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Paradoxes in Worst-Case Thinking:
Three Essays in Constitutional Political Economy

A dissertation submitted in partial fulfillment of the requirements for the Degree of
Doctor of Philosophy at George Mason University.

By

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Bachelor of Science
University of London, 1996

Director: David M. Levy, Professor
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Fall Semester 2002
George Mason University
Fairfax, Virginia

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THREE ESSAYS IN CONSTITUTIONAL POLITICAL ECONOMY

by

Andrew Farrant
A Dissertation
Submitted to the
Graduate Faculty
of
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in Partial Fulfillment of
the Requirements for the Degree
of
Doctor of Philosophy
Economics

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ABSTRACT

PARADOXES IN WORST-CASE THINKING: THREE ESSAYS IN CONSTITUTIONAL POLITICAL ECONOMY

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George Mason University, 2002

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This dissertation subjects worst-case theorizing in constitutional political to critical scrutiny. Worst-case thinking is found wanting. Chapter 1 outlines the paradox of worst-case theorizing, suggesting that constitutional political economy is best-case theorizing in another guise. Chapter 2 explains why the supposition of public-spirited planners reigned supreme throughout the socialist calculation debate. Chapter 3 charges that F. A. Hayek's critique of socialist planning is largely a failure: Hayek's *Road to Serfdom* (1944) makes little sense as a critique of planning. Chapter 4 suggests that classical liberal political economy fails to escape the charge of best-case theorizing: classical liberal political economists subscribing to 'politics with romance' no less readily than did the advocates of socialist planning in the 1930's.

The Mill-Macaulay Debate:

Homo Economicus and the Paradox of Constitutional Enforcement

“I have been reading a very interesting book, a debate between James Mill and [T. B.] Macaulay ... [T]heir view of the institutional process is much different from what you find anywhere today. ... I am calling for a kind of return to the thinking of that period, in thinking about institutional rules” (James M. Buchanan 2001 [1979], 109).

“These little works [Essays on Government, Jurisprudence, Education, &c.], most of which are mere outlines to be filled up, though they have been both praised and animadverted upon as if they claimed the character of complete scientific theories, have been, I believe, more read than any other of Mr. Mill’s writings, and have contributed more than any publications of our time to generate a taste for systematic thinking on the subject of politics, and to discredit vague and sentimental declamation. The Essay on Government, in particular, has been almost a text-book to many of those who may be termed the Philosophic Radicals. This is not the place to criticise either the treatise itself or the criticisms of others upon it. Any critical estimate of it thoroughly deserving the name, it has not yet been my fortune to meet with; for Mr. Macaulay – assuming, I suppose, the divine prerogative of genius – only entered the contest, in order to carry away the argument he protected in a cloud of words” (J. S. Mill 1981 [1833], CW, I: 594).

“[O]ur whole construction is based on the belief, or faith, that constitutions can work, and that tax rules imposed within a constitution will prevail” (Brennan and Buchanan 2000 [1980], 15).

Introduction

Worst-case thinking about government has a long and distinguished history in political economy (Levy 2002; Toma and Toma 1984). The classic statement of worst-case thinking (perhaps the most illustrious example of worst-case modeling in the history of political economy) is that provided by David Hume: “Political writers have established it as a maxim, that, in contriving any system of government, and fixing the several checks and controuls of the constitution, every

man ought to be supposed a *knave*, and to have no other end, in all his actions, than private interest” (Hume, 1985 [1741], 42–43).¹ Despite their illustrious history, worst-case models of government were to strangely disappear from political economy in the early 1830’s, only, however, to then make a return to economics some 150 years later in the shape of the Leviathan model of government that Geoffrey M. Brennan and James M. Buchanan provided in the late 1970’s (see, e.g., 2000 [1980]). Indeed, Brennan and Buchanan overtly acknowledge that their Leviathan model of government marks something of a return to “the [worst-case] spirit of the classical political economists” (2000 [1980], 220).²

Why do I consider the 19th century debate over James Mill’s *Essay on Government* (1820) to have any relevance for James M. Buchanan’s worst-case philosophy of constitutional political economy? For one thing, Mill’s *Essay on Government* (1820) provides a model of government built on worst-case axioms rather similar to those favored by Brennan and Buchanan (1980). Mill modeling the government as a slave driver (Mill 1978 [1820], 67).³ Moreover, Buchanan has readily acknowledged having read the texts in the Mill-Macaulay debate (Buchanan 2001 [1979], 109). Despite having a distinguished pedigree in classical political economy (see, e.g., Hume 1985; Mandeville 1988; Mill 1978) worst-case models of government

¹ “The best of all then not being to be had, let us look out for the next best, and we shall find, that of all possible Means to secure and perpetuate to Nations their Establishment, and whatever they value, there is no better Method than with wise Laws to guard and entrench their Constitution, and contrive such Forms of Administration, that the Common-Weal can receive no great Detriment from the Want of Knowledge or Probity of Ministers, if any of them should prove less able or honest, than they could wish them” (Mandeville 1988, 335).

² “[A]s for our political-economist forebears, so for us: The *Homo economicus*-derived model of social conflict and cooperation seems uniquely appropriate for our constitutional speculations” (Brennan and Buchanan 2000 [1985], 75). See, also Buchanan (2001 [1987], 11).

³ Brennan and Buchanan (2000 [1980], vii) cite Montesquieu: “C’est une expérience éternelle que tout homme qui a du pouvoir est porté à en abuser; il va jusqu’à ce qu’il trouve des limites.” Mill (1978 [1820], 68) cites exactly the same passage. Moreover, Mill (1973 [10 Oct. 1815], 308) urges Ricardo to “make a good sermon upon this text of Montesquieu” prior to citing the same passage as that used by Brennan and Buchanan.

were to disappear from economics for some 150 plus years. Why did worst-case models of government wane in quite so dramatic a style after 1830 though? To answer that question, it is necessary that we pay attention to the issues at hand during the Mill-Macaulay dispute.

James Mill's worst-case model of government was the topic of rather heated – not to mention somewhat acrimonious – controversy in 1829.⁴ Writing in the *Edinburgh Review* (Macaulay 1829a), T. B. Macaulay argued that the type of worst-case theorizing epitomized by Mill's *Essay* was somewhat paradoxical. In particular, Macaulay suggested that the set of political institutions that found favor with James Mill (representative democracy) would surely prove equally vulnerable to the same type of 'worst-case' critique as that which Mill had scathingly leveled in the *Essay* regarding the workings of particular alternative sets of 'rules of the game' (e.g., non-democratic institutions for governance such as monarchy or aristocracy). Macaulay charged that worst-case thinking generated the following paradox: Mill advocated worst-case modeling on classic Humean-type grounds (see, e.g., Hume 1985, 42-43), arguing that to suppose the ubiquity of public-spirited agent-types – particularly taking umbrage at any suggestion that public-spiritedness was ubiquitous amongst political 'rulers' – was to posit far too unwarranted (or fragile) an assumption to seriously entertain when designing a set of rules of the game (institutions for governance) ex-ante. Mill's apparent rejection (at least prima facie) of anything akin to the maximax principle (see, e.g., Nozick 1974, 5, 298) was rooted in his worst-case theorizing. Macaulay suggested that despite appearing to reject the maximax principle, Mill's insistence on the optimality of representative institutions implicitly presupposed something

⁴ Writing to Napier (the editor of the Supplement to the *Encyclopedia Britannica*), Mill remarked, "You need be under no alarm about my article *Government*. I shall say nothing capable of alarming even a Whig" (Lively and Rees 1978, 4). "Mill was quite mistaken. His *Essay* alarmed almost everyone, Whigs, Tories, and those among his fellow Utilitarians who (like his son) regarded themselves as feminists" (Ball 1980, 92). See e.g., Thompson (1825), Smith (1827), and Mackintosh (1830). Ball (1992, xxiv) notes that Macaulay's review provided the reader with a "remarkable mixture of logical criticism, irony, mordant wit, and droll parody."

rather closely akin to the maximax principle (thereby suggesting that worst-case thinking was, in fact, somewhat irrelevant). Macaulay argued that in order for representative institutions to operate in the manner envisaged by Mill, it was necessary that public-spirited agent-types proved sufficiently prevalent amongst the voting populace and their political representatives – a prevalence which Mill’s worst-case axioms surely sought to deny – to ensure that democratic institutions would prove immune to the sub-optimal outcomes which Mill thought were intrinsic to any alternative governance structure (e.g., monarchy and aristocracy).

