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Richard A Epstein

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He has been a member of the American Academy of Arts and Sciences since 1985 and a Senior Fellow of the Center for Clinical Medical Ethics at the University of Chicago Medical School. He served as editor of the *Journal of Legal Studies* from 1981 to 1991, and since 1991 has been an editor of the *Journal of Law and Economics*.

His books include *Torts* (Aspen Law and Business, 1999), *Principles for a Free Society* (Perseus Books, 1998), *Mortal Peril: Our Inalienable Right to Health Care?* (Addison Wesley, 1997), *Simple Rules for a Complex World* (Harvard, 1995), *Bargaining with the State* (Princeton, 1993), *Forbidden Grounds: The Case Against Employment Discrimination Laws* (Harvard, 1992), *Cases and Materials on Torts* (Little, Brown, 5th ed, 1990), *Takings: Private Property and the Power of Eminent Domain* (Harvard, 1985), and *Modern Products Liability Law* (Greenwood Press, 1980).

Professor Epstein has written numerous articles on a wide range of legal and interdisciplinary subjects and taught courses in contracts, criminal law, health law and policy, legal history, property, real estate development and finance, jurisprudence and taxation, torts, and workers' compensation.

Introduction by
Gary Judd QC¹

The philosophical starting position of tonight's speaker is that state power should be confined to counteracting the dangers of force and fraud, and generally should not go beyond that. Similar sentiments were expressed nearly 150 years ago by a French writer. In 1850, when France was being seduced by the false promises of socialism, Frederic Bastiat wrote his monograph *The Law*. Under the heading 'The Seductive Lure of Socialism' he stated:

Here I encounter the most popular fallacy of our times. It is not considered sufficient that the law should be just: it must be philanthropic. Nor is it sufficient that the law should guarantee to every citizen the free and inoffensive use of his faculties for physical, intellectual, and moral self-improvement. Instead, it is demanded that the law should directly extend welfare, education, and morality throughout the nation. This is the seductive lure of socialism. And I repeat again: these two uses of the law are in direct contradiction to each other. We must choose between them. A citizen cannot at the same time be free and not free.

These days we tend to associate socialism with Soviet communism, forgetting its roots in European philosophy and the various political movements spawned by that philosophy. In his most recent book, *Principles for a Free Society: Reconciling Individual Liberty with the Common Good*, Professor Epstein draws attention to the writings of Rousseau prior to

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the French Revolution. In his *Discourse on the Origin of Inequality*, published in 1755, Rousseau demonstrated his hostility to private property when he exclaimed:

What crimes, wars, murders, what miseries and horrors would the human race have been spared by someone who, uprooting the stakes or filling in the ditch, had shouted to his fellow-men: Beware of listening to this impostor: you are lost if you forget that the fruits belong to all and the earth to no one.

Bastiat, by contrast, stressed that state-enforced altruism was incompatible with liberty. Under the heading 'Enforced Fraternity Destroys Liberty', he said:

Mr de Lamartine once wrote to me thusly: 'Your doctrine is only half of my programme. You have stopped at liberty; I go on to fraternity.' I answered him: 'The second half of your programme will destroy the first.' ... I cannot possibly understand how fraternity can be legally enforced without liberty being legally destroyed, and thus justice being legally trampled underfoot.

Professor Epstein's starting position is not dissimilar but in his writings he does examine those special circumstances in which government may legitimately go further.

Professor Epstein is the James Parker Hall Distinguished Service Professor of Law at the University of Chicago, where he has taught since 1972. In addition to a distinguished teaching career, he has been a member of many professional bodies, authored numerous articles on a wide range of legal and other subjects, and written a number of books.

In his work and writings Professor Epstein has sought to find and articulate a principled reconciliation between liberty and the structures of modern society. His book *Principles for a Free Society*, published last year, includes an examination of altruism – that 'fraternity' which Bastiat saw as incompatible with liberty, if pursued by the state. On the way to the conclusion that "less [state] altruism leads to less political conflict, and to more responsible individual behaviour", Professor Epstein makes a point that must surely strike a chord with New Zealanders. Speaking of the

American social security system, he says:

What started out as a system of public sharing has ended up as an intergenerational struggle in which the joys of altruism are experienced only by those fortunate enough to be picking the pockets of the next generation.

With that taste of what is in store for us, it gives me great pleasure to welcome Professor Epstein and to invite him to address us.

Principles for a Free Society

The kind introductory remarks of Mr Judd provide a valuable framework for my topic. And his invocation of Frederic Bastiat offers an instructive, if unintended, way to frame this lecture. Bastiat harboured a deep suspicion of the power of government. Accordingly, he operated from the general presumption that government power should be restricted to controlling force and fraud – a view I certainly endorse. He also recognised that we need to consider exceptions to the general rules. But he warned that we do not want the exceptions to go so far that we find ourselves battling to resist the encroachments of socialism.

