain the benefits of the free market without losing their control over the lives of others. Most often, new construction is exempted from rent controls.

But even this enticement is seldom sufficient to stimulate new construction. After all, the exceptions that can be arbitrarily granted can just as easily be arbitrarily withdrawn. Developers see little reason to take chances on such a possibility, when cities such as Houston offer developers the economic freedom all industries need to thrive.

Rental property in rent-controlled cities is difficult, if not impossible, to sell. Clearly, not many people care to spend good money for the privilege of losing more money. In Houston, despite a soft real estate market in general, apartment complexes are selling rather briskly, as investors hope to make purchases at bargain prices. This demonstrates that capital flows not only to its most profitable uses, but also to its most efficient.

Many rent-controlled cities allow the rents on voluntarily vacated apartments to rise to market levels. But when this occurs, the undersupplied market pushes rents higher than they would be in a completely free market. Conse-


PHOTOS OF HOUSTON HOUSING BY JANE H. HERBENER

quently, new tenants are forced to pay rates much higher than could be sustained if rent control did not exist at all. By artificially establishing and controlling rents, rent control creates huge inequities in rental rates.

In Houston, the average apartment rent reached a high of \$402 in late 1982, shortly after the vacancy rate reached its record low. However, as the vacancy rate increased, rents fell to reflect the market's oversupply. And despite the fact that vacancies have remained relatively stable for the past three years, rents have continued to drop. Today the average apartment rent in Houston is \$303.

## Maintenance Suffers

One of the most visible consequences of rent control is the slow deterioration of rental property due to a lack of maintenance. Property owners, often forced to incur losses on their property, see little economic sense in making repairs. And all too often, owners simply abandon their property, rather than continuing to absorb losses.

In Houston, however, competition encourages apartment owners to maintain their properties. While there are certainly examples of rental housing that is not well cared for, Houston does not have the widespread deterioration of rental housing that plagues most cities with rent controls. Furthermore, most of the vacancies in Houston are in the older apartment developments.

Today, apartment rates in Houston are 25 per cent lower than they were five years ago. During the same period, consumer prices have risen nearly 13 per cent, and Houston's unemployment rate has climbed from 4 per cent to nearly 10 per cent. Consequently, at a time when prices are higher and more people are out of work, i.e., when people have less money available for housing, the market has driven rental prices down in Houston.

Rent control advocates insist that their policies will result in decent housing at reasonable rates. The facts show otherwise—only the free market can provide the best product at the lowest cost to the consumer. Rent control attempts to force property owners to provide affordable housing, ignoring the fact that if a legitimate market exists, free enterprise will provide for that market. While rent control advocates profess to help the consumer, the free market is the best protection the consumer has ever had. □

# The True Charity

by Kenneth McDonald

When government expands, special interest groups divert its powers to their own ends. These groups look upon government as a way to get other people to pay for things which group members would like to have but don't want to pay for themselves.

Often this is done in the name of charity. For example, Africans are starving and we in the West must go to their aid. As private citizens, some of us do. We send money to organizations that channel food to hungry people. When our government sends aid, however, we have no choice but to send part of our tax money to the governments of the countries concerned.

Quite frequently, people there are starving because their own governments have made a botch of things. The post-colonial years of Africa have been marked by collectivization, forced resettlement, confiscation of grain and livestock through excessive taxes and obligations, coercive labor programs: nothing less than state terrorism against the farmers who formerly grew food enough for everyone. Ironically, by coercing us as individuals into yielding part of our incomes in the form of taxes to African governments, our own governments reinforce the socialism that is causing Africans to starve.

This quite minor activity of our governments in the name of charity abroad is an extension of the major activity they indulge in at home, namely the forced redistribution of wealth and income—"redistribution" being a more palatable term than theft.

Again, this is done in the name of charity. It is to relieve poverty, or to "create jobs," or to pay medical bills for the sick, or to build "affordable" housing. In one form or another the object is to subsidize particular groups of people at the expense of others.

This process has been going on for so long that even those of us who prize independence may be tempted to dismiss it as an ingredient not only of taxes but of the duty that citizenship and taxes entail. We pay the taxes and are quit of the duty.

In this way governments have inserted themselves between individuals whose instinct is to be charitable and other individuals to whom they might have offered charity.

It is when we consider the matter as individuals that we are brought up against the morality of it.

Rightly, we prize our independence. We achieve it through self-reliance, a quality that bids us to husband our resources so that we might not become a burden to others. Self-reliance, then, is the quality that would appear to be lacking in those that our governments oblige us to subsidize. The lack is attributable to a number of causes ranging from laziness to imitation, that is, growing up in places where dependence upon government subsidies is accepted as a natural condition.

Whatever the cause, to discourage self-reliance is to condemn those who lack it to a life of dependence. Yet this is where governmental redistribution has brought us. Charity thrice re-

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moved has proved uncharitable. By insulating recipients of public charity from the moral restoratives of work and self-reliance, governments confirm them in habits that morality condemns.

To all this the socialist replies: "Ah! But there is no work for them. They are the weak who have been pushed to the wall by a market-dominated economy. A caring society must show them compassion."

## Governments Intervene

The truth is that most Western economies are dominated not by markets but by government interventions in markets. If markets were free, no one would have the legal power to dominate anyone. The rule of free exchange would apply, namely that participants stand to gain from an exchange, otherwise they wouldn't participate. In Frederic Bastiat's words: "By virtue of exchange, one man's prosperity is beneficial to all others."

This rule is self-evident. Why would anyone wish to interfere with exchanges that are of such obvious benefit to the general welfare?

This brings us back to the role of government. Ideally it should be to maintain a peaceful society in which the citizens would initiate the exchanges from which a nation's wealth is created. The fact that no society embodies that ideal is all the more reason why it should be not only envisaged but also set as the criterion against which societies are measured.

Since the quantities and kinds of exchanges in such an ideal society would be as varied as man's ingenuity, it would be contradictory to limit them. What free men might agree to limit is their own behavior. Thus each would recognize the need to fulfill whatever contracts he was engaged upon just as he would expect his fellow contractors to do the same.

Here, then, is a legitimate role for government: to make and enforce laws (1) that require observance of contracts, and (2) that safeguard persons and property from encroachment.

Those two precepts—fulfilling contracts and refraining from encroachment upon other people or their property—are fundamental to a society of free people. They are fitting matters for a government to legislate because they constitute the underpinnings of a free society.

Moreover, such a society would encourage the self-reliance that forced redistribution policies have done so much to discourage. As Leonard Read pointed out in *Accent on the Right:* "The unprecedented practice of freedom in our country has, one might say, catapulted many millions of 'the masses'—including you and me—into a state of affluence previously unknown to history. . . . The alleviation of poverty is a by-product—a life-saving benefit—along man's way toward the higher ideal of liberty. . . . Restore and preserve the practice of free market, private ownership, limited government principles; and one of the by-products will be as much removal of poverty as possible."

The self-reliance that delivers independence is inhibited by government interventions. The more that we can do to stem those interventions and move our societies toward free markets and private ownership, the more we shall help other people to independence.

Helping other people to independence is the true charity. □

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**IDEAS ON LIBERTY**

# Leonard E. Read

"Thou shalt not steal" presupposes private ownership. Sharing ideas suggests having ideas to share. Charity is possible only if one has something to give. Plainly, the excellence of our performance as social beings stems from private ownership of our labor and its fruits, whether material, moral, intellectual, or spiritual.

# Pay Television and Property Rights

by Joseph S. Fulda

An increasing number of American homes, recently estimated by *U.S. News and World Report* as perhaps 100,000, are now equipped with special antennae, decoders, converters, and other electronic gadgetry capable of receiving the signals from pay television satellites or earthbound microwave transmitters.

Faced with such a large number of potential clients who prefer to freeload, the pay TV industry has begun to fight back. Arguing that the unauthorized reception of their signals is a violation of their property rights, the industry convinced the FCC to issue an injunction prohibiting such reception. A Federal circuit court of appeals upheld the order, thus stamping into law the common notion that these freeloaders are "pirates of the air" or "basement thieves."

Looking at the matter on its face, there is ample reason to be suspicious. First, Federal courts have not shown overmuch concern for the property rights of corporations, preferring instead long and learned disquisitions on "the public good" and the exact meaning of "a taking." As for the regulatory agencies, they have been—until very recently—downright hostile to the very concept of private property (i.e., that ownership implies control). Second, there is no greater protection of personal liberty than the rights of private property. An abridgment of liberty in the name of property rights is thus automatically suspect.