Historians of economics have largely ignored Mill’s worst-case thinking (e.g., Schumpeter 1994 [1954], 430). Indeed, Toma and Toma (1984) failed to include Mill’s slave driver model of government in their survey of the uses of worst-case modeling in classical political economy.⁵ Although this paper will attempt to somewhat redress the undue neglect with which those who write the history of economics have treated the Mill-Macaulay debate, my primary interest in the topic is not directed so much towards the Mill-Macaulay debate per se, than it is aimed towards whatever potential lessons a study of the debate might teach us. In particular, I am interested in any significance that the Mill-Macaulay debate might have for our understanding of the strengths – and far more importantly – any weaknesses, that may prove

⁵ Toma and Toma (1984, 93) note that the “Leviathan assumption appears to be at the heart of the classical conception of constitutional government.” They further note that the Brennan-Buchanan Leviathan model “seems to apply naturally to a monarchical form of government” (1984, 91). Bentham (1989 [1822], 205) argued that a pure monarchy would maximize tax revenues: “[T]he interest of the Monarch is essentially a sinister interest ... [T]he sinister interest when coupled with adequate power capable of giving effect to its tendency, the ultimate effect may be stiled the consummation of the sinister sacrifice. The consummation of the sinister sacrifice has place when by no addition made to the quantity of the matter of wealth endeavoured to be exacted for his own use from the other members of the community, further addition can actually be made: when taxation has arrived its *ne plus ultra*. In every pure Monarchy, taxation is at every point of time at its *ne plus ultra* with reference to that time.” Brennan and Buchanan (2000 [1980], 138) state, “the characteristic feature of our Leviathan model is that, in the absence of any constraints that force him to act differently, ... he will proved none of the public good, G, valued by citizens. He will simply maximize tax revenues, R, and he will utilize all of these for the funding of his own privately consumed goods and services.”

inherent to Brennan and Buchanan's (1985) own worst-case philosophy of constitutional political economy.

I suggest that we reconstruct Macaulay's critique of Mill's Essay (modern constitutional political economy proving guilty – or otherwise – by 'worst-case' association) as follows. Levy (2002, 131) suggests that the use of worst-case modeling is motivated by the "desire to avoid disaster" (see, e.g., Brennan and Buchanan 2000 [1985], 35, 62-63). Constitutional constraints are therefore thought to provide a type of 'insurance' against the welfare losses that a polity consisting of Humean type knaves would otherwise surely generate (e.g., the government in Brennan and Buchanan's Leviathan model engages in the maximal fiscal exploitation of the hapless populace).⁶ Naturally, such 'constitutional insurance' has a positive price: namely, the loss in efficiency (or social welfare) that is sustained when 'political' agent-type is of the public-spirited – rather than knavish – variety (Levy 2002, 132). The price we pay for such 'insurance' occurs when any constitutional constraints (e.g., a balanced-budget rule) serve to hamper the implementation of the welfare-enhancing discretionary policies that public-spirited agent-types would otherwise have sought to implement (see, e.g., Brennan and Buchanan 2000 [1985], 62). At this juncture, however, Macaulay's objections to worst-case thinking rear their head. Worst-case thinking appears to presuppose that constitutional constraints are somewhat akin to a type of non-contingent enforcement technology (see, e.g., Brennan and Buchanan 2000 [1980], 240). The rules of the game are, as such, wholly binding. Thus, agent-type appears to have little – if any – relevance to the 'robustness' (potency) properties attributable to the rules of the game (see, e.g., Buchanan's remarks regarding the "personal characteristics of those who happen to be selected as

⁶ Constitutional norms may "prove acceptable as embodying a minimax strategy aimed at securing protection against the worst-outcomes that might emerge" (Brennan and Buchanan 2000 [1985], xxiii).

governors” 2001, 47). Surely though, as Macaulay points out, constraints require enforcement.⁷ If knavish agent-types are pervasive in the political sphere, what grounds do we have for believing that the general populace (or the judges comprising a hypothetical constitutional court) are sufficiently public-spirited to put a stop to the political knavery? Does the constitutional political economist implicitly posit some type of motivational heterogeneity in their modeling? If so, why not simply argue in favor of the handing over of the ‘reins of power’ to the more public-spirited agent-types?⁸ In terms of the ‘constitutional insurance’ metaphor, we can say – following Macaulay – that the constraints are insufficiently potent to prevent disaster when called upon to actually do so (the ‘insurance’ fails to pay-off), and that when the rules are of sufficient strength to prove adequate to the task of preventing disaster there is very little chance that any such ‘worst-case’ disaster will actually rear its ugly head.

Levy (2002) translates “worst-case” thinking in political economy into the “lingua franca of robust statistics” (131). In doing so, Levy provides a useful taxonomy for classifying political institutions (or more accurately, models of political institutions/sets of rules of the game) according to their “robustness” properties. The following picture (taken from Levy 2002)

⁷ “There is ... one *crucial assumption* which clearly underlies the whole constitutional construction – that of *enforceability*” (Brennan and Buchanan 2000 [1980], 13, italics added).

⁸ This raises the problem of how to identify the relatively public-spirited agents ex-ante and how to design electoral rules that will select public-spirited candidates over knavish candidates. I shall not pursue this line of thought any further, however, instead referring the reader to the fascinating work of Brennan and Hamlin (2000). Richard Whately invoked worst-case considerations to devastating effect in the great debate over racial slavery (see Levy 2001). In particular, Whately invoked the principle of motivational homogeneity against those who argued that slavery was no evil where the slave-owner was public-spirited: “Are they [the citizens of the United States] prepared ... to substitute for their boasted republican institutions absolute monarchy? Yet it is plain that a perfectly wise and good monarch would devote himself to the welfare of his people, and would most effectually promote it. And if so *many hundred thousands* of their slave-owners are thus qualified (which they must be, to insure the good treatment of the slaves,) it would not be difficult for them to select *one* who should be thus qualified, and make him their autocrat” (Hill, Hinds, and Whately 1852, 245). Despite an admission that “if it were possible to secure a succession of perfectly wise and perfectly benevolent despots, I would surrender to them my liberty.” (37) Nassau Senior candidly states, “I could not believe in their performance” (Senior 1878, 37).

represents the performance of two institutions (or models of sets of rules of the game) as a function of the posited state of the world (or theory).

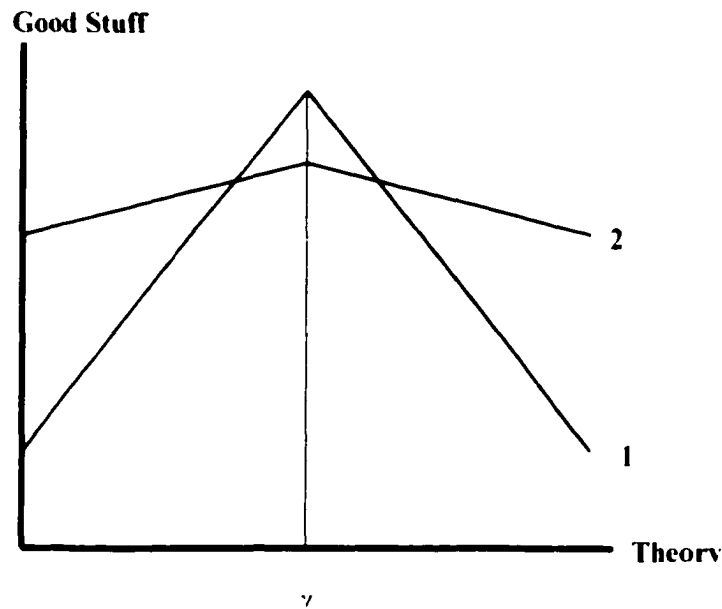


Figure 1: 2 is more robust than 1

When the state of the world (or supposition of the model) is γ , institution 1 generates a greater amount of the metric "good stuff" (Levy's terminology) than does 2. If γ holds, then 1 outperforms 2 (in terms of the desired metric). To illustrate the point, let γ represent public-spirited socialist planners and let 1 represent market socialism (see, e.g., Lange 1964 [1938]; Lerner 1944). Socialist planning (1) is superior to markets (2) given a posited lack of self-interest on the part of the planners. Now weaken the supposition of public-spiritedness (γ), allowing the planners to be no less motivated by self-interest than are the rest of us. Deadweight losses are

now pervasive (Levy 1990). Institution 2 outperforms institution 1 when γ does not hold. Socialist planners readily exploit the fact that socialist planning transforms the entire economy into one giant de facto monopoly.⁹ Models of market socialism are decidedly non-robust (or fragile) when planners are akin to Humean knaves. Robust institutions (2) limit the loss of "good stuff" that results from the failure of γ . The literature on institutional robustness is inextricably intertwined with the minimax approach to decision making.¹⁰ Maximax considerations, however, would lead us to favor 1 over 2.¹¹ Any consideration of the possible failure of γ would not impact on our choice. Minimax considerations, by contrast, would lead us to take rather seriously the possibility of γ failing.

Macaulay essentially charges that Mill implicitly switches from reasoning in terms of the minimax principle (when discussing monarchy or aristocracy) to reasoning in terms of the maximax principle (when arguing in favor of representative institutions). If you like, Mill – in terms of figure 1 – readily limits the best-case supposition of γ to only one point for monarchy (institution 1). At the same time, however, Mill draws 2 all the while implicitly presupposing that γ (or some very close approximation to γ) holds true for all points.

⁹ Market socialism is fragile if the supposition of public-spirited planners fails (Knight 1982 [1940], Levy 1990, Shleifer and Vishny 1992). See Stiglitz (1994, 106-107): "we can ask, is the model robust? Do slight changes in the assumptions – particularly the assumptions about which we may have limited confidence – result in marked changes in the conclusions?" Frank Knight – in common with the modern public choice literature on socialist planning – had very limited confidence in the assumption that socialist planners were public-spirited (see, e.g., Knight 1982 [1940]).