Under socialism, redistribution between individuals occurs, not through charity or compassion, but simply through coercion. The level of so-called benevolence is determined through political processes, which are strongly influenced by the recipients of a transfer payment rather than by the decisions of free donors. Our task is to create a set of collective arrangements that allow us to move beyond the prohibitions on force and fraud, where appropriate, but to do so in a way that allows us to restrict the scope of state action so that government itself does not become the agent of illicit redistribution. We do not want everybody believing that the appropriate way to earn an income, win a fortune, or obtain property is to pick the pocket of the person sitting next to them. Such a state is most undesirable, because each time a pocket is picked, the amount available for the next pickpocket is a little less. If we repeat that process often enough, too much social wealth will eventually be lost in the transfers. There will be too little remaining, either for people to use

productively themselves or to give to others. It is a major challenge to organise a society that works its way through these trade-offs between the proper use, and the dangerous abuse, of government power.

Reconciling private choice and state monopoly

Understanding how this challenge can be met forces us to think about the fundamental nature of economic and social activity among individuals. We possess an ideal of liberty, whether manifested in the so-called theory of natural rights or in a consequentialist approach to social policy that is driven more by evaluating outcomes in terms of the well-being of individual citizens. Both approaches lead to similar conclusions. A world with free and open markets, in which people can choose their trading partners, will outperform any system involving constrained choices for individuals and extensive duties of forced association. We therefore seek an open arena for association and exchange, in which the existence of choice by others is the main constraint on the arbitrary behaviour of any particular individual or group. In such an arena, people encountering arbitrary behaviour can simply switch their allegiance to other traders rather than battling with a single provider of a good or service. That is one reason why the argument for restricting government activities to controlling force and fraud is so strong. In a nation containing many separate individuals, the counterweight to the arbitrary power of one person is the ability of each to shift his or her business, custom or friendship to other people. Given free entry and free exit from various markets, it is that range of choice which offers the securest guide for our liberty. Indeed that is how we each tend to envisage our own private liberty.

But this ideal of freedom through choice does not correspond to a state of anarchy. Certain actions against others will be intolerable – above all the use of aggression. Unfortunately, it is impossible to secure a series of voluntary contracts among private individuals sufficient to stop all aggression amongst them. We might, for instance, wish to protect ourselves against the worst aggressor in the world, who may be threatening to do

us serious harm. We might enter into a peace treaty with that person and pay a ransom. But by such partial actions we have not obtained peace: we have simply invited the second worst aggressor in the world to come after us and demand a similar exaction. Thus if we extended this approach to all individuals at all times, we would need such a huge number of bilateral contracts to control the use of force that we could never satisfactorily do so. Owing to these deficiencies, we need to accept and enforce some collective and social understanding about the mutual renunciation of force as a way of doing business amongst individuals.

But who will be the enforcer? Unfortunately, to obtain genuine enforcement, we must wistfully turn our gaze away from the flickering light of liberty and embrace the unlovely spectre of government monopoly. We cannot have two referees acting as enforcers if one can decide that A will win while the other decides that B will win. In disputes between individuals over the boundary of their properties or the interpretation of their contracts, there can be no common master if each party is entitled to its own authoritative referee. The moment we allow one common master, we inevitably create a system involving monopoly power. The great problem is to reconcile as best we can the tension between these two imperatives – the monopoly vested in government and the free choice that we wish to see retained by individuals.

While that is a difficult enough problem, it is not the only one. In the general organisation of society, our usual intuition is that free and voluntary exchange through private property should predominate. We have sound reasons for disliking monopoly. But there is a complicated and interesting feature about people as they go about their daily lives, whether today or in any other era: they are constantly forced to take into account the interaction between their activities on private property and those on public property. In their sensible but unreflective style, they make the transition amazingly well. When they require a network to get themselves or a product from point A to point B, they must put together some form of social infrastructure – building roads, organising sea transport, or creating networks to run railways, telecommunications and

electricity. And while we can privatise most of these operations, some form of state power must be retained in order to keep the networks open. Thus, obtaining the optimal structure for these network industries requires accepting some degree of regulatory power, and then understanding how we can best constrain the way in which that power is used.

The most modern manifestation of this problem is interconnection arrangements in telecommunications. There is a wide difference of opinion over how these are best handled. There is an even wider difference in performance between, for instance, the relatively efficient telecommunications system in New Zealand and the rather ramshackle system in Australia, even though the two countries face the same basic problem. The United States is somewhere in between New Zealand and Australia, perhaps lumbering along closer to Australia. For centuries the whole question of how to organise infrastructure has been a major problem confronting societies. Writing in the seventeenth century, the distinguished English legal historian and author Lord Matthew Hale said that for state-created monopolies or networks, there would need to be clever systems of rate regulation or pricing, so that exorbitant charges were not imposed on individuals. Hale clearly understood that excessive charges would lead to fundamental resource misallocations. Thus there are two types of exceptions to the rules allowing individual choice – the civil enforcement function and the infrastructure provision function. The problem of a free society is to find a set of legal rules that enables us to maintain the best balance between necessary state monopoly and individual freedom.