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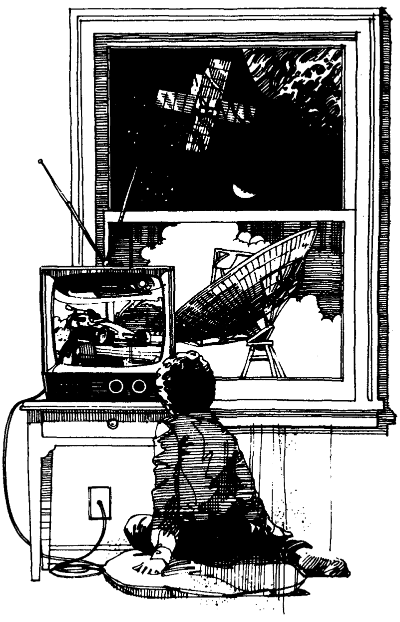

Examining the matter in more detail, it is clear that broadcast frequencies, commonly referred to as "airwaves," are real property. Like other real property, they are properly acquired by appropriation and continuous possession and use over a period of years, not by government distribution.

Now real property cannot be stolen, but it can be illegally occupied. This is known as trespass, the prevention of which is properly a function of government, part of its mandate to secure our rights.

In considering how one illegally occupies a broadcast frequency, we must distinguish between transmission and reception. When one transmits on another's frequency, he is indeed a broadcast pirate for he illegally occupies that which is someone else's. It makes no difference that the offender may broadcast from his basement. (Is the man who launches a missile into his neighbor's yard any less guilty because he owns the launch pad?)

When one receives another's transmission in the privacy of his home, however, he neither damages nor occupies the broadcaster's real property and has not violated anyone's rights. If the broadcaster chooses to dump what economists call positive externalities, such as the entertainment emanating from his airwaves, on another's private property, the property owner is free to take advantage of this. One must distinguish between the airwaves, the real property that the broadcaster owns, and the programs, the positive externalities the freeloaders enjoys, despite the fact that the latter originate from the former.

Harvard philosopher Robert Nozick makes a similar point in his landmark *Anarchy, State, and Utopia* in disputing the idea that someone's positive behavior toward me necessarily requires reciprocation or compensation, even when he acts voluntarily and without my contractual agreement to pay. The core of this idea is that all freeloading is theft, an idea that can be easily adapted to justify all manner of anti-libertarian state endeavors. Nozick asks whether a man who throws books into my yard from his can demand payment. Here it is from his yard (real property he owns) that the books (analogous to positive externalities) enter my yard (real property I own).

Although it may be felt that airwaves and programs are somehow different from yards and books, in practice we are quite ready to grant the similarity. Is there anyone who would claim that a CB radio buff who demands payment after being entertaining for a bit is entitled to use the coercive apparatus of the state to exact it? Pay television companies differ from the CB user only in that they entertain professionally, at considerable expense, and for their livelihood. But if the greater extent of the freeloading is all that separates the two cases, then if one is not theft, neither is the other.

If anything, programs and airwaves present an even weaker case for mandatory compensation than the likes of books and yards. Consider the case of a man's apples falling into his neighbor's yard. Leaving aside the separate question of whether such placement (of the tree and/or apples) can be enjoined or whether rent (compensation for the negative externalities) can be exacted, the man is entitled to the return of his apples. He has lost personal property which can be restored to him. But programs dissipate as they are watched, and at the show's end the broadcaster has whatever he had before. Put plainly, there is neither anything to return nor anything that was lost. Only when lost income is the result of some rights-violating activity is compensation in order; lost income cannot be used as the basis of a claim for compensation.

At the heart of the confusion lie several mistaken analogies. First, there is the sentiment expressed by Assistant FCC Counsel Norman Blumenthal, "It's like sneaking into the movie theater." Not at all. It's rather like viewing a drive-in movie from your living-room window or watching your neighbor's Fourth of July fireworks display from the comfort of your backyard hammock. In each case, you receive benefits without payment, but without fault, for to be a thief you must positively violate someone's domain by aggressing, intimidating, deceiving, or the like. In none of these cases does any such rights-violating activity occur.

Now there is a parallel to the movie house sneak: someone who attaches a feed to a cable company's line. This we do not defend, for the connection illegally occupies part of the cable. This is *taking* rather than being *given* and demonstrates the possibility of being a bona fide thief in reception as well as in transmission.

Second and quite similar is the notion that our case rests on the ease with which this sort of freeloading may be perpetrated. Again this is not so. We do not plead the liberal notion that "If you leave the door open, you invite theft," but rather the libertarian notion that not all freeloading is theft. If one were to enter an unguarded home, he would illegally occupy another's real property and indeed would be guilty of trespass. That is precisely why the relative ease of basement transmission on owned frequencies is no defense. As we have shown, however, the case with reception is different: here the "home" has not been entered at all and no trespass has occurred.

But the notion persists that airwaves are somehow different from other real properties. Let us return to the case of the fireworks display. Is there any philosophical difference between a visible air display dumped on you and an invisible electromagnetic-wave display which carries the programs you capture on your screen? The necessary use of complex receiving equipment in the latter case is surely philosophically irrelevant. If your house was some distance away from the drive-in and you watched with a telescope, would you then be a thief or a "movie pirate"? "Do burglars' tools make the burglary?" we might well respond!

By broadening the rights of pay television companies (after many years of deliberately strangling them), the FCC weakens the individual's right to use his property in entirely permissible ways. This is always the case when new "rights" are granted by the state. Why should we expect airwaves to be any different?

Having said this, we should note that service providers with built-in positive externalities such as these are not as defenseless as is often claimed. The drive-in can erect a wall, the next-door neighbor can make his display contingent on his neighbor's contribution, and the pay television companies can and are building increasingly sophisticated and impenetrable electronic "fences."

Should broadcasters shield their transmissions? Morally, the question has no answer: they have the right to do so or not to do so as they choose. Financially, they should do so if and only if the added cost of the protective equipment used in both transmission and reception will lose them fewer subscribers than they will gain by welcoming some erstwhile freeloaders. This becomes a moral consideration only if there is a fiduciary trust, as in a publicly owned corporation. If the market dictates, however, that the shielding is not worth the costs, no one should expect the state to shoulder them. The state already undertakes a multitude of unproductive activities. Why one more? □

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**IDEAS ON LIBERTY**

# Nobody's Property

People do not effectively "own" the airwaves simply because they are public property. While this "people's ownership" may be true in a strict legal sense, it is not true in practice. At present, the airwaves hardly belong to anybody. The government does not really own them fully because their use has been allocated to private broadcasting by the Communications Act. Yet, the private broadcasters are not owners either—they simply have three-year licenses. Thus, everybody's ownership rights have been diluted. It is a stalemate that ought to be broken—and it can be by removing the airwaves from their special "public property" classification.

In discussing the possibility of removing Federal control of the airwaves, one quickly finds himself swept into a narrow "either-or" argument. Either we have Federal licensing and control, the argument goes, or we face broadcasting anarchy. After all, governments have to provide policemen to direct traffic, don't they?

The fallacy of the argument is in its assumption that we have a choice only between Federal control and chaos. Even persons who are quite suspicious of any kind of Federal control of broadcasting cannot see other alternatives. We must remember that this Federal control has existed ever since broadcasting's infancy, so the idea of liberating the airwaves has had little consideration. Ownership of the airwaves has been a government monopoly, to be shared sparingly with others. So long as this monopolistic ownership goes on unchallenged, there is little chance that the roots of broadcasting's problems will be touched. —MELVIN D. BARGER

# Privatizing Federal Programs

by Hans F. Sennholz

Most attempts at Federal budget cutting fail. Powerful interest groups stand in the way and fight to safeguard their entitlements and favorite programs. By contrast, taxpayers offer little opposition. Program costs are spread thinly among millions of taxpayers, amounting to a few dollars per capita. While the costs are dispersed, benefits are concentrated, providing an important guidepost for politicians. It indicates that they have nothing to gain, but much to lose from opposing particular spending programs.

Because of all the pro-spending incentives, few programs are ever terminated or even reduced. Federal spending rises continuously and Federal debt increases with no end in sight. Some observers despair over the democratic process, but many are convinced that there is a better tactic for spending control—"privatization."

Privatization transfers services from government agencies to private producers. The efficiency gains that flow from competitive enterprise are to be used to cut spending.[1] Privatization is also said to pay rich political dividends. It creates powerful groups of providers and beneficiaries who profit from the programs. They may be mobilized to support privatization and build a coalition for decisive spending cuts.[2]

At the present there is no coalition for spending reductions; but we do sense a powerful movement for privatization in all corners of politics, from the extreme right to the radical left. On the left, it may spring from the search for new government programs and the need for new sources of revenue. On the right, it may be a new version of the old vision of individual freedom and enterprise, or merely a natural reaction to more than ten thousand off-budget government enterprises that have sprung from local, state, and federal governments in recent years.