¹⁰ Levy (2002) makes the link between Brennan and Buchanan's (1983, 2000) worst-case philosophy of constitutional political economy and J.W. Tukey's worst-case philosophy of mathematical statistics. Moreover, Levy (2002, 131) notes, "von Neumann's minimax loss approach to decision making is absolutely central to robust [worst-case] thinking". See, e.g., Brennan and Buchanan (2000 [1980], xxiii, 220, 240).

¹¹ The "maximax" criteria ... would proceed on the most optimistic assumptions about how things would work out – Godwin, if you like that sort of thing" (Nozick 1974, 5).

David Hume's worst-case model of political knavery (1741) provides the fundamental intuition for the institutional robustness literature.¹² Indeed, Hume's own worst-case model provides the impetus for modern constitutional political economy (Brennan and Buchanan 2000 [1980], 42; 2000 [1985], 68) and Mill's slave driver model of government (Mill 1978 [1820], 1992 [1835], 306-307): Mill avowing his own worst-case model to be in exactly the same Humean 'worst-case' tradition as that to which Brennan and Buchanan readily subscribe.

The Mill-Macaulay Debate.

Donald Winch (1983) suggests that the Mill-Macaulay debate provided a rather "suitable climax" (93) to the early 19th century dispute between the Philosophic Whigs and their Philosophic Radical opponents (see, e.g., Thomas 1979; Winch 1983). James Mill had launched a Benthamite jihad against the *Edinburgh Review* (quarterly periodical of the Philosophic Whigs) from the very first issue of the *Westminster Review* (quarterly periodical of the Philosophic Radicals) in 1824, filling the pages of the *Westminster* with a torrent of heated invective aimed towards the "lackeys of the aristocracy" at the *Edinburgh Review* and their Whig fellow travelers and supporters in the country at large (see, e.g., Bain 1882).¹³ The *Edinburgh Review* hit back at the philosophic radicals in 1829, publishing T. B. Macaulay's devastating review of Mill's *Essay*

¹² Worst-case thinking focuses our attention on the potential costs of 'institutional' failure (Brennan and Buchanan 1983). Best-case thinking, by contrast, ignores any such worst-case considerations. "The talk of designing institutions so that bad men at their head can do little harm, and of checks and balances, can be interpreted as prompted by a minimax principle, or, more accurately, by minimax considerations built into a less stringent principle. ... Everyone who has considered the matter agrees that the maximax principle ... is an insufficiently prudent principle which one would be silly to use in designing institutions. Any society whose institutions are infused by such wild optimism [best-case thinking] is headed for a fall" (Nozick 1974, 298).

¹³ "So formidable an attack on the Whig party and policy had never before been made; nor had so great a blow been ever struck, in this country for radicalism: nor was there, I believe, any living person capable of writing that article, except my father" (J. S. Mill 1989 [1873], 86). Also see Lively and Rees (1978, 4-5).

on Government (1820). Macaulay struck a mighty powerful blow against the Utilitarian cause, wreaking havoc with Mill's worst-case logic, and charging Mill with having failed to take his own worst-case axioms seriously.^{14, 15}

J. S. Mill claimed in his posthumously published *Autobiography* (1989 [1873]) that his father's *Essay on Government* (Mill 1820) was intended as little more than polemic written to further the cause of parliamentary reform.¹⁶ The evidence, however, suggests otherwise, and that in actuality James Mill thought the *Essay* as far more than mere polemic. Indeed, in the *Fragment on Mackintosh* (1992 [1835], 304-314) Mill treated the *Essay* as more akin to a scientific treatise on politics than polemic, viewing the *Essay* as having provided a more detailed and generalized treatment of the logic that was implicit in Hume's own worst-case model:

Political writers have established it as a maxim, that, in contriving any system of government, and fixing the several checks and controuls of the constitution, every man ought to be supposed a *knave*, and to have no other end, in all his actions, than private interest. By this interest we must govern him, and, by means of it, make him, notwithstanding his insatiable avarice and ambition, co-operate to public good. Without this, say they, we shall in vain boast of the advantages of any constitution, and shall find, in the end, that we have no security for our liberties and possessions, except the good-will of our rulers; that is, we shall have no security at all (Hume, 1985 [1741], 42-43).

¹⁴ "We think that the theory of Mr. Mill rests altogether on false principles, and that even on those false principles he does not reason logically" (Macaulay 1978 [1829a], 99). William Wilberforce, wrote to Macaulay's relative, Mr. Babington, stating, "I am much pleased with a review of Tom Macaulay's in the *Edinburgh*; it is not merely the superior talent which it indicates, but its being on the right side. The *Westminster Review*, of which Mill is a principal support, is a very mischievous publication; and this review will be a death-blow to Mill as a reasoner" (Bain 1882, 227). On the strength of Macaulay's review (1829) of Mill's *Essay*, Lord Lansdowne offered Macaulay a seat in the House of Commons.

¹⁵ Thomas states that with Macaulay's final reply (October 1829) to the *Westminster Review*: "The rout of the utilitarians was complete" (Thomas 1979, 140).

¹⁶ "I was not at all satisfied with the mode in which my father met the criticisms of Macaulay. He did not as I thought he ought to have done, justify himself by saying, "I was not writing a scientific treatise on politics. I was writing an argument for parliamentary reform". He treated Macaulay's argument as simply irrational; an attack upon the reasoning faculty; an example of the saying of Hobbes, that when reason is against a man, a man will be against reason" (Mill 1989 [1873], 128).

Mill suggested that Hume's worst-case logic served to illustrate the "very same application of the same general law, for which carried out into detail, Mr. Mill is accused [by Sir James Mackintosh] as shewing his ignorance of the most notorious facts in human nature" (Mill 1992 [1835], 306).¹⁷ Mill never wrote a rejoinder to Macaulay's review of the *Essay on Government*, viewing the target of the Fragment – the Whig lawyer Sir James Mackintosh¹⁸ – as providing an adequate surrogate for Macaulay.¹⁹

The Mill-Ricardo Correspondence: Worst-case Modeling and the Rules of the Game

In common with modern constitutional political economy, James Mill appears to readily accept – at least prima facie – David Hume's suggestion that all "plans of government which suppose great reformation in the manners of mankind, are plainly imaginary. Of this nature, are

¹⁷ Bentham explains Hume's maxim thus: "[I]n public life ... that error which asserts the existence of the predominance of social regard in the breast of any public man in any such degree as shall engage him willingly to give up, for the sake of any quantity of happiness in all other breasts put together, any the smallest particle of his own happiness is in its practical consequences by far the most pernicious, productive of evil in the greatest quantity. In the framing of laws, suspicion can not possibly be carried to too high a pitch. No man ought to be presumed actually guilty to the purpose of judicial punishment: every man ought to be presumed disposed to be guilty, and endeavouring to be guilty to the purpose of legislative enactment: every man, and most of all he who, having it most in his power to be guilty, and most assured of being guilty with impunity, has the strongest propensity to be guilty, and at the same time is most vehement in his assurance that in his breast no such propensity has place" (Bentham 1989 [1822], 15-16).

¹⁸ Mackintosh's *Dissertation on Ethical Philosophy* (1830) had attacked Mill's *Essay* (see Ball 1992). "Mackintosh's mode and manner of argument was borrowed, as the author acknowledged, from "the writer of a late criticism on Mr. Mill's *Essay*. – See *Edinburgh Review*, No. 97, March 1829"" (Ball 1992, xxv). Earlier, Mackintosh had scathingly reviewed Bentham's *Plan of Parliamentary Reform* (1817) in the *Edinburgh Review* (1819). See Lively and Rees (1978, 4-5).

¹⁹ "[T]he answer which does for Sir James, will answer the same purpose with the *Edinburgh Review*" (Mill 1992 [1835], 305). Francis Place wrote in his diary: "The articles in the *Edinburgh Review* were written by young Mr. Maccauley [sic] for a purpose. I was with Mr. Mill at Dorking when the last were published. Mr. Bickersteth was there also. He and I were of [the] opinion that they were equally unfair and foolish, and not such as Mr. Mill should reply to" (Fenn 1987, 122). Ball (1992, xxv.) states that Mill, "thoroughly dissatisfied with the *Westminster Review*'s replies, ... [tried] without success, to persuade his friend and fellow Benthamite Etienne Dumont to reply to the *curly-headed coxcomb* [Macaulay], *who only abuses what he does not understand*." (Mill's own words italicized).

the *Republic* of PLATO, and the *Utopia* of Sir Thomas More” (Hume 1985, 514).²⁰ Indeed, in extensive correspondence Mill had repeatedly tried to convince David Ricardo that worst-case models of government were of value, arguing that even if one were to accept any supposed fixity of agent-type – thereby ruling out any possibility for positive change in the “manners of mankind” – suitably changing the constitutional rules of the game would still suffice to preclude the sub-optimality that Mill (1973 [10 Oct. 1815], 308) readily characterized as “bad government”:

[Were] any other men, with the same bad education, [to be given] the same powers to prey upon their country; the same motives to betray the principles of good government: - money and praise, for upholding bad government: ... they will act in the same way as the members of the noble and honorable houses. *It is the constitution* [the rules of the game], *therefore, of the honorable houses, that does the mischief*, by placing men’s interest and their duties not in accord (Mill 10 Oct. 1815, 308).