Recapitulating the simple rules

Dealing with the principles governing a free society takes me back to 1990, when I first visited New Zealand and Australia. I talked then about simple rules for a complex world. In putting together a legal structure that reconciles private competition and state monopoly, while avoiding socialism, I believe the rules I then proposed best answer the basic challenges.

The first rule is one of *individual autonomy*. It is a very innocent rule to state, but profoundly important to endorse. Individuals own their minds and bodies, and control their various faculties, talents and abilities. It is not that morally they can do anything they want with their bodies, but that they are the only party who legally can make decisions concerning their own persons. The justice of the autonomy rule is easily apparent if we contemplate other possible rules. For instance, one could imagine a rule that required divided ownership of the person. If any individual wanted to do something, they would need the approval of all the rest of humankind. But the rest of humankind would hardly be in a position to give that approval, because none of them would any longer own their own faculties either. Since they are themselves subject to collective ownership, their faculties would also be under divided authority. Another alternative and unsatisfactory rule might be a system of slavery. Or we could decide that nobody can really decide what anybody can do, because the creation of rights in individuals is wholly arbitrary and to be rejected – a post-modern approach designed to maintain psychological and legal chaos for all concerned.

But if we start with rules such as individual autonomy, they turn out to be immensely durable. We cannot imagine major changes in political or economic structures that would lead us to abandon or modify such a rule. This is reinforced by any historical survey, from Roman times (Roman law was where I started my legal education) up to the present day. When rules serve such a dominant social function, they almost invariably come to be endorsed as natural law.

There is a peculiar convergence of two traditions in the way in which we think about the principles of a free society. There is a feeling that some rules are almost God-given, or invariant, or laid down by nature. At the same time we have strong utilitarian and functional justifications for the same rules: it is claimed that other rules would lead to social consequences so bad that nobody would want to endorse them. There is thus a great deal of often unappreciated common ground between what lawyers and philosophers sometimes call the deontological approach and a

consequentialist or functional approach. The deontologist believes we understand justice in any particular dispute by relying on certain antecedent principles of right and wrong, while the consequentialist or the functionalist uses outcomes as the justification for any position. On reflection, I believe there is a false antithesis between these two approaches as measured by the results they support. We have confidence in the norm of individual autonomy, not because it is divinely inspired but because it is humanly functional. It is not possible to find an alternative that will allow people to have as much as they want, consistent with the desires of others.

In the light of this general approach, the second step in establishing our rules for a free society is to find mechanisms for matching *property* with individuals. This is complicated by the fact that sometimes property should be held in common and sometimes in private. Here classical liberals like Bastiat, who did not have the perspective of a lawyer, had too great a tendency to focus exclusively on the superiority of private property with respect to a wide variety of goods and services, as well as resources such as land and labour. In the process, he forgot that resources like waterways and airways were often held in common. Half the basic theory of property rights is essentially that of Bastiat, but there is another half which complements his picture. We need a reasonably coherent theory distinguishing the two types of ownership. For the moment I want to concentrate on those forms of property, such as land and chattels, which are privately owned. With respect to these, two additional functions have to be served, one of exchange and the other protection, and these are the objects of our third and fourth rules.

Accordingly, the third essential rule for a free society concerns *contracts*: if we need rules both for giving people the ownership of their labour (the autonomy rules), and for giving people the ownership of land and other forms of property (property rules of first possession), we next need a system of rules for voluntary exchange, so that resources owned by one

person can be transferred to another. The most important feature of rules of voluntary contracts is the ability they confer on people to multiply gains through piling transaction upon transaction upon transaction. A good transactional lawyer is not somebody who can simply work through the mechanics of a sale. He or she is somebody who understands how to structure multiple sequences of voluntary transactions. Out of a very simple principle we get joint ownership, the lending industry, the sale industry, the leasing industry, and indeed all manner of businesses by a constant and repetitive application of these transactions.

Then in order to make this system secure, we need the fourth and last of our basic rules – rules of protection that we call the *law of tort*. Once again the basic theory informs us of the formation of the rule. There are only two choices we have for the transfer of labour and property between individuals: voluntary exchange or coerced transaction. If the former generates mutual gains, then the latter most certainly does not. The central office of the law of torts is to direct most human interactions into the voluntary arrangement by prohibiting one individual from taking or destroying the property of another. The most obvious danger from this quarter is of course deliberate harms, and it is to these that the tort law is first directed. But some additional protection must be given against the accidental destruction of property by others as well, lest we all succumb to the temptation of ignoring the harms that our actions inflict on others in our efforts to secure benefits to ourselves. There are of course certain limited cases – involving the so-called doctrines of 'privilege' – in which one individual may take the property of another in order to avoid some imminent peril to their self. These cases show that on rare occasions forced interactions can yield social gains. But it is important to stress that while these are theoretically important, they constitute only a tiny fraction of involuntary interactions between strangers. The strong presumption is that the tort law must work to keep people apart, so that they can bring themselves together voluntarily.