No matter what the motive powers may be, the movement should ring an immediate alarm with all friends of genuine privatization and put them on the alert about the actual meaning of privatization. If so many reformers agree on an economic program, it is likely to be either empty and meaningless or vague and fuzzy. In this case, "privatization" has at least seven different meanings and many more connotations that permit everyone to endorse it:

1. Federal assets may be sold at market prices to individuals who acquire unhampered ownership and control of the assets.
2. Federal assets may be sold at bargain prices to favored individuals.
3. Federal assets, such as Amtrak, may be sold to individuals who remain under the jurisdiction of regulatory authorities.
4. No assets are sold, but private contractors are engaged to bolster expensive and unsatisfactory services of government enterprises, such as the Postal Service.
5. Private contractors are engaged to assist

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transfer and welfare agencies and make their programs more effective, from public housing to the administration of Medicaid and Medicare benefits.

6. Privatization may take the form of a wide system of vouchers that give low-income people access to competitive markets, such as the education and housing markets.

7. Privatization may place loan assets in the hands of private investors, such as the portfolios of the Farmers Home Administration and the Export-Import Bank.

All but the first of these versions of privatization are bound to be disappointing in the end because they do not really reduce Federal expenditures; they merely seek to make the present system more efficient. In fact, some are likely to cause government expenditures to increase as they call upon private contractors to supplement government services, or create new classes of beneficiaries who hope to profit from government largess. Experience also teaches that the new classes of beneficiaries will not replace the old classes, but instead can be expected to take their places in line with the others.

Wherever these versions of privatization make the present system of transfer and entitlement more effective, they give it new vigor and strength and cause it to grow. Surely, a successful voucher system that provides better housing is likely not only to offer better homes for more people and cause the housing industry to profit and expand, but also to boost the demand for ever more housing vouchers and generate a demand for vouchers for other goods and services. Such privatization is likely to extract more income and wealth from taxpayers, lead to more deficit spending, and pave the way for more collectivization and socialization.

## Genuine Privatization

The only privatization worthy of its name is the sale of government assets at market prices to individuals who acquire clear and unhampered title to the property. For example, until the beginning of this century it was public policy to sell Federal land to homesteaders. Unfortunately, in recent decades the policy has been to take land from private owners and use it for "public purposes," such as irrigation and flood control, power projects, wilderness areas, or any number of programs. The federal government now owns more than 30 per cent of all the land within the continental U.S., and its holdings are increasing steadily. It now owns more than 69 per cent of the area of Arizona, 71 per cent of Utah, 85 per cent of Nevada, and 90 per cent of Alaska.

It is rather difficult to assign present-day market values to Federal real property, consisting of public domain property, donated property, and properties under the supervision of the Architect of the Capitol. But this writer is willing to conclude that, at the height of the real estate boom in 1978-79 when the Federal debt was less than one trillion dollars, the market value of more than one million square miles of Federal land probably exceeded the Federal debt. Unfortunately, the debt has doubled since then while real values have fallen substantially, which no longer permits us to draw this conclusion. But it is fair to assume that a "privatization" of Federal land not only could be made to cover the budget deficits and reduce the mountain of Federal debt, but also would substantially enlarge the real base of individual income and wealth.

Many other Federal assets and enterprises could be liquidated and the proceeds allocated to the reduction of the Federal debt. In many cases the sale would represent significant losses by government, which usually manages to acquire assets in most inopportune moments and at exhorbitant prices. In 1979, for example, when oil prices exceeded $35 a barrel, the federal government established the Strategic Petroleum Reserve (SPR). At the end of 1986, when the price stood at less than $15 a barrel, more than 600 million barrels of crude oil were in storage. Plans call for a 750 million barrel stockpile that is to be maintained in standby readiness, providing protection against supply disruptions.

Genuine privatization would liquidate the stockpile immediately because its continued existence only makes matters worse. At the outset, its accumulation lent aid and comfort to OPEC, purchasing huge quantities of oil when OPEC was restricting world supplies and boosting prices. When OPEC finally succumbed to market pressures and oil prices retreated to recession levels, the SPR stockpile depressed prices even further. The stockpile as well as current SPR policies continue to disrupt the oil market, as did Federal controls over U.S. oil production before 1981. SPR should be abolished immediately and its assets liquidated forthwith.

The Synthetic Fuels Corporation (SFC), another glaring folly of Federal politicians and officials, provides subsidies for "nonconventional" fuel production. With world oil prices declining since SFC was created in 1980, prospects for commercial use of synthetic fuels have diminished substantially. A program of genuine privatization would terminate SFC operations and liquidate its assets immediately.

## Sale to Favored Individuals

A form of privatization that has been practiced rather successfully by the Thatcher Administration in Great Britain is the sale of assets to favored individuals. Government housing, for instance, is sold at bargain prices to low-income and public-assistance tenants, who are likely to applaud the sale and oppose any future attempt at renationalization. Similarly, government-owned enterprises are sold at bargain prices to their employees, who hope to profit from the sale. To assure highest possible market prices of their shares, the new owners are likely to demand an unrestricted freedom of sale to other individuals.

Obviously, such a policy of asset liquidation pays rich political dividends to the sellers of the property. But it usually overlooks the fact that a sale amounts to just another favor to a pressure group that reaps benefits at public expense. The bargain price that is so attractive to buyers is a distress price to taxpayers who provided the assets in the first place. The fact that the sale may be the lesser evil among several evil alternatives does not change the nature of the taxpayer loss.

This kind of privatization would not find much popular support were it not for the bargains and favors. At market prices most government assets offered for sale probably would be bought by investors and speculators who would want to safeguard their investments and improve their yields through cost reductions and productivity improvement. Public-housing tenants would strenuously oppose such sales, just as civil servants would reject such a privatization of their places of employment. In final analysis, this privatization program promises to pay political dividends because it enriches some people at the expense of others, just like all other transfer and entitlement programs.

Many friends of the private property system nevertheless favor such privatization because it may reduce the economic scope of government and bring us a step closer to an unhampered market. It may necessitate another handout in the short run, we are told, but will bear economic freedom in the long run. It may even turn civil servants and transfer beneficiaries into staunch defenders of the private property order.

Surely, privatization as an interim step toward unhampered economic freedom deserves our undivided attention and assistance. But such an interim step must not be confused with just another step on the old road of transfer and entitlement. Privatization that safeguards old privileges, grants new favors to old interest groups, and imposes stipulations and conditions on the new owners is a make-believe privatization designed for gullible observers and investors.

## Counterfeit Sales

Federal assets may be sold to individuals who remain under the jurisdiction and control of regulatory authorities. Such a privatization unfortunately does not change the employment of the asset in the process of production. Surely the legal title to an asset does change from government to private hands, but its control, which is the economic essence of property, does not change at all; government continues to wield authority over the asset through its agencies.

All sales of assets that have public utility status are likely to be spurious and fictitious. The sale of the northeast corridor of Amtrak to employees and other private interests, as suggested by The Heritage Foundation,[3] would merely transfer economic control from the Department of Transportation to the Interstate

Commerce Commission and several other agencies that regulate the use of capital and dispense immunities and privileges to labor unions. Sale of the two Washington airports, National and Dulles, to individual investors, which cost taxpayers some $2.3 billion to build and millions of dollars every year to maintain, would raise new cash for other Federal programs, but would not alter the economic status of the airports. Government agencies would continue to control every aspect of operation, would limit the maximum investment yield which stockholders would be permitted to earn, but would refuse to give assurance of a minimum yield. Investors may do better by buying Treasury bonds, notes, or bills than to invest their savings in Federal utilities offered for sale.

## Private Contractors to the Rescue

The federal government owns and operates some 125 economic enterprises, most of which suffer substantial losses and serve their customers rather poorly. To reduce budget deficits and improve services, the enterprises should be privatized forthwith—their assets should be sold at market prices, without regulatory restrictions, to anyone willing to operate them in competition with other businesses.

But this is not the intent of most privatizers. They would like government to retain ownership and control over enterprises, but would be willing to have private contractors render some of their services. They would assign difficult and expensive tasks to private contractors, but retain profitable services and other activities that are likely to pay political dividends.