Thus, Mill promised Ricardo a plan, one that would clearly demonstrate how “the evil [of bad government] would be effectually and easily remedied, without any change in any man’s circumstances [agent-type],” the suggested remedy (representative institutions) merely necessitating the “shutting up for the future [of] the channels of unjust gain” (Mill 10 Oct. 1815,

²⁰ In the Fragment on Mackintosh (1992 [1835], 304-314), however, Mill praised Plato’s *Republic* effusively: “The whole of Plato’s *Republic* may be regarded as a development, and in many of its parts, a masterly development, of the principle applied by Mr. Mill: that identity of interests between the governors and the governed affords the only security for good government” (309). “Without identity of interest with those they rule, the rulers, Plato says, instead of being the guardians of the flock, become wolves and its devourers” (310). “Plato, seeing thus clearly the necessity of identifying the interests of the guardians with the interests of the guarded, bent the whole force of his penetrating mind, to discover the means of effecting such identification: but being ignorant, as all the ancients were, of the divine principle of representation, found himself obliged to have recourse to extraordinary methods. He first of all prescribes a very artificial system of education for the class of guardians: a system of such vigilance, begun so early, and continued so long, as to make of them a *very different sort of beings from the ordinary race of mortals, to make of them, in short, philosophers*. Plato laying it down as a universal truth, that there can be no happiness for states, until either philosophers are the rulers, or the rulers philosophers” (311, italics added). This surely belies Mill’s apparent *prima facie* insistence that the rules of the game adequately substitute for agent-type on all relevant margins (see, e.g., Mill 1973 [10 Oct. 1815], 308, 1978 [1820], 73). Bentham is highly skeptical towards any such claims of motivational heterogeneity: “To say – they [constitutional constraints] ought not to apply to me, is as much as to say – *I am not of the human species*: or at least with the Pharisee, *I am not as other men are*” (Bentham 1984 [1830], 120). “Is it the *ruling one* that is in question? His estimate of himself, as expressed in his own language, is – *I am not as other men are: they are of the species between God and man*” (121).

308).²¹ Upon reading a draft of Mill's *Essay on Government* prior to its publication in the *Encyclopedia Britannica* (1820), Ricardo wrote to Mill on July 27th 1820 with enthusiasm: "I have read with great pleasure the article on Government which you have written for the next volume of the Encyclopedia [Britannica] – I think it excellent, and well calculated to serve the good cause. It is written in the true philosophic temper – the best reasons are given for the propositions advanced, and they are made clear and convincing" (Ricardo 1973 [27 July 1820], 210).

Mill's Worst-case axioms: Government as Slave Driver

In the *Essay on Government* (1820), James Mill provided a principal-agent model of government (55-59).²² Men created government to provide them with the public good of civil peace: a good, which Mill thought otherwise wholly unattainable.²³ Mill viewed the establishment

²¹ Mill's worst-case axioms were evident in a letter to Ricardo dated October 10th 1815: "[This] rapacity of the members of the two houses – their insatiable, unprincipled desire to live at the expense of the public, to plunder the people for money which they may spend," is no more than the "steady operation of the laws of human nature" (Mill 1973 [10 Oct. 1815], 307-308). Hollander (1979, 1985) provides an illuminating discussion of David Ricardo's rejection of James Mill's worst-case methodology.

²² David Hume's property theory (1741) provides the foundation for Mill's *Essay*: "[I]f nature had produced spontaneously all the objects which we desire, and in sufficient abundance for the desires of all, there would have been no source of dispute or of injury among men: ... The results are exceedingly different, when nature produces the objects of desire not in sufficient abundance for all. The source of dispute is then exhaustless" (Mill 1978 [1820], 56). "[I]t is obvious that every man, who has not all the objects of his desire, has inducement to take them from any other man who is weaker than himself" (Mill 1978 [1820], 57). On Hume's property theory, see Levy (1992, 23-25, 95-101). Anarchic 'rules of the game' are fragile in the face of opportunistic behavior, which, although proving disastrous from the standpoint of collective rationality, proves a somewhat rational strategy from the viewpoint of the individual (see, e.g., Buchanan 2001, 91-96).

²³ "It is obviously impossible that the community in a body can be present to afford protection to all of its members. It must employ individuals for that purpose. Employing individuals, it must choose them: it must lay down the rules under which they are to act: and it must punish them if they act in disconformity to those rules. ... The management of the joint affairs [Administration, Legislation, and Judicature] of any considerable body of the people they never undertake for themselves. ... Even in the case of a common Benefit Club, the members choose a Committee of Management and content themselves with a general control" (Mill 1978 [1820], 59). Mill's agency model of government ought to be considered an important precursor of the katalactic tradition in public finance (e.g., Whately 1832; Buchanan and

of government as somewhat analogous to the creation of a "common Benefit Club" (59), one where the citizenry traded tax payments for protection (see, e.g., Papenfuss 1998; Whately 1832).²⁴ Despite viewing the initial creation of government (the solution to a large numbers prisoners' dilemma game) as largely unproblematic, Mill recognized that a secondary prisoners' dilemma type game²⁵ arose from the remedy that government provided to the sub-optimality of anarchic equilibrium (Mill 1978 [1820], 57; Bush 1972; Tullock 1972).²⁶ Though the populace had initially created government in order to temper the worst-case equilibrium necessarily generated by the "law of human nature, that a man, if able will take from others anything which they have and he desires" (Mill 1978 [1820], 61). Mill's avowed worst-case supposition of motivational homogeneity²⁷ necessarily implies that government proves equally susceptible to the perennial lure of the off-diagonal pay-off. Thus, the citizenry have a somewhat urgent need to provide an adequate remedy for the situational logic inherent to this secondary prisoners'

Tullock 1962; Buchanan 1975; Papenfuss 1998). Katalactic – or exchange – theories of government view the successful creation of government as no different than the realization of any other potential gains from trade.

²⁴ "[A] great number of men combine ... and delegate to a small number the power necessary for protecting them all. This is government" (Mill 1978 [1820], 57).

²⁵ The "Edgeworth Box" of society is predicated upon a structure of rules and mores. The lure of gain is ever-present. The relevant question is as to what form such gain will take? Trade can be modeled as a simple prisoners' dilemma game. The possibility of mutual gain coexists alongside the ubiquitous temptation of differential advantage (see, e.g., Levy 1992, 17-24). The constitutional contract might prove subject to similar time consistency problems.

²⁶ Constitutional political economy appears to be plagued by a variety of paradoxes. For example, if we assume that individuals are capable of solving collective action problems such as that which involves creating a government (or Hobbesian sovereign), surely analytical symmetry would suggest that the individuals are surely equally capable of enforcing any bargains made in a state of nature (anarchic equilibrium). Constitutional economics appears to fall foul of the Hobbes paradox. The very possibility of creating a Sovereign (Hobbes) appears to necessitate the absence of any requirement for the services of the Sovereign. See, e.g., Boettke (1993, 183).

²⁷ "That dissection of human nature which would be necessary for exhibiting ... the primary elements into which human happiness may be resolved, it is not compatible with the present design to undertake. We must content ourselves with assuming certain results" (Mill 1978 [1820], 55).

dilemma type problem (the game now played by citizenry and government rather than by the citizenry alone), thereby inducing the government's adherence to the terms of the original 'constitutional contract' (see, e.g., Buchanan 1975).

Though the creation of government potentially facilitates a Pareto improvement on the sub-optimality of anarchic equilibrium (Bush 1972; Tullock 1972), Mill's task in the *Essay* had but begun, since (just as for Buchanan and Tullock): "All the difficult questions of Government relate to the means of restraining those, in whose hands are lodged the powers necessary for the protection of all, from making bad use of it" (Mill 1978, 58). Though providing a katalactic model of the origins of government (recognizing the potential welfare gains generated by 'political' trade), Mill followed Hume's worst-case maxim to the letter (Hume 1985, 42-43): prudence dictating that government, while utterly indispensable to the preservation of anything closely akin to civil society, thus be modeled a knave writ large:

Whatever would be the temptations under which individuals would lie, if there was no Government, to take the objects of desire from others weaker than themselves, under the same temptations the members of Government lie, to take the objects of desire from the members of the community, if they are not prevented from doing so. Whatever, then, are the reasons for establishing Government, the very same exactly are the reasons for establishing securities, that those entrusted with the powers necessary for protecting others make use of them for that purpose solely, and not for the purpose of taking from the members of the community the objects of desire (Mill 1978 [1820], 58).²⁸ ²⁹

Mill summarizes the political agency relationship thus: "All the difficult questions of Government relate to the means of restraining those, in whose hands are lodged the powers necessary for the

²⁸ Government is founded on the "law of nature" that a "man, if able, will take from others anything which they have that he desires" (61). To suppose that a Monarch would refrain from such spoliation would be to "affirm that Government is unnecessary; and that human beings will abstain from injuring one another of their own accord" (Mill 1978 [1820], 61).