Private and common property

The first four rules work well with interests in labour and property that are conveniently made private. It is there that thinkers like Bastiat understand why we do not want, and cannot endure, a social system that tolerates aggression against individuals, where 'aggression' is the act of a stranger imposing losses on one person in order to generate gains for another. But our analysis is not yet complete. There is another problem which goes back to the issues relating to network industries. Often, the gains to one individual from contracts will depend, not merely upon securing a single trading partner, but upon the more daunting task of securing the unanimous consent of all individuals. That is exactly the familiar problem of social order generally. If there is a contract in which people agree not to use aggression against anyone else, a single person outside the network can disrupt the peace for every other individual. In other words, we have an immense coordination problem. We may be forced to use coercion where the dangers of one person holding out are so great that they could disrupt the overall system. The New Zealand Public Works Act 1981, under which land may be taken for public purposes provided compensation is paid to the owner, is an example of such a mechanism. Under any system of property rights, there is almost invariably a trade-off between the externalities created by aggression and the holdout problems when certain common pool resources must be introduced or controlled by unified management. Dealing with land, chattels, water and air space involves a constant tension between these two problems. Thus, a society concerned about the advancement of the common good will not generate a relentless pressure towards private property in all circumstances, but towards the creation of certain common properties as well.

In merely talking about common properties, does this mean we are falling into the trap that writers like Bastiat so much feared – that the moment we have common properties and common goods we will lurch into socialism? Socialism is, of course, not very far away, because the very

word means collective ownership over the means of production. But the answer to that question is happily in the negative, at least if we approach it from a sensible theoretical perspective that understands the place for common property. It is here that we also find a place for forced exchanges, instituted by government, upon payment of just compensation to those deprived of their property or otherwise restricted in its use.

In order to keep the intellectual lines clean, it is critical to draw one key distinction. We create a system of common property to make sure collective endeavours can take place in those circumstances where it is just too difficult and costly to organise common contracts amongst all individuals. From that fact, it hardly follows that we want collective ownership of the means of production to be a disguised method of transferring wealth from A to B. A system of social insurance will not run the risk of redistribution if it takes from everybody and gives everybody in return something of greater value than each person surrendered. But a system that takes from one group of individuals and provides benefits to a different group not only runs that risk of redistributing, but also invites that outcome. Thus, with many systems of social insurance, it is important to determine whether or not the benefits and burdens run in parallel. If they do, a principle of reciprocity will typically mean that everybody gains from the transaction. If they do not, it is a telltale sign of illicit government action.

In thinking about the common good, therefore, we must always be careful to consider whether the relevant definition of the 'common good' is collective or individualistic. Under the collective definition, if group A benefits while group B is harmed, that transfer could be in the common good – if we decide the transfer is justified by some principle of political philosophy. But if we take seriously the idea of individual autonomy, then we will consider the common good to be advanced only to the extent that all citizens within a society benefit.

This distinction between the collective and individualist definitions of the common good suggests that the most important principle of natural

justice is often the idea that when the government takes for the benefit of the public at large, it should ensure that the burdens are not disproportionate by providing compensation to the losers. Under the ideal compensation mechanism, the losers will be compensated up to the point where they are indifferent between the property they were forced to surrender and the compensation received. One of the difficulties with many classical liberal formulations of individual liberty and the common good is that they tend to underestimate the complexity, difficulty and dangers associated with thinking through the practical implications of the just compensation principle. I have undertaken work on the takings clause in the American constitution, which deals with just compensation. But that analysis is not confined to either the American or legal context. It arises whenever the question of social coordination has to be fairly addressed. When confronted with complex systems of social regulation, it takes an enormous effort for us to get the balance right.

The issues confronting telecommunications systems provide a good illustration of the basic problem. In constructing a network, we typically want the interconnections to work so that everybody in the network is better off, given the combination of costs and benefits they face, than if no network had been possible. But in the United States, under the guise of the universal service obligation, and in New Zealand under the Kiwi share obligation, massive amounts of redistribution can take place, only partially obscured, within this programme. Hence, it becomes very easy in political life to confuse the two rationales for collective action. One rationale is to overcome holdout problems, while the other is to undertake various forms of redistribution. In a comprehensive and systematic theory of individual liberty we must be constantly alert to this distinction. We must use all our intellectual powers, and all our legal skills, to apply that distinction correctly. In the end, the concessions we make to collectivism will lead to a higher level of public ownership than a pure libertarian might desire, yet may still ward off the truly dangerous tendencies of socialism.

In distinguishing the collective definition of the public good from the individualistic, we have been talking about forced exchanges, that is, those exchanges associated with the social contract. To see the power of the term 'social contract', we need to take the words one at a time, and they will lead us back to the general dominance of private markets.

Recall, for these purposes, the definition of a contract. In a contract each person takes something they own – whether it be their liberty of action, or property they possess – and surrenders it to somebody else in exchange for something in return. The hallmark of a voluntary exchange – and the voluntary principle is one we must constantly stress – is that it leaves both parties to the transaction better off than they would have been in the absence of the transaction, as measured by their own subjective evaluation of the exchange. We like voluntary trade precisely because it generates these mutual gains. *Social* contracts are those contracts that people cannot make for themselves because the obstacles to the transaction are too large, and so we have a forced exchange in the manner already described. We take from one person but avoid the charge of aggression by giving that person something of equal or greater value in return. Thus, in theory we are promoting the common good while not trampling on the rights of any individual.