The Postal Reorganization Act of 1970 established the U.S. Postal Service as an independent Federal enterprise. Annual appropriations to the Service will reach an estimated $2.7 billion in 1987,[4] which include not only subsidies for carrying certain categories of mail at free or reduced rates but also total actuarial costs of employee pensions. The hourly labor costs of some 740,000 Postal Service workers are estimated at $19.11, which are 33 per cent higher than the wage rate for equivalent work in competitive business. Moreover, USPS labor productivity lags far behind that of private couriers, which suggests that every phase of the postal service can be contracted out at considerable savings to taxpayers. According to a Congressional Budget Office investigation, contracting out janitorial services alone would save $980 million annually.[5]

Such a conclusion is based on a simple assumption that must not be taken for granted in government enterprises. It assumes that the transfer of an activity from government to private hands will reduce government outlays. Actually, the transfer may set civil service labor free, but is unlikely to terminate its employment and expenses. Government workers enjoy civil service protection, which bars dismissals no matter how much work is contracted out. Surely it is unlikely that contracting the management of national parks to environmental and conservation organizations would bring any savings to the seven land-management agencies: the Bureau of Land Management, National Park Service, Army Corps of Engineers, Forest Service, Bureau of Reclamation, Fish and Wildlife Service, and the Tennessee Valley Authority. Contracting out undoubtedly would improve the service, but would necessitate additional expenditures.

Similarly, replacement of the Legal Services Corporation with legal services provided through State Bar Associations and contracts with private legal clinics may not bring forth the dismissal of a single Legal Service Corporation attorney and his staff, but merely cause their transfer to other agencies. In recent years, the mere attempt at agency reduction has led not only to frantic interagency shifting but also to the creation of many thousands of off-budget government corporations that have greatly enlarged the scope of government. Surely, they all should be privatized; in reality, they are merely reorganized.

Private contractors may also be called upon to assist transfer and welfare agencies in their service to special beneficiaries. But it is unlikely that such assistance will help to reduce government expenditures. For example, contracting out the management of public housing to tenants' organizations is unlikely to yield any savings. Instead, it is more likely to invite ugly tenant strikes and lead to expensive legal confrontations between the tenants' unions and public authority. Similarly, it is doubtful if freezing all VA hospital construction and leasing hospital facilities from private owners would effect any savings. Instead, it would make more private capital available for VA use.

## Vouchers Expand the Sphere of Government

Many privatizers would introduce an extensive voucher system in order to slash the Federal deficits. They would issue signed or stamped credit documents to beneficiaries who could spend them for purposes designated, under conditions stipulated, and in places clearly defined. They would establish systems of education vouchers, Medicaid vouchers, Medicare vouchers, health benefit vouchers for Federal employees, subsidized housing vouchers, VA health care vouchers, and many others.

But it is rather doubtful that the voucher system would provide any savings to the U.S. Treasury. On the contrary, a system granting educational benefits to certain beneficiaries might not only boost government outlays, but also greatly expand the sphere of government influence and control. It is unlikely to lead to a contraction of public education in any form, but undoubtedly would thoroughly affect private education. Private and parochial schools would have to meet government-imposed conditions to qualify for vouchers. After all, the authority that is issuing the vouchers and spending the money can be expected to set the conditions under which they may be used. In the end, refusal to accede to such conditions might spell financial ruin to the resistor.

Similarly, a voucher system for housing would affect all sectors of public and private housing. The influence of government, which already is very extensive in this industry, would reach ever further and touch every aspect of housing as the voucher authorities would define the official conditions. Moreover, a voucher system would be likely to bring forth new governmental powers of enforcement over recalcitrant individuals who refused to honor and accept the official vouchers. Woe to the builder who failed to meet the voucher conditions and woe to the house owner or private school that refused to honor the voucher!

A health care voucher system for Federal employees, veterans, or Medicare and Medicaid patients surely would not be permitted to diminish beneficiary services. Nor could it be expected to reduce the present army of health care workers who render services to Federal employees, veterans, and Medicare and Medicaid beneficiaries. Surely the voucher system would not be allowed to close a single veterans hospital. But it would soon permeate the whole industry—as do Medicare and Medicaid—with hospitals, doctors, and nurses scrambling to meet the voucher conditions. Indeed, it is difficult to find a trace of genuine privatization in the voucher system.

## Sale of Loan Portfolios

Federal government loan asset sales have gained widespread support on Capitol Hill and on Wall Street. Federal politicians and officials are eager to turn the bulging Federal loan portfolio into cash in order to meet Gramm-Rudman-Hollings deficit reduction targets. Investment bankers are eagerly awaiting the sales; when the Farmers Home Administration recently announced its intention to sell portions of its rural housing portfolio, 39 investment bankers made unsolicited bids to manage the sale. The Administration, too, is ready to sell all new direct loans to private investors. In fiscal year 1986, the total amount of new direct loans is estimated to exceed $26 billion. In future years it may be much larger.

Some privatizers would like the federal government to sell outstanding assets of the Guaranteed Student Loan Program to private investors. The sales, they tell us, would not only generate deficit-reducing revenue, but would also bring discipline and efficiency to the credit process. They heatedly argue with lawmakers and bankers about the details of the sales, especially Federal guarantees and private insurance. Federal guarantees, they are convinced, would jeopardize the discipline and efficiency of the marketplace by reducing the incentive for private investors to pursue collection. On the other hand, Federal guarantees would bring higher loan prices in the sale.

It is significant that these privatizers do not advocate an immediate end of the loan program on grounds of political economy and morality. On the contrary, they would like to render it more efficient. They do not question the role of government in credit affairs, nor the economic consequences of the proposed privatization. They merely engage in idle discussions about the efficiency of government in the collection business and the sale of student loans to private companies better suited to the task. Unfortunately, they completely miss the crucial effect of the privatization program: it permits government to tap more private resources that heretofore escaped taxation and borrowing, to consume more private capital, and otherwise extend its influence beyond its previous bounds. This kind of privatization is completely counterproductive. If there were truth in politics, it would be called "the new collectivization-extension program."

At the end of 1986 the outstanding loan portfolio of the GSL program was an estimated $40 billion.[6] The portfolio carried over $2.2 billion in defaulted loans, with the present default rate at 11.7 per cent and expected to rise to 13.6 per cent by 1990. The sale of this portfolio or any part thereof would affect the loan market in precisely the same way as a Treasury bond offering. Both would crowd out private borrowers. It does not matter whether the loan assets are guaranteed and insured or merely left to the play of the market, they all would take the place of cash or other assets in the portfolios of private investors. The student loan might replace a mortgage loan, commercial loan, or just another government loan. In fact, it is even conceivable that such a privatization might permit government in time to pre-empt the entire loan market through massive credit activity and simultaneous portfolio sales. With off-budget accounting it would not even show up in the budget, and the deficits would be limited to the defaulted loans not yet sold to private investors.

It is a sad commentary on the state of political and economic thought that conservative organizations and foundations which profess to promote the principles of a sound economy are using their meager resources to promote this kind of privatization. While the battle at the Federal entitlement trough is raging and hundreds of billions of dollars of income and wealth are tossed about by the Washington agents of entitlement, the self-styled defenders of individual freedom and the private property order are proposing the privatization of the buoy maintenance program, the sale of National Airport, and the opening of rural postal delivery to private carriers. "Please support our national grassroot campaign," they urge their readers, "to help the President gather support for privatization."

Privatization is the new catchword that fires the imagination of many believers in political salvation. If they would only stop and listen, they would hear the persistent calling for more government and more spending. □

1. Stephen Moore, editor, *Slashing the Deficit, Fiscal Year 1987* (Washington, D.C.: The Heritage Foundation).
2. *Ibid.*, p. x.
3. *Ibid.*, p. xviii.
4. *Budget of the United States Government, Fiscal Year 1987*, pp. 5-64.
5. Congressional Budget Office, *Curtailing Indirect Federal Subsidies to the U.S. Postal Service*, August, 1984.
6. *Budget of the United States Government, Fiscal year 1986*, pp. 5-93.

# Worse Than Thieves

**IDEAS ON LIBERTY**

When your money is taken by a thief, you get nothing in return. When your money is taken through taxes to support needless bureaucrats, precisely the same situation exists. We are lucky, indeed, if the needless bureaucrats are mere easy-going loafers. They are more likely today to be energetic reformers busily discouraging and disrupting production.

—HENRY HAZLITT
*Economics in One Lesson*

# Defending the Rich

by William H. Peterson

Listen. The winds of egalitarianism still blow. . . . Listen, for example, to Rep. David R. Obey of Wisconsin, then chairman of the Joint Congressional Economic Committee, issuing last summer a Committee report (later withdrawn as incorrect) alleging that the so-called "super-rich" have become 38 per cent richer in the last 20 years:

"This study is proof that the rich get richer. A continuation of this trend erodes the basic confidence of the American public in our entire system. It increases cynicism, and adds to the us-vs.-them attitude about all institutions, economic and governmental."