²⁹ "The bad measures or bad appointments of a minister may be checked by Parliament ... but *quis custodiet custodes?* who shall check the Parliament?" (J. S. Mill 1998 [1861], 274).

protection of all, from making bad use of it" (Mill 1978 [1820], 58).³⁰ Mill thought it axiomatic that government would seek to "make use of [political power] ... to defeat the very end for which government exists" (61).

Eliminating the off-diagonal: Inducing Moral Aptitude or Transforming Agent-Type?

Mill argued that the situational logic inherent to the agency relationship between citizen and government provided adequate reason for 'constitutional' meta-rules of the game (or constraints). Mill suggested that such meta-rules would provide "securities" (58) precluding the possibility of government predation against the citizenry (e.g., fiscal exploitation). Mill argued that such rules would eliminate the perennial lure of the off-diagonal, inducing 'moral aptitude'³¹ on the part of public functionaries. Modeling government as *homo economicus* writ large (Mill 1978, 66), Mill repeatedly argued that the very principles of human nature (agent-type was that of *homo economicus*) that made government necessary surely implied that without adequate constraints against fiscal exploitation (or any other form of predation by government), the government was sure to engage in a "degree of plunder" such as would reduce the great mass of men to the "bare means of subsistence" (67). This unhappy situation, we shall designate as the

³⁰ "[T]he people ... must entrust [the powers of Government] to some one individual or set of individuals, and such individuals will infallibly have the strongest motives to make a bad use of them" (Mill 1978 [1820], 72).

³¹ Bentham writes, that "moral aptitude is a negative quality: it is constituted by the absence, in so far as possible, of a certain propensity universal in human nature ... the propensity to sacrifice all other interests to ... his own preponderant interest" (1989 [1822], 13). What does Bentham mean by "moral aptitude"? Although it may appear that Bentham envisages the transformation of agent-type (13), I suggest that "moral aptitude" is better understood as referring to an incentive-compatible set of rules of the game (with agent-type a given): "By moral aptitude is therefore here meant but practical innoxiousness; and such innoxiousness not having any other cause than impotence, in the station of each functionary to establish this impotence, leaving to him at the same time the necessary power – to render him unable to do wrong, yet sufficiently able to do right, is the great difficulty, and ought to be the constant object and endeavour of whatsoever labour is employed in the field of legislation" (15).

slave-driver equilibrium (67).³² Mill referred any reader who might prove skeptical regarding the validity of such worst-case thinking to the data:

The world affords some decisive experiments upon human nature, in exact conformity with these [worst-case] conclusions. An English gentleman may be taken as a favourable specimen of civilization, of knowledge, of humanity, of all the qualities, in short, that make human nature estimable ... Wherever the same [worst-case] motives exist, the same conduct as that displayed by the English Gentleman may be expected to follow ... [N]ot one item in the motives that led English Gentlemen to make slaves of their fellow-creatures, and to reduce them to the very worst condition in which the Negroes have been found in the West Indies, can be shown to be wanting, or to be less strong in the set of motives, which universally operate upon the men who have power over their fellow creatures (Mill 1978 [1820], 67).

Thus, Mill thought his worst-case conclusions indisputable: “[It is proven], therefore, by the closest deduction from the acknowledged laws of human nature, and by direct and decisive experiments, that the ruling One [monarchy], or the ruling Few [aristocracy], would, if checks did not operate in the way of prevention, reduce the great mass of the people subject to their power ... to the condition of Negroes in the West Indies” (68).³³

In keeping with the general ‘rational-choice’ tenor characteristic of ‘philosophic radical’ political economy (see, e.g., Mill 1992, 212-219), Mill sought to provide a rational-choice type mechanism – a system of “checks and controuls” (Hume 1985) or meta-rules of the game – that would operate so as to induce “moral aptitude” on the part of public functionaries (government), thus averting the degree of “plunder” (or fiscal exploitation) otherwise characteristic of the slave-driver equilibrium. Mill reiterated the importance of the *Essay*’s supposition of motivational

³² The suggestion that one model government as a slave driver was not unique to James Mill: “[T]ake the case of *Negro* slavery ... The Slave-holder – it may be said – for it is continually said – has an interest in common with that of his slaves. True: and so has the Mail-Coach Contractor in common with that of his horses. While working them, and so long as they appear able to work, he accordingly allows them food. Yet, somehow or other, notwithstanding this community of interest, so it is that but too often Negro as well as horse are worked to death. – How happens this? – How? – but because in the same breast with the conjunct interest is lodged a separate and sinister interest, which is too strong for it. Even so is it in the case C _____ r-General and Co., under whose management, the condition of the poor people is day by day approaching nearer and nearer to the condition of the Negro and the horse” (1817, xxvi-xxvii).

³³ “Every Monarch is a Slave-holder upon the largest scale” (Bentham 1989 [1822], 171).

homogeneity³⁴ throughout the *Essay on Government*, repeatedly stipulating the importance of holding fast to the *Essay*'s worst-case suppositions regarding agent-type (see, e.g., 60-61).³⁵ The particular rational-choice mechanism (or set of "checks and controls") that found favor with Mill was that of representative democracy (75). Mill suggested the "system of representation" (74) would operate to temper the possibility of malfeasance otherwise inherent to any relationship of political agency (74-75), serving to (potentially) short-circuit the operation of the situational logic that induced public functionaries to 'defect': leading them to select co-operative over non co-operative strategies. Mill was equally insistent, however, that representatives, once granted political power, would – just "like any other men" (75) – and in accordance with the worst-case suppositions of the *Essay on Government* seek to use "their power, not for the advantage of the community, but for their own advantage ... [H]ow can they be prevented?" (75). How indeed? Mill's worst-case logic clearly places him in the company of modern constitutional economists (e.g., Brennan and Buchanan 2000 [1985]; Tullock 1987).

Mill was quite adamant that for the "system of representation" (71) to provide adequate "security" against the realization of the slave-driver equilibrium, it was vitally important that an identity of interests³⁶ characterize at all times the relationship between the representative body and the general populace. Failing any such conjunction of interests, however, and Mill – once again in accordance with the *Essay*'s worst-case axioms – was adamant that the representative body would prove the great engine of fiscal exploitation, seeking to extract maximal surplus from the hapless populace. Thus, Mill argued that the "grand difficulty," was one of constituting "a

³⁴ See Brennan and Buchanan (2000 [1985]).

³⁵ The assumption of motivational homogeneity got Mill into much trouble with T. B. Macaulay (1829).

³⁶ J. S. Mill (1998 [1861]) thought the doctrine of an "identity of interests" just "sound without meaning".

checking body, the powers of which shall not be turned against the community for whose protection it is created" (75).³⁷

Readily accepting the proposition that "upon the right constitution of checks, all goodness of Government depends." (73) Mill argued that regular electoral sorting (representative democracy) would facilitate the screening and sorting of candidates for political office. The "system of representation" (71) would operate to continuously subject all potential Humean knaves who were drawn into the candidate pool to the scrutiny of the electorate, thus tempering their otherwise knavish proclivities. Mill suggested that electoral sorting would create adequate incentive for any political knave (whether actual or potential) to act as if they were somewhat rather more akin to a political angel (Madison) than to a political knave: the electoral constraints sufficing to induce the requisite degree of "moral aptitude" (Bentham 1989 [1822], 13) on the part of any public functionary. Thus, (at least *prima facie*) performance in office appears somewhat invariant to agent-type.³⁸ It is clear, however, that the length of a representative's time-horizon and the height of their discount rate are vitally important to the workability of Mill's electoral scheme (Levy 1992).³⁹

Although modeling government as akin (at least potentially) to a slave driver (67), Mill thought that representative institutions were adequate to constrain the ever-present proclivity for

³⁷ Tullock (1993, 16) has charged that constitutional political economy fails to take this problem seriously, suggesting that constitutional political economists readily abandon their worst-case methodology when addressing this question.

³⁸ Intriguingly, constitutional political economy places emphasis on "setting up rules or constraints within which politicians must operate, rules that will make it a *relatively trivial matter as to the personal characteristics of those who happen to be selected as governors*" (Buchanan 2001 [1981], 47, italics added).