But in real life, an actual contract will generally outperform a social contract. For that reason, we should be seeking constantly to introduce new technology that will break down monopolistic barriers and allow voluntary transactions to take place. When we place the whole system into focus, its rules essentially say that when we tax people in order to fund the system, our primary use for that money is to ensure that our infrastructure is maintained, and that individuals cannot attempt shortcuts around voluntary exchange by coercing others into undertaking transactions. In sum, the basic principles of a free society effectively constitute rules of voluntary exchange over individual property rights, owned by autonomous people, subject to the complicated rules associated with forced exchanges and eminent domain and takings, and with taxation to allow the structure to be maintained.

Attacks on the principles of a free society

One of the most striking features about this market economy system is that despite its commendable intellectual coherence and ancient origins, it has fallen into disrepute over most of the world. It is instructive to consider the attacks made on the system, and to assess their credibility.

At one time the attacks in favour of socialism were made in very crude utilitarian terms. It was claimed that through centralised control of the means of production one could devise a social system capable of outproducing capitalism, through avoiding the waste created in a competitive market. The 1930s saw the classic debates between economists such as Oskar Lange (Poland), who argued for socialism, and Friedrich von Hayek (Austria), who defended the market economy. The claim from the socialist corner was: 'My socialist biceps are bigger than your capitalist biceps. You will be forced from the field, because central planning will allow us to harness all the means of production in a way that no system involving private, voluntary exchange can do'. There were some weaknesses in Hayek's counter-argument, but his great achievement was to understand that the decentralised and localised knowledge implicit in markets transmits information through the price system, which, in the long run, is a far better coordination mechanism than anything central planners can imagine, let alone create. The significance of Hayek's work is demonstrated by the fact that today hardly any socialist on the Left attempts to compare biceps. They are forced to look to arguments that are more subtle, more complex, more confusing, more innate, and generally more irrelevant, in order to make their cases limp along. Most of these arguments have a distinct academic flavour, but that does not render them unimportant. We academics are not completely irrelevant, and the immense credibility of socialist ideas in academic circles gives them some influence on public affairs.

One popular argument attacks the assumptions about human psychology presupposed by our rules for a free society. My system (classical liberal) does indeed assume a vision of human nature consistent with our

model of autonomy with voluntary and forced exchanges. Accordingly, once the frontal economic assault has been turned aside, an anti-marketeer can fall back on the claim that we cannot believe in the market because it presupposes an account of individual preferences inconsistent with human psychology, and even logic. Our classical liberal rules do depend for their internal coherence on some degree of stability in the preferences of individuals. If people do not know what they want, and cannot keep those preferences consistent over time, meaningful exchanges will be difficult. It may turn out to be a mistake to surrender today some good in exchange for a different good I will be acquiring tomorrow. For when I gaze into my psyche tomorrow, I may discover that the good I just gave up is now just what I wish to have, and that the good I now possess is something I wish to part with again through exchange. If this occurs often enough, people effectively become so mixed up psychologically that exchanges become almost random activities. Thus it allegedly takes the benevolent hand of the state to rectify this problem by giving people, not what they may crudely believe they want, but what the state in its greater wisdom knows they need.

We refute such an attack by turning to what we know about human psychology, to show that the position being advanced is highly implausible. Most writers in the classical liberal tradition like myself take seriously the biological accounts of human nature. We sense a continuity between the biology of human nature on the one hand, and the question of how best to organise society on the other. It is this continuity which leads people to talk in terms of natural law as a description of the link between the two.

Two important facts about human nature stand in contrast to the rather chaotic view of human psychology just described. First, there is a certain degree of self-interest built into us all. That is why we have reason to rejoice about other human beings, to the extent that self-interest can often be channelled into great achievement. But self-interest is also why we have reason to fear them, to the extent that people can misuse their

capacities by trespassing against others. Accordingly, it is utterly pointless to create a legal system governing relationships between individuals that presupposes a degree of benevolence towards strangers that none of us possesses. One of the great merits of the classical liberal system is that it allows benevolent feelings to express themselves where they can be quite strong – most particularly with family and close friends. Yet it also gives us an intelligent way to interact with perfect strangers. Some people lament the impersonality of the market. Personally I regard it as wonderful to be able to enter a supermarket, put down some money and buy a can of beans, without the supermarket checkout people telling me all their personal problems and insisting that before they sell me beans I must tell them all about my life as well. We truly welcome the level of impersonality normally associated with such a transaction, because a market system allows us to conserve our emotional energy in dealing with other people. We understand that there is generosity in this world. But we do not want to make too much of a good thing: we also recognise that we have our more limited sides. A market system manages to channel these self-interested energies into socially productive uses, so that we are not afraid of ordinary people making their living by entering into contracts with others. We are concerned only when people use force to achieve their ends.