Or, listen to economics professor David M. Kotz of the University of Massachusetts last fall writing à la Robin Hood in *The New York Times* on the annual *Forbes* listing of the 400 richest people in America: "How many billionaires are enough? The share of income and wealth flowing to the rich has been expanding at the expense of the poor. The free-market policies that lie at the heart of the Reagan program have produced this redistribution, while conferring no compensating economic benefits. Instead, we have the worst of all possible worlds: rising inequality amid sluggish growth."

Or, listen to Professor David Gordon of the New School for Social Research and co-author of the newly released Democratic Party study, "Democratic Alternative to Economic Decline": "The most important story about the U.S. economy in the '80s is the economic warfare that the wealthy and powerful have been waging against the vast majority of Americans." His proof: "The real median income of families in the U.S. dropped by 5.7 percent from 1979 to 1984."

*Dr. Peterson, the first holder of the Scott L. Probasco, Jr. Chair of Free Enterprise at the University of Tennessee at Chattanooga, has just formed with his wife a Washington research consulting firm.*

Handling charges like these has been my lot in a professional teaching career spanning almost four decades. As an ingrained supporter of freedom and free market policy, I have long found myself having to defend what many critics deem the undefendable: the rich. Or, having to put down personal innuendos, usually getting them second- or third-hand, that I am perforce a lackey, a sycophant for the rich.

Sometimes my defense is technical. To Messrs. Obey, Kotz, and Gordon, for example, let me remind them of a new Joint Economic Committee study by Ohio University Professors Lowell Gallaway and Richard Vedder. Professors Gallaway and Vedder note family erosion in America and accordingly think that income per family or household *member* is the appropriate measure. They then show a "real household income growth per household member of nearly 5.9 percent" from 1980 to 1984.

Moreover, a recent U.S. Census Bureau Survey on Household Wealth and Asset Ownership finds a long-term *declining* trend in family wealth concentration. This finding ties in with those of University of Chicago economist Yale Brozen. Brozen determined from U.S. Government statistics that in 1929 employee compensation amounted to 60 per cent of national income while the top 5 per cent of all families received 30 per cent of national income. In the next 40 years the share of the top 5 per cent steadily eroded while the employee share rose. By 1969 the employee share reached 72.5 per cent while the top 5 per cent share dropped to 16.5 per cent, almost down to half of what it was in 1929.

To be sure, employee share improvement has slowed since 1969. But Brozen notes a declining U.S. savings rate (net national savings as a percent of net national product) from 15.2 per cent in the 1961-1970 decade to 11.7 per cent in the 1971-1980 decade. Thus the pace of business investment also slowed, with the upshot of much slower growth in labor productivity. Output per manhour fell from a postwar annual average of around 3 per cent through 1970 to under 1 per cent in the 1971-1980 decade.

With such data as this, Yale Brozen has unabashedly formulated Brozen's Law: *Whenever the government attempts to redistribute income from the rich to the poor, it creates more poor people, impoverishes the nation, and decreases the portion of the tax burden borne by the rich.*

I concur, heartily.

Why does more investment lead to a more equal distribution of income? The reason: Capital, mainly in the form of plant and equipment, complements labor: more capital per employee means greater employee productivity—and higher pay. Thus capital, Karl Marx to the contrary, turns out to be labor's best friend, with labor exploiting capital rather than the other way around. Indeed, the greater the capital investment relative to labor the lower the return to capital and the higher the return to labor. This is the history of the "exploited" working man with his ever-rising living standards under capitalism.

But sometimes my defense of the rich is less technical and more philosophical. I have to remind my critics that eventually rich entrepreneurs like Henry Ford, Andrew Carnegie, John D. Rockefeller, and Thomas Alva Edison, as well as more recent commercial pioneers like David Sarnoff (RCA), Edwin Land (Polaroid), Ray Kroc (McDonald's), and Sam Walton (Wal-Mart—Mr. Walton, who started from scratch, is *Forbes'* No. 1 billionaire), helped make America great, that they forged millions upon millions of jobs, that they mightily boosted capital formation and thereby advanced America's living standards, that, accordingly, they belong in America's pantheon of heroes. It follows that all incomes are not created equal—nor should they be. Equality of opportunity, yes, equality of outcome, no.

I have also to remind my critics of the wisdom of my graduate teacher, Ludwig von Mises, whom I lucked into at New York University in 1950 as a result of his being a refugee from Hitler's Festung Europa (Mises escaped in 1940, working his way to New York City). Said Mises in his *The Anti-Capitalistic Mentality* (1956):

> Nobody is needy in the market economy because of the fact that some people are rich. The riches of the rich are not the cause of the poverty of anybody. The process that makes some people rich is, on the contrary, the corollary of the process that improves many peoples' want satisfaction. The entrepreneurs, the capitalists and the technologists prosper as far as they succeed in best supplying the consumers.

Moreover, critics, hear this: Investment inevitably involves risk, while pushing up all incomes, including those of the poor. Stocks, bonds, real estate, and so on are ever subject to the vagaries and risks of the market, and a number of historians have propounded the thesis of "from shirt-sleeves to shirt-sleeves in three generations."

Hence, Mises argued in *Human Action* (1949) that wealth is in reality a "social liability," very much subject to loss:

> Ownership of the means of production is not a privilege, but a social liability. Capitalists and landowners are compelled to employ their property for the best possible satisfaction of the consumers. If they are slow and inept in the performance of their duties, they are penalized by losses. If they do not learn the lesson and do not reform their conduct of affairs, they lose their wealth.

One more thing: Is there a hidden agenda in the attack on the rich? Is envy, one of those ancient Seven Deadly Sins, at work? Scores of Latin, German, Russian, Polish, Spanish, Chinese, and Jewish proverbs tell us, *inter alia,* envy has never made anyone rich, envy cuts its own throat, envy makes life bitter, envy envies itself, envy sees faults rather than virtues, the envious die over and over before they finally keel over, and so forth and so on. Dryden put it this way: "Envy, that does with misery reside/ The joy and the revenge of ruin'd pride."

To me, the attack on the rich ties in with the theology behind the progressive income tax—with the opposition toward flatter tax rates. Interestingly, the first modern supply-sider was not Ronald Reagan but John F. Kennedy. In pushing for a reduction of tax rates from a top bracket of 91 to 65 per cent and a bottom rate from 20 to 14 per cent, enacted into law in 1964, President Kennedy voiced a simple truth: "A rising tide lifts all boats." □

# Banking Before the Federal Reserve: The U.S. and Canada Compared

by Donald R. Wells

The recurring financial panics in the U.S. during the 19th and early 20th centuries led Congress to establish the National Monetary Commission in 1908 to study the problem and recommend a solution. After several years of study and debate, Congress passed the Federal Reserve Act in December 1913. Even though the Federal Reserve did not prevent the Great Depression, and even though it has permitted substantial inflation since World War II, many observers still believe that some Federal control over private banking is needed to prevent the bank suspensions and failures that brought such instability to the economy in the pre-1914 years.

The purpose of this paper is to show that it was only government interference into banking before 1914 that prevented the U.S. from having a stable monetary system. Restrictions on banknote issuance, severe limits on branching, and regulations forcing banks to hold useless, idle cash reserves made the American banking system vulnerable to panics while other nations, such as Canada, avoided these crises. It also will be shown that even though Canadian banks were allowed more freedom of action, the few restraints that did exist led the Canadian government to intervene further into banking to undo the harm that otherwise would not have existed.

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## U.S. Banking Before 1863

Only two quasi-governmental banks were allowed to establish interstate branches in this period, the First United States Bank (1791-1811) and the Second United States Bank (1816-1836). The federal government owned one-fifth of the capital of each bank, causing political resentments which resulted in neither bank's twenty-year charter being renewed.

When the charter of the Second United States Bank was not renewed, all banks were either chartered by the various states, or given permission to operate without a charter under the so-called "free banking" laws. No banks were allowed to branch across state lines, and some states prohibited branching altogether. This prevented a natural system of nationwide clearinghouses from developing to exchange banknotes and later, deposits. Thus, when these banknotes ended up at great distances from their point of issue, they often fell to a discount. Banknote reporters tried to keep the public informed about the value of these various notes, but some fraudulent issuers were able to take advantage of the lapse of time until this information was disseminated (Rolnick & Weber, p. 14).