³⁹ "The smaller the period of time during which any man retains his capacity of Representative, as compared with the time in which he is simply a member of the community, the more difficult it will be to compensate the sacrifice of the interests of the longer period, by the profits of mis-government during the shorter" (Mill 1978 [1820], 75).

government to engage in fiscal exploitation, voters observing a signal of performance (agent-type in office) and casting their vote accordingly: representatives who were angels (or who had not as yet revealed their knavish agent-type) were returned to office, while those who had revealed themselves as knaves fell at the electoral hurdle. Regular electoral sorting thereby facilitates the removal of knaves from political office: those representatives who are genuine angels (*non-homo economicus*) or have yet to reveal their knavish agent-type enjoying electoral success (Mill 1978 [1820], 77).⁴⁰

While ‘philosophic radical’ constitutional political economy placed immense importance on the role that electoral constraints played in tempering the ever-present potential for political agents to abuse their hold on the ‘reins of power’,⁴¹ the problem of mitigating malfeasance during a representative’s final-period in office still remained; presumably, however, Bentham’s *Auto-leon* plan (1832) was originally envisaged as a suitable means to somewhat reduce the net gains resulting from such malfeasance (Levy 1992, 2001). Mill recognized, however, that continuous electoral review was somewhat sub-optimal (see Barro 1973), arguing that frequent elections were costly. Moreover, Mill recognizes that if the power of “Government” were to continually shift “from one set of hands to another every day, the business of [government] could not proceed” (76). We note that Mill ignored the welfare costs that legislative durability might

⁴⁰ Mill assumes that the voter observes a non-noisy signal of agent-type. The various essays (e.g., *Liberty of the Press*) collected in Mill’s “*Political Writings*” (Ball 1992) are invaluable in helping to clarify the informational assumptions that Mill implicitly made in the *Essay on Government* (1820).

⁴¹ “[T]he only practicable way of preserving a check over those appointed to the directorship of the great Company, is to send them back to their constituents frequently; and the more frequent the reference, the more perfect the check” (T. Perronet Thompson 1978 [1829], 145). “They [the principal] do not appoint an agent, with liberty to do as he pleases, and without reserving the power of instantaneous dismissal. If they did, they would expect that the obligations of his trust would be disregarded, when in competition either with the interest of his pocket or with that of his ease” (J. S. Mill CW: XVIII, 19).

occasion (Landes and Posner 1975).⁴² We shall now consider Macaulay's attack on worst-case thinking.

Utilitarian Logic and Politics: Macaulay's attack on Mill's Essay

T. B. Macaulay's highly acerbic review – *Mill's Essay on Government: Utilitarian Logic and Politics* (Macaulay 1978 [1829a], 99-129) – appeared in the March 1829 edition of the *Edinburgh Review*.⁴³ Though thinking that Mill's slave driver model of government lacked empirical relevance,⁴⁴ Macaulay steadfastly held Mill to the worst-case implications of the *Essay's* logic. Macaulay was insistent that if one took Mill's worst-case thinking truly seriously, the various objections that Mill had raised against monarchy and aristocracy would surely prove equally applicable to democratic institutions. Indeed, Macaulay charged that Mill's worst-case logic implied that the security representative institutions provided against bad government would rather prove “no security at all” (1978 [1829a], 114): Mill's worst-case axioms surely implying

⁴² T. Perronet Thompson did recognize the potential for such welfare losses, arguing that any potential rent-seeker would “recommend the extension for the period of service; in order that it might be better worthwhile for the candidates to bribe” (1978 [1829], 146). The greater the perceived durability of any envisaged rents, the greater the amount of expected rent-seeking expenditures (Fullock 1967). Bentham's *Plan of Parliamentary Reform* (1817) provided an insightful discussion of the costs and benefits accompanying legislative durability. Referring to the monetary value of rents as “venal value”, Bentham thought annual elections as beneficial to the extent that lower rent-seeking waste would result: “In proportion to the short-livedness of the power [legislative durability], diminishes, both to purchaser and thence to sellers, the venal value of it” (Bentham 1817, ccliv). Annual parliaments would serve to make legislation less favorable to sinister-interests (Bentham) less profitable to supply. Annual parliaments would reduce the perceived value of such legislation, thereby facilitating the attainment of a political equilibrium characterized by less rent-seeking expenditure.

⁴³ “[T]he assault on the *Essay on Government* and its admirers was overwhelming. Macaulay's attack on James Mill is one of those controversial pieces of writing, like Gibbon's *Vindication* or Newman's *Apologia*, in which the arguments are so well turned, and the demonstration so conclusive, that they have proved more enduring than the work which provoked them. Mill is, as it were, preserved in effigy in Macaulay's pages” (Thomas 1979, 136).

⁴⁴ “During the last two centuries, some hundreds of absolute princes have reigned in Europe. Is it true that their ... rapacity has left no more than the bare means of subsistence to any of their subjects, their ministers and soldiers excepted? Is this true of all of them? Of one half of them? Of one tenth part of them? Or a single one? (Macaulay 1978 [1829a], 104).

that the poor – given the opportunity – would no less readily plunder their fellow men than would a tyrannical monarch.⁴⁵

Moreover, Macaulay suggested that Mill's worst-case assumptions regarding agent-type had the implication that ex-post time consistency problems were sure to plague the ex-ante pledges made by those elected to office:

[T]he representatives, as soon as they are selected [by the voters], are an aristocracy, with an interest opposed to the interests of the community? Why should they not pass a law for extending the term of their power from one year to ten years, or declare themselves senators for life? (Macaulay 1978 [1829a], 114).

Although the advocate for representative institutions might have attempted to rebut Macaulay's charge by ruling out any possibility of change in the "fundamental [constitutional] laws ... without the consent of a convention, specially elected for the purpose," Macaulay was wholly unyielding: "still the difficulty recurs: Why may not the members of a convention betray the trust, as well as the members of the ordinary legislature?" (114). Macaulay suggested that Mill's worst-case logic (in conjunction with the *Essay*'s assumption of motivational homogeneity) inexorably led one to the following worst-case conclusion:

When private men, they [the members of the imagined constitutional convention] may have been zealous for the interests of the community. When candidates, they may have pledged themselves to the cause of the constitution. But as soon as they are a convention, as soon as they are separated from the people, as soon as the supreme power is put into their hands, commences that interest, opposite to the interests of the community, which must according to Mr. Mill, produce measures opposite to the interests of the community (Macaulay 1978 [1829a], 114-115).

Macaulay's charge that worst-case thinking implies the possibility that time consistency problems (Kyddland and Prescott 1977; McCallum 1995) would plague the move from higher-level constitutional politics to lower-level in-period politics (Buchanan 1987) may well prove

⁴⁵ "If the 'foundation of government' was the tendency of each man to make others 'subservient to his pleasures', then the enfranchised majority could be expected, on Mill's own principles, to plunder the rich minority" (Thomas 1979, 137).

applicable to modern constitutional political economy.⁴⁶ Despite having initially raised the possibility of time inconsistent choice at the constitutional level, Macaulay, however, rejected the likelihood of such an occurrence: “[T]here is no danger in such a case [that of the constitutional convention]. But there is no danger, only because there is no truth in Mr. Mill’s [worst-case] principles” (115). Macaulay suggested that legislators were dissuaded from engaging in constitutional-malfeasance by the fear of inflaming negative public opinion: “[L]egislators will be deterred by the fear of resistance and of infamy, from acting in the manner which we have described” (Macaulay 1978 [1829a], 115).

Approbational Incentives and the Slave-Driver Equilibrium

Macaulay repeatedly castigated Mill for unduly neglecting the important role that approbational incentives (public opinion) played in helping to mitigate the worst-case propensity for the misuse of government power (e.g., fiscal exploitation). Macaulay, stringently objecting to the worst-case specification of Mill’s model, suggested that “Mr. Mill has chosen to look only at one-half of human nature, and to reason on the [worst-case] motives which impel men to oppress and despoil others, as if they were the only motives by which men could possibly be motivated” (108). Macaulay was adamant that Mill had provided far too narrow an account of human motivation in the *Essay on Government*, thereby suggesting to the reader that items of tangible wealth provided the only example of a positively signed argument entering into a utility function, thus unduly neglecting the fact that men – although valuing tangible wealth – also placed a positive value on the receipt of public approbation: “Of those objects [positively signed

⁴⁶ Jon Elster has leveled a somewhat similar charge against modern constitutional political economy: “The [constitutional] framers are assumed to be exempt from the vices of politicians – impulsive passions, standing passions, and private interests – that constitute the rationale for constitution-making. But this, once again, is cant. The idea that framers are *demigods legislating for beasts* is a fiction” (Elster 2000, 172).

arguments comprising one's utility function] there [are] ... none which men in general seem to desire more than the good opinion of others. The hatred and contempt of the public are generally felt to be intolerable" (Macaulay 1978 [1829a], 105). Thus, Macaulay thought that the desire of public functionaries for the receipt of public approbation helped to constrain the abuse of government power at the relevant margin, thereby mitigating somewhat the worst-case conclusions of Mill's slave-driver equilibrium (see, Cowen 2000).⁴⁷

We can read Macaulay's argument (1978 [1829a], 125) as follows: Imagine a canonical 2x2 prisoner's dilemma game matrix. The underlying situational logic of the game is such that the perennial lure of the off-diagonal pay-off provides each player with sufficient incentive to defect (other things equal). The logic of the incentive structure (the logic of row and column dominance) guarantees the attainment of sub-optimality (cell 4 of game theoretic fame). Now allow for the possibility that the monetary pay-offs are supplemented with approbational rewards and punishments: Defection is punished with widespread public infamy, whereas co-operation is rewarded with public approbation (Levy 1992, 100-104).⁴⁸ Attainment of the optimality

⁴⁷ "The desire of posthumous fame, and the dread of posthumous reproach and execration, are feelings, from the influence of which scarcely any man is perfectly free, and which in many men are powerful and constant motives of action" (Macaulay 1978 [1829a], 106). David Ricardo had raised similar objections against Mill's Essay: "I dare say you had good reasons for not explaining the influence of public opinion on government, but as it is one of the checks, and a most powerful one in such a government as ours, I should have expected that you would have noticed it" (Ricardo 1973 [27 July 1815], 211). Further, "you allow too much force to the stimulus of money, and the praise of Princes, and too little to the effect of public opinion, and the consciousness of deserving approbation" (Ricardo 24 Oct. 1815, 311). "No other assembly [the House of Commons] is perhaps so much under the influence of public opinion which you will allow is a great security for virtue" (Ricardo 30 Aug. 1815, 263).