The second key point about human nature is that our preferences are stable over time. That too comes from evolutionary biology. Biologists do not measure the success of a member of a species in days, hours or weeks, but in its ability to replicate itself over time. Thus human beings will be successful parents only if they can raise their children to be successful parents. This ability demands from parents constancy of purpose – a degree of loyalty that allows them to stand by their children through life, and at a time when those children are helpless. Any theory that sees preferences as shifting and unstable, or socially constructed, or in some sense mere matters of convention, cannot explain the fact that, long before the comforts of today, people were prepared to brave all manner of hazards in order to help their children reach maturity. Thus the idea that we

cannot trust people to enter into exchange because their preference maps are constantly shifting is generally completely misguided.

Another argument against markets is the claim that when classical liberals talk about concepts such as freedom and coercion, they literally do not know what they are talking about. This argument is a conceptual attack: it claims that the very elements of force and fraud, which classical liberals take to be so central to their system, are on reflection deeply debatable and ultimately incoherent. The most influential advocate for this view was the lawyer/economist Robert Hale, who in the first half of this century attacked the definition of coercion in a supposedly libertarian state. According to Hale, every time any individual does anything that some other individual does not want, he has, perhaps unwittingly, engaged in a form of coercion against other people. The illustration he gives concerns an employer in a capitalist system. If somebody comes to that employer wanting a job and is turned down, the refusal to hire constitutes an act of coercion. And if I go into a store, see something that I do not wish to acquire at the price offered and refuse to buy it, then as a customer I have engaged in coercion. If we swallow this definition of coercion, we discover that there is no such thing as freedom, because coercion is ubiquitous. Only where there is perfect harmony of sentiment between all individuals can we say there is no coercion. And perfect harmony amongst all people at all times would of course present no political or social problems whatsoever, since under the heavenly choirs of this utopian state everything would be resolved by unanimous agreement. All the complicated issues we have been grappling with in building up our rules for a free society would long ago have disappeared.

Now the answer to the Hale charge is surely, 'Come on: get real'. Any definition of coercion in which everybody is always coercing everybody else is utterly useless for explaining human relations. If coercion is in such abundant supply that, no matter what we do, we are always engaged in it, it simply becomes nonsense to condemn it. We need to decide the forms of coercion we most care about. We then keep the word 'coercion' for those cases, and remove the term from those activities that do not fit

the definition. We do that easily by recognising the fundamental difference between refusing to make a deal with another person and committing an act of force.

The explanation for this difference is again extremely simple. We cannot have a system of voluntary bargains and exchange unless people can walk away from transactions they do not desire. If refusing to deal really constitutes coercion, then the only way to secure other people's freedom is to enforce a rule of a 'necessity to deal'. But that will guarantee the loss of our own freedom. Since the ability to walk away from a transaction has system-wide consequences that are so positive, we overlook the short-term disappointment felt by people when they make an offer that is not accepted. For instance, if we were sufficiently silly, we could revolutionise the law of marriage on the basis of one suitor's disappointment that some proposal made to another was turned down. We could regard that spurned lover as duly coerced by the decision of the other, and introduce a system of forced marriages in which one person must accept a suitor against their will. In reality we understand the nature of intimate human relationships, and so would not dream of applying the Hale definition in such a context.

This does not mean of course that refusals to deal are always unproblematic. If there is a single provider of a necessary service, such as the sole railroad linking two cities, a refusal to deal may create genuine problems of monopoly. But while monopoly is a social problem, it is not the same problem as aggression. That is why we can, if we wish, legitimately impose rate regulation on the monopoly railroad, which is not the same as requiring it to service customers free of charge. The entire question of rate regulation has always been enormously difficult: nobody, in nearly 500 years of trying, has devised a system that makes a monopolistic carrier act exactly like a competitive enterprise.

This in turn leads to a much more sober understanding of our human limitations. Some classical liberals like Bastiat always seemed to see things in very black and white terms. The question of whether we can make certain second best accommodations under conditions of uncertainty did

not feature in the Bastiat quotations heard in Mr Judd's introduction to this talk. And a factor that truly drives modern society, and which should give us all some added humility, is the recognition that complex questions of public regulation inevitably involve two types of error. Sometimes we regulate when we ought not; other times we do not regulate when we should. Uncertainty with respect to remedial choice is always there. Consequently we can only ever approach the ideals of liberty, rather than achieve them perfectly.

Two illustrations of this point are worth mentioning. The first concerns simple criminal enforcement. Typically, we can wait too long before neutralising someone who might be about to attack us: the attack may succeed in the interim. On the other hand, if we intervene too soon we may prevent conduct that would have been lawful if allowed to proceed. Questions about whether we give licences to people, for example, to carry guns or drive automobiles, always involve such a trade-off. To resolve these questions satisfactorily, it is not enough simply to be a libertarian. We also need a fairly good estimation of the relevant error cost. The second area of uncertainty concerns monopoly control and regulation: nobody has ever come up with an optimal rate structure. For instance, do we only allow people to obtain a recovery for profitable investments, at which point their rate of return may be unduly low? Or do we allow a normal return on all investments, at which point they have no incentive to avoid losses? These issues have occupied economists for years. Nobody has found the first best solution.