Some banks, particularly in cities along the eastern seaboard, were able to maintain a stable value of their notes. The best known was the Suffolk system, which operated in the Boston area. The Suffolk Bank was able to keep smaller regional banks from overissuing by means of a clearinghouse. Banks that refused to join the Suffolk system had their notes collected and immediately presented for payment in specie; those that joined were able to count on their notes being received at par.

One problem with the so-called "free banks" was the requirement that they hold an amount of state bonds equal to the banknotes they issued. These bonds often proved to be an illiquid investment for the banks, preventing them from holding the desired amount of specie to redeem their notes on demand. Since this requirement usually specified par rather than market value of the bonds, these securities in many cases were an inadequate protection for the note-holder (Rolnick & Weber, p. 16). Six states attempted to ease public fears about irredeemable banknotes by establishing a note guarantee system (FDIC, 1953, pp. 45-46) — which might not have been necessary had banks been free to branch and to hold the type of assets they preferred.

## The National Bank System

Two of the methods used to finance the Civil War involved money manipulation. One was the issuance of a fiat currency (greenbacks) which was given legal tender status, and the second was the establishment of the National Banking System as a convenient place to sell low-interest bonds. The war led to the federalization of the U.S. currency because national banks were the only issuers of banknotes after Congress taxed the state banknotes out of existence. These new, uniform national banknotes were almost a government currency because they were printed by the Bureau of Engraving and the banks were forced to hold $100 of these 2 per cent government bonds for each $90 of notes they issued.

This system proved to be no improvement over pre-Civil War banking; it was just as prone to panics and to suspension of cash payments. The three main weaknesses of this new system, which were avoided in Canada, were: lack of branching, forced holding of a specific cash reserve, and a government bond-backed banknote. These governmentally imposed restrictions put the U.S. banking system in a strait jacket, making it vulnerable to shocks.

All national banks were forced to be unit banks except for those state banks that converted to a national charter were allowed to retain their intrastate branches. Nationwide branching would have been more stable and efficient, permitting safer bank portfolios through geographical and industrial asset diversification. Unit banks in farm states were at a special disadvantage during agricultural depressions, whereas Canadian banks could carry a non-performing loan to a farmer much more easily (Beckhart, p. 450). Branch banks can be opened more easily in new areas without the trouble of acquiring a new charter and establishing a separate board of directors (Dunbar 1904, pp. 195-197). In addition, branch banks can move reserves to where they are needed more quickly, and at lower cost, since they are held within the same institution and no other bank need profit on the transfer of these funds (Breckenridge, p. 377).

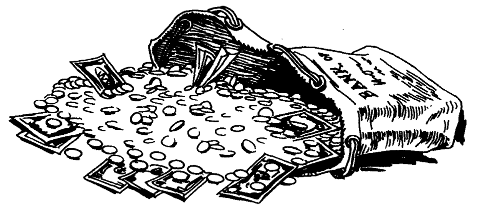
Secondly, national banks were forced to hold a fixed cash reserve against their deposit liabilities, even though any reserve that must be held is no reserve at all, since it cannot be used. The law mandated that country banks hold two-fifths of their 15 per cent reserve in vault cash while the rest could be on deposit in a reserve city bank. These reserve city banks were required to hold half of their 25 per cent reserve in vault cash while the other half could be deposited in a central reserve city bank in New York, and after 1887, Chicago or St. Louis. The latter banks were forced to hold all their 25 per cent reserve in vault cash, which meant gold, greenbacks or other treasury currency. Only state-chartered banks could count national banknotes as part of their reserve.

Since banks could not use these required reserves, they had to carry an excess amount in order to operate; in a crisis, banks often had to suspend cash payments precipitating financial panics. The pyramiding of reserves in a unit bank system aggravated the problem. When faced with an increased demand for cash, each bank had to think of itself first and would pull its deposits from its correspondents. By contrast, each Canadian bank held its own reserve in whatever amount it felt adequate, with the one provision that government-issued Dominion notes had to consist of 40 per cent of whatever cash reserve the bank chose to hold (Breckenridge, p. 242). The pyramiding of reserves in the U.S. made American bank runs contagious; in Canada, a bank failure did not cause the public to distrust other banks.

The third restriction on national bank behavior that weakened the system was the requirement that each bank deposit with the Comptroller of the Currency $100 worth of 2 per cent government bonds for each $90 of banknotes they issued. (In 1900, banks were permitted to issue notes equal to the amount of bonds deposited.) Since these notes were printed by the Bureau of Engraving and were uniform in appearance, they were received and paid out by banks throughout the country. This system failed to test the ability of each bank to redeem its own notes as did the Canadian system with its distinctive banknotes (Dunbar 1917, p. 228). Yet underissuance rather than overissuance was the problem with national banknotes because of the government bond restriction.

## Liquidity Crises

The value of these special bonds, rather than the demand for banknotes, became the constraint on banknote issuance. Some national banks never issued notes at all while others charged higher interest rates to borrowers who demanded loan proceeds in banknotes instead of deposits. The reduction of the Federal debt in the 1880s intensified the problem as evidenced by a decrease in banknotes outstanding from $325 million in 1880 to $123 million at the end of 1890 (Dunbar, 1917, p. 232). This underissuance of banknotes led to several liquidity crises which only U.S. banks suffered because they could not exchange one liability for another—banknotes for deposits—as the public demanded. Instead, they had to pay out



legal tender cash from their assets, thus depleting their reserves, which often led to suspension of cash payments.

By contrast, Canadian banks have not suspended cash payments since the late 1830s. All banks were allowed to issue their own distinctive banknotes without holding a legally mandated asset to back them. These notes were subjected to the daily market test of public acceptance as each bank sought to get its own notes into circulation while simultaneously driving home rival notes to their respective issuers through note exchanges. Furthermore, these banknotes were an inexpensive till money because they were not a liability until issued (Beckhart, p. 377). This reduced the cost of establishing branches in newly developed areas.

Canadian banknotes also had excellent elasticity, expanding and contracting as the demand for them changed. This was especially evident during the autumn when crops were moving to market and the demand for banknotes sometimes increased as much as 42 per cent of the yearly minimum (Curtis, p. 20). During the Panic of 1907, some Canadian banknotes even circulated in parts of the U.S. after American banks suspended cash payments (Johnson, p. 78).

The only government restriction on the issuance of Canadian banknotes was an unnecessary one that proved to be harmful in the early 20th century. No bank was permitted to issue notes in excess of its paid-in capital, which excluded the surplus account. When passed in 1871, no bank had approached that limit, but by 1908, some had. But instead of removing this unnecessary restriction, Parliament passed a special law that year permitting banks to issue notes to an amount 15 per cent over their combined capital and surplus accounts during the crop moving season if banks paid a 5 per cent tax on this excess issue. Banks obviously disliked this tax so in 1913, Parliament passed another law which allowed banks to avoid the tax if their excess issue were fully banked by deposit of gold in the newly-created Central Gold Reserve in Montreal (Neufeld, p. 108). Banks in Canada had only about a year's experience operating under these new provisions before World War I broke out which saw the Canadian government undertake inflationary wartime measures, such as suspending the gold standard and permitting banks to borrow fiat base money from the Minister of Finance.

## Emergency Currency: The Illegal Clearinghouse Loan Certificate

In times of crisis when U.S. national banks were forced to suspend cash payments, these banks cooperated through their respective clearinghouses to issue a free market money which, though illegal, worked quite well in preventing the contagious runs that were to implode the whole system in the early 1930s. The clearinghouse allowed unit banks to put up a united front in times of panic by marshaling the resources of all the members, thereby stretching the scarce supply of currency. The clearinghouse would authorize the issuance of loan certificates which banks with deficits could use instead of regular currency to settle their balances after these banks pledged acceptable securities as collateral. Banks holding surpluses accepted these loan certificates as payment to earn the 6 per cent interest that was paid on them (Timberlake, pp. 4-6). If a deficit bank failed and the collateral was insufficient to cover the loan certificates, the members of the clearinghouse had to share the loss.

During the Panics of 1893 and 1907, clearinghouses used small denomination certificates for hand-to-hand currency in addition to large denominations to settle their balances (Noyes, pp. 20-22). The public obviously preferred legal currency to these small certificates as evidenced by the fact that the makeshift currency usually fell to a discount until suspension of cash payments ended (Andrew, pp. 507-509). Yet these free market arrangements mitigated each panic by preventing the fractional reserve collapse that was to occur after the Federal Reserve was in operation. On the other hand, it is possible that these crises would not have occurred at all if U.S. banks had been allowed to issue banknotes without restrictions, to branch where they wanted, and not made to hold a useless cash reserve.