⁴⁸ There is, however, far less of an actual disagreement between Mill and Macaulay regarding the importance of public opinion than Macaulay's review would suggest. In his *Essay on Education* (1992 [1823], 139-194), Mill suggested that moral education could remake the utility functions of the young. Moral education could induce a change in the marginal rate at which one would substitute monetary income for approbation. By increasing one's willingness to substitute income for approbation, thus increasing the slope of one's relevant indifference curves, moral education would reduce the likelihood of non-cooperative behavior in later life. Moral education was envisaged as eliminating the lure of the off-diagonal by means of remaking agent-type.

associated with cell 1 – the co-operative outcome – is now assured. Or are we missing something?

Reputational Externalities and potential failure in the Market for Approbation

In light of the important constraint provided by public opinion, Macaulay raised the possibility that monarchy might provide a somewhat more focal institution (Schelling 1960) upon which public opinion could readily coordinate than was the alternative set of rules of the game associated with democratic institutions: Macaulay suggesting that a monarch might prove somewhat easier to hold strictly accountable for the poor quality of public policy.⁴⁹ Macaulay suggested that the workings of representative institutions were far more opaque, however, than the workings of monarchy, and were thus more likely to be plagued by reputational externality problems: “[A] man who is lost in the crowd [a single representative] is less likely to have the fear of public opinion before his eyes than a man whose station and standard of living render him conspicuous” (108). Macaulay argued that no single representative had any incentive to internalize those negative externalities (loss of reputational capital borne by the representative body collectively) that resulted from his personal malfeasance. Any single representative would personally suffer but a mere fraction of the ensuing total loss of reputational capital (Klein 1974). Although Macaulay thought that public opinion provided a “most important restraint,” one that, were it to prove “sufficiently at command would supersede the use of the gallows and tread-mill” (106), he also recognized, however, that the marginal effectiveness of public opinion as a constraint upon government would be weakened wherever a reputational externality problem

⁴⁹ Macaulay, recognizing the potential for failure in the market for approbation, states, “when the popular estimate of virtues and vices is erroneous, which is too often the case, the love of approbation leads sovereigns to spend the wealth of the nation on useless shows, or to engage in wanton and destructive wars” (1978 [1829a], 128).

reared its ugly head. Were representative institutions to wholly replace the British constitution, however, and Macaulay argued that public approbation would be transformed from a non-common to a common pool resource, thereby making the slave-driver equilibrium somewhat more – rather than less - likely.⁵⁰

Complementarities in Mill's Constitutional Political Economy: Transparent Institutions

It is very important at this juncture to note that Macaulay later provided a somewhat more charitable reading of Mill's *Essay*. Macaulay,⁵¹ readily (and publicly) ceded that Mill had always intended for the *Essay on Government* (1820) to be read in conjunction with Mill's other political writings (Ball 1992). Indeed, Mill's other writings had ceded that the prevalence of reputational externalities would serve to weaken the constraint that public opinion provided against fiscal exploitation ("plunder"):

It is a great security, both for diligent and upright conduct in the judge [or any other public functionary], that he occupy *singly* the judgement seat. When a man knows that the whole credit and reward of what is done well; the whole punishment and disgrace of what is done ill, will belong to himself, the motive to good conduct is exceedingly increased (Mill 1992, 89-90).⁵²

It is truly important that we note the immense importance placed by utilitarian constitutional political economy placed on the necessity that the workings of government policy prove wholly transparent (Semple 1993, 317-323). Transparent policy, of course, helps to mitigate the any

⁵⁰ Reputational externalities lead to the unraveling of the cooperative equilibrium (that characterized by moral aptitude). The Folk Theorem holds that either equilibrium is a possibility.

⁵¹ See Trevelyan (1961 [1876], 127-128, 324, 421).

⁵² "Moral aptitude must be considered as exactly proportioned to the strictness of the functionary's dependence on *public opinion*" (Bentham 1984 [1830], 174). "Singly seated, a functionary finds not any person on whom he can shift off the whole or any part of the imputation, of a mischievous exercise given to any of his functions. Not so, when he has a colleague" (174). "He finds not, in the same situation with himself, any person to share with him, and in proportion draw off from him, the whole, or any part, of any lot of approbation" (174). "His reputation stands altogether upon the ground of his actions" (174).

reputational externality problems.⁵³ Mill suggested that “publicity” (1992, 88) provided the “great instrument” (88) upon which the marginal effectiveness of approbational constraints depended. Indeed, Mill thought that such “publicity” (or common-knowledge) provided the “principle of life and strength to all other securities” (Mill 1992, 88; see, e.g., Feigenbaum and Levy 1996).⁵⁴

Where the first-best solution of wholly transparent government policy⁵⁵ was unattainable, however, Mill thought that a free press would facilitate a second-best solution to any potential reputational externality problem. Mill thought the relationship between agent-type and the rules of the game was more one of complementarity than the prima facie substitutability that is suggested by a cursory reading of the *Essay*. Mill’s 1823 essay *Liberty of the Press* (Ball 1992, 95-135) provides ample evidence that Mill was aware of the somewhat stringent informational requirements that were necessary for electoral mechanisms to prove efficacious in removing political knaves from office. Mill made it quite clear that the electorate had to have adequate

⁵³ A reader of Jeremy Bentham’s constitutional writings, failing to recognize the great importance placed by Bentham upon the transparency of policy, might dismiss Bentham’s remark that upon “architecture good Government has more dependence than men have hitherto seemed to be aware of” (1984 [1830], 55) as no more than eccentricity. See, however, Semple (1993). “The prospect of the immediate and public exposure of all acts of [knavery] ... would be a most effectual expedient to prevent their being committed” (Mill 1992, 106). “That motive [to refrain from opportunism] almost every man would derive from the knowledge that he had the eyes upon him of all those, the good opinion of whom it was his interest to preserve: that no immoral act of his would escape their observation, and a proportionate share of their hatred and contempt. It is in this view that the aid of religion has been sometimes regarded as of importance to morality: suggesting the idea of a high and constant observer” (Mill 1992, 107). Mill (1992, 199, 218) makes clear the importance that Bentham placed upon architecture as a means by which to make policy transparent.

⁵⁴ “Every transaction of the great functionaries of the state is, by means of the press, conveyed in two days to the extremities of the kingdom, and the alarm is sounded if any measure is adopted, or even proposed, which might in its tendency be hurtful to the community ... The press, amongst an enlightened and well-informed people, is a powerful instrument to prevent misrule” (Ricardo 1971 [1824], 497).

⁵⁵ Mill illustrated the first-best solution thus: “The fable of Momus has always been understood to carry an important moral. He found grievous fault that a window had not been placed in the breast of every man, by which, not his actions alone, but his thoughts, might have been known. The magnanimity of that Roman has been highly applauded, who not only placed his residence in such a situation that his fellow-citizens might see as much as possible of his actions, but declared a wish that he could open to all eyes his breast as well as his house” (Mill 1992, 106).

knowledge of any acts of legislative malfeasance if they were to vote the miscreants out of office: "If the people have not the means of knowing the actions of all public functionaries, they have no security for the good conduct of their representatives" (1992, 123).⁵⁶

Approbational incentives mitigate the ever-present lure to 'defect' that is provided by the off-diagonal pay-offs, thus serving to modify the pay-offs accruing to one's choice to co-operate or defect (see Levy 1992). Exchange (e.g., the Edgeworth Box) is somewhat vulnerable to opportunism on the part of the traders. Any trader would prefer to grab rather than engage in exchange (Levy 1992): It is far better to have nuts and oranges rather than oranges (or nuts) alone. Katallactic models of government view politics as a set of highly intricate political exchanges. If two-party trade is modeled as akin to a simple prisoners' dilemma game of the standard type, the katallactic account of government is more akin to a large-numbers prisoners' dilemma type situation. In each case, the perennial lure of the off-diagonal pay-off – the incentive to 'grab' in one case or engage in political 'looting' in the other – is ubiquitous. The principal difference between 'private' and 'political' exchange, however, is the fact that approbational incentives are relatively more efficacious in mitigating any incentives to defect in the case of two-party trade. Each player can monitor with relative ease (and at low cost) what the other player is doing (playing co-operate or playing defect). Furthermore, the lure of repeat dealings conjunct with the positive or negative approbation that accompanies one's choice to co-operate or defect helps to negate the 'grabbing' problem. In the case of politics, however, the problem of opacity rears its ugly head: It is somewhat unclear as to which players are identifiably engaging in grabbing rather than trading. Similarly, opacity serves to short-circuit the incentives to co-operate

⁵⁶ "Suppose it is the duty of their representatives to watch the conduct of the judges, and secure the perfection of the judicature, the people cannot know whether their representatives perform this duty, unless they know what the conduct of the judges is. Ignorance of this would of itself suffice to vitiate the government. ... They [the populace] are deprived of all trust-worthy means of knowing, if any limit whatsoever is placed to the power [of the press] to censure (Mill 1992 [1823], 123).

that are provided by the lure of repeat dealings (plus time horizons are somewhat attenuated in the case of politics. See, e.g., Brennan and Buchanan 2000 [1985], 87-107). Transparency, however, as was recognized by Bentham and James Mill, privatizes approbational pay-offs, thereby rendering Macaulay's 'approbational commons' objection to representative institutions somewhat impotent. Approbational incentives – conjunct with transparent institutions – greatly mitigate the incentive to engage in political 'grabbing', thereby helping to induce the co-operative outcome.