Conclusion

In conclusion, I believe we can go a long way towards avoiding major public policy blunders by staying focused on our fundamental principles. These principles require action to control the use of force. With more caution and a few more qualifications, the principles also require control of private and public monopolies. But we should never assume that we can reach a steady state of perfection. In the real world, the problems of uncertainty will always come back to haunt us. These problems will bring

genuine disagreement among people who accept the same broad conceptual framework, but who nonetheless disagree about specific empirical circumstances. We cannot solve all the problems in the abstract. But with the right framework, we can narrow the areas of disagreement and improve our chances of obtaining the right answer in particular cases. We can also avoid the howlers that occur when, in addition to the usual confusion and uncertainty of ordinary life, we start with the grave handicap of adopting the wrong set of principles. That is a key lesson for us all. We should have confidence in the abstract principles, but caution in our concrete applications. We will then go a long way towards preserving a free society.

Questions

To help structure the discussion, could you perhaps summarise the key ideas in your talk?

The first point is that devising classical liberal rules is a little more difficult and complicated than simply creating laws to minimise force and fraud, because we must also take into account the need to create various public goods. Secondly, it is very dangerous to create public goods without appreciating that we may thereby bring about massive systems of redistribution under the guise of maintaining public infrastructure, and so we must be constantly on our guard against collective action turning into covert socialism. Thirdly, in the enforcement of any legal system, whether the libertarian rules for voluntary contract or public rules for infrastructure and political enforcement, it is not enough simply to have a clear set of objectives. We need to understand the complications that arise under uncertainty. The classical liberals were very good at stating ideals. But they were weaker at offering guidance when we are unsure as to the relative importance of over-enforcement and under-enforcement, such as when we do not understand how to calculate the value of a rate base.

So our basic programme now has two components. The first involves constant attention to the trade-off between controlling force and creating public goods. The second involves understanding how we deal with uncertainty in the provision of both private and public goods. Thus the standard accounts of libertarianism are not complete: they tend to stress

the prevention of force and fraud to the exclusion of the public good side of the equation, and they systematically underestimate the role of uncertainty in fashioning rules that provide relief before the occurrence of harm.

Many countries have recently moved towards the Left. Is this because the market economy message is not getting through, or is it the message itself?

A combination of factors. First, it is not an easy message to get across. One of the difficulties is that if one takes a strong anarcho-libertarian line, one is quickly and rightly dismissed as a quack. If one claims, for instance, that there should only be obligations assumed by consent, people will put you in the 'no taxation at all' camp. In that position, you are simply not credible. People have an intuitive sense that there are public goods, and that we need a theory of optimal taxation rather than a theory of no taxation. The strong libertarian position fouls that up. But once we try to build in all the other key elements, it takes time to explain the message, and we can easily go off the rails.

The second difficulty is that there is a fundamental tension between the ideal I have been outlining and any system of democratic politics. It is always sobering to recall that in a 'democratic' society 51 percent of the voters can confiscate the wealth of the remaining 49 percent. We clearly need social or political mechanisms to prevent that. Fortunately, there are powerful social norms against overt confiscation. But disguised confiscation in the form of political programmes is everywhere, and is the bread and butter of almost every politician. Political programmes are systems of social insurance, and such a system is not a social contract. The American health economist Alain Enthoven has described how medical insurance in the United States involves built-in subsidies to one group of individuals from another. Those who believe this to be an appropriate function for democratic politics must still recognise the propensity of voters to create factions, act strategically, and so on. This means there are forces constantly at work which undermine the rules of a free society.

It is even unlikely that we can preserve a classical liberal order more effectively by employing constitutional mechanisms. That is a lesson we can draw from comparing different democratic systems. The English, Australian, New Zealand and American legal orders all make similar distinctions with respect to the protection of property against arbitrary seizure by government. The government will not force us off our land without compensation, at least without strong justification. But it will regulate us to the death in respect of the use of our property. That is the American position, despite the strong protection written into the constitution, and it is basically the same outcome under Westminster systems. So our great problem with democracy today is how we prevent gigantic and often perverse wealth transfers through regulation. Can we win this battle? There is always somebody who wants any transfer that is mooted. To the extent that they can advance some type of special pleading and call it a general case, there is perpetual political tension between those people who are trying to create the transfers and those trying to stop them. So as a purely factual proposition, it is most unlikely that the political equilibrium in a country such as the United States or New Zealand will involve a zero level of net transfers.