## Emergency Currency: The Legal Aldrich-Vreeland Banknote

In the aftermath of the Panic of 1907, Congress passed the Aldrich-Vreeland Act of 1908 which authorized national banks to issue a legal emergency currency until a permanent solution could be found. This law, which was to expire on July 1, 1914, attempted to overcome two of the three shortcomings of the national bank system: the lack of branching and the rigid restrictions on issuance of banknotes. Any ten or more national banks with an aggregate capital of at least $5 million could form a national currency association to issue notes backed by commercial paper or other securities, rather than just the 2 per cent government bonds to which banks had been restricted. These new banknotes, for which all banks in the association would be liable, could not exceed 75 per cent of the market value of the securities backing them and, in addition, could not be issued until the banks in the association had regular government bond-backed banknotes outstanding equal to 40 per cent of their capital stock. Congress further imposed a 5 per cent tax on this emergency currency for the first month of its circulation and this tax was to increase by 1 percentage point a month until it reached a maximum of 10 per cent (Comptroller 1908, pp. 73, 75).

Even though 21 national currency associations were formed during the next 6 years, no emergency currency was issued, either because the tax was considered to be excessive, or no occasion warranted it. Congress passed the Federal Reserve Act on December 23, 1913, but the new System did not begin operating until November 16, 1914. However, the Federal Reserve Act extended the provisions of the Aldrich-Vreeland Act for one year, until July 1, 1915. Ironically, had it not been extended, the Act would have expired before the need to use it arose. Congress also reduced the tax on the emergency currency to 3 per cent for the first 3 months it was outstanding, after which the tax was to rise by half a point each month until a maximum of 6 per cent was reached (Comptroller 1914, p. 12-13).

The occasion for using the new currency was the crisis following the outbreak of World War I in August 1914. Foreign holders of American securities tried to liquidate them for gold, and depositors tried to convert their deposits into currency, both of which put extreme pressure on bank reserves (Sprague, p. 517). Before banks could issue the new currency on demand, however, Congress had to repeal the restriction that banks could only issue it if they had bond-backed banknotes outstanding equal to 40 per cent of their capital. Congress responded quickly, even increasing the aggregate amount of notes that could be issued (*Wall Street Journal,* August 5, 1914, p. 6).

For the first time national banks could issue banknotes for deposits on public demand, thereby preventing suspension of cash payments which were so characteristic of past American crises. Even though only 1,363 of the 2,197 banks in the 45 currency associations in existence at that time actually issued the emergency currency, it was the immediate response to public demand that prevented the panic (Comptroller 1915, pp. 92, 99). Only $386.4 million was taken out during the emergency that lasted into the spring of 1915, but $368.6 million, or 95 per cent of the total, was issued by the peak period in October (*Wall Street Journal,* November 3, 1914, p. 1). By the first week of January, 60 per cent had been retired; the remainder was retired by the end of June, except for $200,000 in a failed bank (Comptroller 1915, p. 101).

Less than a fourth of the legal maximum was ever issued, with banks in New York City taking out 37.5 per cent of the total; these banks were the first to issue the currency and the first to retire any and all of it (Comptroller 1915, pp. 100-101). This Act allowed national banks to act as Canadian banks would under stress, issuing banknotes as demanded and saving their gold and treasury currency for use as a reserve. State chartered banks could use the emergency currency as part of their reserves, but as often happens, once they realized this currency was readily available, they, along with the general public, stopped demanding it. Much of the emergency currency sent to the interior was later returned to New York in its original wrappings (*Wall Street Journal,* November 14, 1914, p. 8).

## Conclusion

From hindsight we know that both legal and illegal emergency currency outperformed the Federal Reserve during the credit implosion of the early 1930s. Banks can respond to market forces if they are allowed to issue banknotes, which are an "inside money" just as are deposits, but they cannot issue "outside" Federal Reserve Notes. When the public found out that currency was not available, they demanded it all the more, precipitating the fractional reserve collapse during the depression.

The problems of pre-1914 banking in the U.S. involved too many government restrictions, not too few. Politicians may have believed that private banking was unstable, but had they looked to the Canadian model as a guide, they could have concluded that market forces can give us a successful banking and monetary system just as it provides us with food, clothing, and other necessities. □

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A REVIEWER'S NOTEBOOK

# Out of Step: An Unquiet Life in the Twentieth Century

by John Chamberlain

Sidney Hook's *Out of Step: An Unquiet Life in the Twentieth Century* (New York: Harper and Row, 628 pp., $29.95) is the story of an inspired career that has been responsible on more than one occasion for saving the United States from the disaster of a too trusting agreement with the Soviets.

A professor of philosophy at New York University in the Nineteen Twenties and after, Hook was a foremost disciple of John Dewey. This committed him to a credo that has always seemed to me to have its porous aspects. But porous or not, it never kept Sidney Hook from taking positions that were firmly against totalitarianism of any sort.

Before going into the subject of Hook's lifelong career in fighting for freedom as a pragmatic good (which it certainly is), I should perhaps indicate the source of my own differences with Hook and Dewey himself. My trouble with Hook is rooted in the Deweyite use of the word "intellectual."

Midway in his book Sidney Hook breaks off to state his own secular humanist credo. "I have held the lifelong conviction," he says, "that faith in the existence of an all-powerful and all-loving god has no more intellectual justification than faith in the existence of a cosmic Santa Claus, and I agree with Marx that the critique of religious abstractions is strategic to the critique of all reified abstractions."

Bringing in Santa Claus and raising the question of a god's lovingness are distractions from the issue of the so-called argument from design, which is a wholly intellectual construct. Since Hook is committed to a defense of the human mind, he should think twice before rejecting the argument from design as something rooted in mysticism. Either the universe is the result of a series of unpredictable accidents, or it has some preordained order. It is only logical to suppose that some guiding presence that is otherwise completely mysterious is behind the creation of our world. Hook is free to reject any particular logic, but he can't say that the intellect is not involved in tilting toward acceptance of the argument from design.

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Sidney Hook

As it turns out, Hook is perfectly willing to discount the importance of his own credo about ultimates. He says that religion is a private matter. Dismissing arguments about divine purposes, he says "I just as strongly hold that freedom of religious belief (or unbelief) is integral to any morally acceptable schedule of human rights. I am therefore prepared to make common cause with believers in religious freedom against every form of totalitarianism, religious or secular."

This brings matters back to the real importance of Sidney Hook's autobiography. He has been "out of step" with the events of seven or eight decades in the matter of temporary response. But fortunately for all of us, events have always worked out in a way to justify Hook's expectations.

Hook is amusedly rueful about this business of being "out of step." "I was prematurely anti-war in 1917-1921," he writes. He was also "prematurely anti-fascist, prematurely a Communist fellow-traveller, prematurely an anti-communist, prematurely (in radical circles) a supporter of the war against Hitler, prematurely a cold warrior against Stalin's effort to extend the Gulag Archipelago, prematurely against the policy of detente and appeasement, prematurely for a national civil rights program and against all forms of invidious discrimination, including reverse discrimination."

## Foreseeing World Conflict

Hook might just as well have entitled his book "Ahead of the Game." He was not the first to see that German nationalism would take an ugly turn in the Nineteen Thirties. But his experience in Munich and Berlin on a Guggenheim grant in 1929 convinced him that the thoroughly justified German animus against the Versailles Treaty would, in the absence of intelligent action by the League of Nations, result in a new world conflict.

He didn't manage to foresee the course of Stalinism when he was in Moscow at the end of the Twenties, but he sensed that something was amiss when Stalin struck against both the Left and the Right in order to rid himself of any opposition in the Politburo. The starvation of the kulaks in Stalin's man-made Ukraine famine of the late Twenties and early Thirties was no surprise to Hook. Nor were the Moscow trials of the mid-Thirties an unexpected thing.

Where other people may have anticipated Sidney Hook in identifying and reporting trends, nobody could beat him in the business of mobilizing intellectual opinion against totalitarianism in constructive ways. Hook put together many intellectual coalitions (the American Committee for Cultural Freedom and the international Congress for Cultural Freedoms are two examples.) His most important work was in rallying American intellectuals to the defense of Trotsky's right to an asylum in Mexico. He persuaded John Dewey to head a committee that not only established the right to asylum, but also absolved Trotsky of charges made against him and his son Leon Sedoff in the Moscow Trials. The importance of the Dewey "preliminary commission of inquiry at Mexico City" had little to do with the question of Trotsky's revolutionary theories. What John Dewey was after was an opportunity to prove that the right to a fair trial should belong to anybody, revolutionaries included.