Then there is the question of poverty. Under the traditional classical liberal synthesis, it was understood that the redistributive role of society would not be discharged by the state. Such an understanding involved, and required, a powerful social consensus that the relief of poverty should be undertaken privately. This was always consistent with *laissez-faire*, and with natural rights and natural justice theories. One of the unfortunate features of modern political theory is that we tend to be deeply cynical about imperfect obligations – those moral obligations, such as charity, which are in a sense optional in comparison with a strict duty such as the duty not to kill. We regard imperfect obligations as ephemeral, and this attitude is supported by a weakening of religious and social pressures. Thus we have only two ways of doing things: either we mandate something or we prohibit it. What is striking about modern political discourse is that charitable obligations are simply not part of standard

Anglo-American political philosophy. They are not in Nozick (United States), or Rawls (United States), or any other major twentieth-century political thinkers. Yet charitable obligations were very central to the nineteenth century. If we could re-institute that tradition, we might forge a convincing weapon for fighting collectivism. But the current tragedy can be summarised in a sentence. We write whole libraries about the need to make social transfers to the poor, yet in practice find so many ways to invent transfers to the politically powerful and influential. Any good motivation turns out to be a regrettable cover for bad deeds, whether in the form of privileges for the rich through various tax dodges, or subsidies to dairy farmers (a sore point in the United States and here), or an elaborate set of transfer payments to older people with high incomes from younger people of more limited means.

That is the nature of the political game, and we need to confront fairly candidly and vigorously the transfer society. It is very hard to vanquish it utterly. All I can do is talk and write about these problems and hope that by making people more sensitive to them I can influence behaviour at the margin. But do not expect a miracle. There has been some success in New Zealand because key people understood some of the essentials of sound public policy, and were not afraid to act. The shift to a floating exchange rate may have been only a small action of government, but it was very beneficial to the country. So I do believe ideas matter, and I think one has to work hard in order to make one's own ideas coherent. But there will never be a monopoly of ideas. We all believe in free speech, and we accept that sometimes bad ideas will win out over good ones. In the end, we always hope that we can do our best to alter the equilibrium in ideas by putting forward our own views in a clear and insistent manner.

You talked about the social contract. What happens when lawyers and judges become the state, as they have in this country and the United States, and the body that is supposed to protect us from tyranny is actually the tyrant?

Quis custodit ipsos custodes? Who guards us from the guardians? This has always been the major problem of political theory. Every time you

determine that X will protect us from certain bad outcomes, X turns out to be a villain. We have already discussed the dangers of legislatures. We might in consequence attempt to fashion constitutional rules, in order to limit the power of the legislature. Then we must start worrying about judges, and their frequent habit of deviating from constitutional principles. There is no clear answer that any political theorist can supply. We must simply attempt to choose the set of institutional arrangements that minimises the imperfections. For the most part, a system that divides authority will, in the long run, outperform those that create single monopolies. That is why in the United States we have the separation of judicial, legislative and executive powers, and observe a shifting balance between them.

Even if we adopt the American system, we find the record of its judiciary to be remarkably uneven: in some cases the classical liberal synthesis is completely and robustly enforced by judges, yet in other cases totally ignored. For instance, the enforcement by judges of the constitutional rules on free speech is around 85–90 percent of the ideal – as good as one can reasonably expect from any complex long-term political arrangements. The United States has a system of federalism that is much more complicated than any governing structure in New Zealand. Our judges probably also score around 80 percent when they deal with interactions between the States, but only around 20 percent when dealing with interactions between the States and the federal government. When it comes to freedom of contract and its constitutional protection, our judges are down around the 10–20 percent level. The reason for this pattern cannot be a lack of intelligence on the part of the judges, because the same basic intellectual structure applies. It is rather a question of whether the judges believe the intellectual endeavour is worth undertaking. Unless we can persuade them of that, we can do nothing to solve this particular problem. Moreover, we will never win on a theoretical level if we have nothing to say against the schemes introduced by judges with whom we disagree. We accept that judges must have a monopoly, in order for there to be some system of enforcement. We can

try to change the odds by putting forward our own compelling vision, and hope that somebody will listen, and that gradually we can make progress. So with respect to the judiciary the answer is essentially the same as for the legislature. There have been some improvements and we can try to make further improvements, slowly and persistently, by applying reason to problems.

It is not a very comforting answer, and I am willing to yield to anybody with a better one. But I have been through many such discussions over many years. People say we cannot trust the legislature because it is elected. Then they say we cannot trust the judges because they are not elected. They then suggest we need an executive, but he turns out to be Bill Clinton. So no matter where we turn, somebody will always occupy a role in which their performance is far from ideal. That is the pessimistic assessment. The optimistic assessment is that we have seen some improvements and we might see more, so long as we do not lose sight of the intellectual underpinnings of the free society. I am not a cynic with respect to ideas – I believe they do make a difference. But for every good idea there is a bad idea out there, heading in the opposite direction, which may have greater contemporary allure. One must go after them, and that is what I try to do.

Do you agree that incremental improvement can be important?

Absolutely. In any practical situation it is not only helpful, but often the only way to proceed. Sometimes, however, you must do the jitterbug, and take many steps in a row. People can only do that if they have a clear sense of where they want to go, and the political courage and savvy to get there. Sometimes in crisis situations we can take many small steps, which are equal to one large step. In other cases the slogging gets slower. I have been in New Zealand in 1990, when the mood was bleak, in 1995, when it seemed almost euphoric, and in 1999, when it seems to be recovering but has not fully done so. I have thus seen the barometer in New Zealand set at various points, and the reality is that the climate for the uptake of good ideas is always changeable.