Hook persists in being a socialist in a time when more and more intellectuals (the neo-conservatives) are finding new justifications for capitalism. But he has learned from recent history that the property right cannot be dismissed with impunity if there is to be individual freedom in the world. I remember the day when Sidney Hook, when challenged, defended the right of possession with some heat. "Not my little place in Vermont," he said when a heckler sought to challenge his possession of a few acres of Green Mountain vacation ground.

Hook commends Norman Thomas for coming around to the belief that if the State has too big a role to play in economic planning, the potential for totalitarian takeover is vastly enhanced. But the question of how to limit a mixed economy in a way to preserve fundamental property rights is not resolved in Sidney Hook's book. When Hook comes up against a contradiction in the terms of discourse he often heads for the nearest exit.

Intellectual inconsistency, however, has not kept him from writing a magnificent chronicle of our times. He not only recalls such vivid figures as Max Eastman, Bertrand Russell, and

Robert Hutchins, he also resurrects many interesting minor characters such as Sol Levitas and V. F. Calverton, whose magazines provided a forum for radical dissent beyond the leftist orthodoxies of *The Nation* and *The New Republic.*

There is richness in everything that Hook writes. As Jeane Kirkpatrick says, his book is required reading for those who care about freedom. □

**REGULATING GOVERNMENT: THE POSITIVE-SUM SOLUTION**

by Dwight R. Lee and Richard B. McKenzie

Lexington Books, D. C. Heath and Co., 125 Spring Street, Lexington, Massachusetts 02173 • 1986 • 206 pages, • $22.95

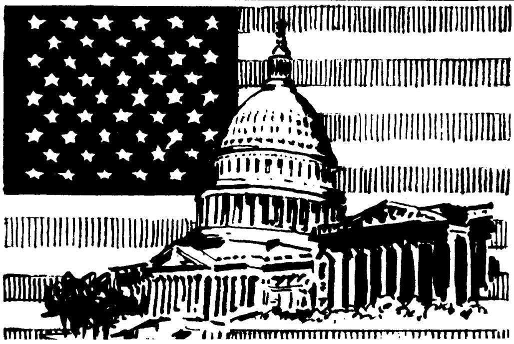
*Reviewed by William H. Peterson*

Quite a few journalists and intellectuals were bewildered late last year when James Buchanan won the Nobel Prize in Economics for his theory of public choice.

James Buchanan? Public choice? What goes on? Fortunately, a book comes along which applies, in a timely and illuminating fashion, the ground-breaking yet commonsensical work of Buchanan and his fellow thinker, Gordon Tullock, both of whom are professors at George Mason University and distinguished members of The Mont Pelerin Society.

The book is *Regulating Government,* a valuable study by two students of Buchanan and Tullock at their Center for the Study of Public Choice. Dwight Lee holds the Ramsey Chair of Private Enterprise at the University of Georgia; Richard McKenzie serves as professor of economics at Clemson University and senior fellow at The Heritage Foundation.

The Lee-McKenzie thesis is plain: Public choice theory assumes, rather persuasively, that voters, legislators, and bureaucrats act mainly in their own interest, that political science and economics are thereby tied together in terms of incentives, that accordingly what we Americans need now is not regulation *by* government but regulation *of* government.



For government today, point out the authors, is a lot more than a referee; to quite an extent it is a participating player. It educates our children, aids foreign nations, delivers the mail, runs Amtrak, pensions the old, and much more. In the case of agriculture, government forces citizens to pay for unwanted or "surplus" farm goods—making them public goods—which it proceeds to buy, store, and hand out in the form of school lunches, senior citizens nutritional programs, low-income surplus butter and cheese distributions, and Public Law 480 "Food for Peace" foreign donations.

Professors Lee and McKenzie thus clarify some of the vital distinctions between private goods and public goods. Private goods engender conservation and positive-sum trade—trade which synergizes mutual gain. Public goods engender waste if not plunder—zero- if not minus-sum "solutions" to social opportunities which hence become social problems.

Cows and chickens, for example, are private goods, and nobody sees any chance of shortages or "endangered species" in such goods. Snail darters and blue whales, on the other hand, are declared to be endangered species and thereby, in effect, public goods. Accordingly, people who otherwise place high value on individual freedom urge not privatization of whaling (which is technically possible) but government controls on whalers.

Drs. Lee and McKenzie are anything but anarchists; they are Lockeans, holding that the end of law is not to abolish or restrain but to preserve and enlarge human liberty. In this year of our Constitutional Bicentennial, these two Public Choicers make the point that the raison d'être of constitutional constraints on government is to prevent people from doing through government that which they would not do in the absence of government. The very purpose of constraints on government is the same as the purpose of government. Here they echo James Madison who, in arguing for ratification of the U.S. Constitution, wrote in *The Federalist:*

*If men were angels, no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary. In framing a government which is to be administered by men over men, the great difficulty lies in this: you must first enable the government to control the governed; and in the next place oblige it to control itself.* □

**Frances Kendall and Leon Louw, authors of *After Apartheid: The Solution for South Africa,* were visitors to Irvington last December, where they spoke to a gathering of FEE Trustees.**

## AFTER APARTHEID: THE SOLUTION FOR SOUTH AFRICA

by Frances Kendall and Leon Louw

ICS Press • 243 Kearney Street, San Francisco, California 94108
250 pages • $17.95 hardcover.

*Reviewed by Bettina Bien Greaves*

South Africa's situation is desperate. English, Afrikaners, blacks, coloreds, Indians, and other minorities are fearful. Many blacks, resenting the restrictions imposed on them, resort to violence. In view of the fact that so much power is centralized, the demand for radical reform has become a struggle for control of the national government. World opinion, incensed at the immorality of apartheid, threatens economic sanctions, or worse.

The white minority in power in South Africa makes *some* concessions to the black majority, but is reluctant to shift to a one-man, one-vote democracy. Given the prevailing climate of opinion, it is feared that this would mean one man, one vote *once!* If such a vote resulted in a more tyrannical central government, the rights of minorities would inevitably be further impaired. The chances for bringing about social change by peaceful means would also then be lost.

The South African crisis led Leon Louw and Frances Kendall, a husband and wife team, to write a remarkable book about their native land. A quote from black leader Allan Boesak became their text: "Change does not roll in on the wheels of inevitability. It comes through the tireless efforts and hard work of those who are willing to take the risk of fighting for freedom, democracy, and human dignity."

The Louw-Kendall book offers a radical, but realistic, proposal for a new kind of constitution. The authors blame the currently depressed situation of the black South Africans on the fact that they have been forced to live under socialist restrictions. In the past, when blacks were free to embark on enterprises as they chose, their accomplishments were so impressive that the white minority strove purposively to restrict their efforts. And then the whites made sure that the central government remained under their control.

Laws were enacted over many decades making it difficult or impossible for blacks to succeed in farming or other enterprises. Legislation deprived them of their rights to own, accumulate, and transfer property freely, to make contracts, and to go into business. It is no wonder that the blacks are now desperate. However, Louw and Kendall maintain that most blacks are not fiery militants who refuse to listen to reason. Rather, Louw and Kendall believe most blacks are moderates who would be willing to live at peace with their neighbors if assured that their lives and property would be protected and that they would not be constantly harassed by "blacks-only" rules and regulations.

Louw and Kendall suggest a completely new political arrangement for South Africa—a confederation patterned more or less on the Swiss model. The central government would be limited drastically; many small cantons would be entrusted with most of the matters that concerned the people. The crux of the Louw-Kendall proposal is a powerful bill of rights, granting freedom to own property, to make contracts, to trade, to move, and so on. Under the Louw-Kendall scheme, all citizens of voting age would have the franchise, but the power of the central government would be so limited that national elections would be relatively unimportant. The important votes would be those at the canton level, for it would be in the cantons that matters affecting individual rights would be decided.

The Louw-Kendall book has become a best seller in South Africa and it is now being released in a new, slightly revised U.S. edition. Because of the authors' success in introducing free market ideas in the small poverty-stricken black homeland, Ciskei, the fellow countrymen of the authors are beginning to take their suggestions seriously.

The change Louw and Kendall recommend is a radical one, but it is a reasonable one which should appeal to reasonable men and women—blacks, whites, coloreds, Indians, and every other fair-minded person. Certainly, any reasonable alternative that offers hope for reducing the strife in South Africa is well worth considering. ☐

*(Mrs. Greaves is on FEE's senior staff.)*

**Freeman** readers may order copies of ***After Apartheid*** at $17.95 each (includes shipping) from Laissez Faire Books, Department FEE, 532 Broadway, New York, NY 10012, (212) 925-8992.