Macaulay's worst-case critique of representative institutions.

Macaulay displayed great umbrage at what he saw as Mill's clear failure to pursue the worst-case axioms of the *Essay on Government* (1820) to their logical conclusion. In particular, Macaulay was quite adamant in maintaining that Mill's democratic conclusions were plainly incompatible with the worst-case axioms employed in the *Essay*: "How is it possible for any person who holds the [worst-case] doctrines of Mr. Mill to doubt, that the rich, in a democracy such as that which he recommends, would be pillaged as unmercifully as under a Turkish pacha?" (Macaulay 1978 [1829a], 120). Macaulay worried that democratic institutions would bring a particularly acute inter-generational externality problem in their wake: "[Why should we] suppose that the people will be deterred from procuring immediate relief and enjoyment by the fear of distant calamities, of calamities which may not be fully felt till the times of their grandchildren" (121).⁵⁷ In light of Macaulay's suggestion that representative institutions created a

⁵⁷ Macaulay's worst-case view of universal suffrage is illustrated by the speech he gave on the People's Charter in 1842: "My firm conviction is that, in our country, universal suffrage is incompatible, not with this or that form of government, but with *all forms of government* and with everything for the sake of which forms of government exist: that is incompatible with property, and that it is consequently incompatible with civilisation" (Bain 1882, 227). Although spoliation is detrimental to the long-run interests of the masses, their short-run interests dictate that they engage in present plunder. We shall see below, that T. Perronet Thompson, replying to Macaulay in the pages of the *Westminster Review*, invoked best-case thinking to evade Macaulay's point. J. S. Mill (1998 [1861], 294-295), however, clearly recognizes the potential validity of Macaulay's argument.

reputational common pool, it is clear why he thought that approbational incentive mechanisms provided a wholly inadequate means by which to mitigate the worst-case effects of any such inter-generational externality problems.

Despite Mill's statement that the *Essay* was meant as a "skeleton map" illustrating "the principles of human nature" (see, e.g., Ball 1980, 93), the *Westminster Review* rather strangely chose to treat the *Essay* as though it were a stand-alone piece when mounting its defense of Mill against Macaulay's pungent strictures.⁵⁸ We shall turn now to consideration of the second-stage of the Mill-Macaulay debate: the somewhat acrimonious exchanges involving Macaulay and the *Westminster Review*.

The Debate with the *Westminster Review*: T. B. Macaulay vs. T. Perronet Thompson

The *Westminster Review*, mounting a defense of Mill under the title: '*Greatest Happiness' Principle* entered the Mill-Macaulay fray in June 1829.⁵⁹ Intriguingly, it was T. B. Macaulay, however, who more readily warrants the name of worst-case thinker (certainly far more than Mill) when evaluating the consequences of universal suffrage: "Is it possible that institutions may be established which, without the help of earthquake, of famine, of pestilence, or of the foreign sword, may undo the work of so many ages of wisdom and glory, and gradually sweep away taste, literature, science, commerce, manufactures, every thing but the rude arts

⁵⁸ Mill (1992, 304-314) equally treats the *Essay on Government* as though it were a stand-alone piece. This contradicts many of the remarks scattered throughout his *Political Writings* (Ball 1992).

⁵⁹ Thomas (1979, 139) states, "Bentham MSS., U.C.L., Box xiv, ff. 314-411, shows that the article was a co-operative effort between Bowring, Bentham, and Thompson." Also see Lively and Rees (1978, 5). Bentham, however, "felt that he must dissociate himself from such a clumsy display. He wrote a letter to the *Examiner* in which he admitted to offering or consenting to the use of (he could not recall which) his notes on the *Greatest Happiness Principle*, but adding that he was not responsible for anything that had been said in the published article against the *Edinburgh Review*. He completed the impression of senile disingenuousness by denying that he had read the article in question" (Thomas 1979, 140). Ball (1992, xxv) notes James Mill's extreme dissatisfaction with the *Westminster Review*'s replies to Macaulay.

necessary to support animal life?" (Macaulay 1978 [1829a], 122; see Bain 1822, 227). The question of what incentive the poor majority would have to plunder the property of the wealthy lay at the very heart of the Mill-Macaulay debate.⁶⁰ T. Perronet Thompson (proprietor of the *Westminster Review*)⁶¹ argued that the poor – once fully cognizant of the social benefits generated by the institution of private property – would have no incentive whatsoever to plunder the property of the rich. Unsurprisingly, T. B. Macaulay (fully aware of the pervasive lure provided by the off-diagonal pay-off) found Thompson's reply anything but persuasive.⁶²

Incentive-compatibility: Christianity and the Greatest Happiness Principle.

The participants in the Mill-Macaulay debate quite readily accepted that the Greatest Happiness Principle and the Golden Rule of Christianity were formally equivalent (Levy 2001).⁶³ Where they did differ with one another, however, was with regard to the incentive-compatibility (or otherwise) of the Greatest Happiness Principle. Macaulay, for one, was adamant that the Benthamite principle was incentive-incompatible, proving "no more than the Golden Rule of the Gospel without its sanction" (Macaulay 1978 [1829b], 176). The Greatest Happiness Principle –

⁶⁰ See Ricardo (1971 [1824], 499-500, 501).

⁶¹ "John Mill later said of him that he had "an understanding like a pin, going very far into a thing, but never covering a larger portion of it than the area of a pin's point" (Thomas 1979, 139).

⁶² "So essential does it appear to me, to the cause of good government, that the rights of property should be held sacred, that I would agree to deprive those of the elective franchise against whom it could justly be alleged that they considered it their interest to invade them. But in fact it can only be amongst the most needy in the community that such an opinion can be entertained. The man of a small income must be aware how little his share would be if all the large fortunes in the kingdom were equally divided among the people. He must know that the little he would obtain by such a division could be no adequate compensation for the overturning of a principle which renders the produce of his industry secure" (Ricardo 1971 [1824], 500-501).

⁶³ "There is no war between Christianity and philosophy. Pure and undefiled Christianity is sound philosophy" (T. Perronet Thompson 1978 [1830], 245).

although formally equivalent to the Golden Rule – was in practice a wholly inadequate substitute for the Golden Rule of Christianity:

In the Christian scheme, accordingly, it [the Golden Rule] is accompanied by a sanction of immense force. To a man whose greatest happiness in this world is inconsistent with the Greatest Happiness of the Greatest Number, is held out the prospect of an infinite happiness hereafter, from which he excludes himself by wronging his fellow creatures here (Macaulay 1978 [1829b], 175-176).

Macaulay thought the Golden Rule (rendered adequately incentive-compatible by the pay-offs of heaven and hell) somewhat akin to that “practical philosophy,” upon which “penal legislation is founded” (176). The Greatest Happiness Principle, however, simply failed to provide the individual with any inducement to good conduct akin to that provided by the promise of heaven and hell. Macaulay challenged Thompson thus:

[A] man may so greatly prefer the life of a thief to the life of a labourer, that he may determine to brave the risk of detection and punishment, though he may even think that risk greater than it really is. ... [H]ow on Utilitarian principles, is such a man to be convinced that he is in the wrong? “You will be found out” ... “You will be hanged within two years” ... “[W]hy do you pursue this lawless mode of life?” – “Because I would rather live for one year with plenty of money, dressed like a gentleman, eating and drinking of the best, frequenting public places, and visiting a dashing mistress, than break stones on the road, or sit down to the loom, with the certainty of attaining a good old age.” ... Does he [T. Perronet Thompson] not see that it is no more possible to reason a man out of liking a short life and a merry one than a long life and a dull one, than to reason a Greenlander out of his train oil? We may say that the tastes of the thief and the tyrant differ from ours; but what right have we to say, *looking at this world alone*, that they do not pursue their greatest happiness very judiciously? (Macaulay 1978 [1829c], 217-218).

Macaulay was adamant that whereas the Golden Rule provided the thief with sufficient “motive for doing as he would be done by” (Macaulay 1978 [1829b], 176), the Greatest Happiness Principle simply failed to provide any set of incentives adequately substituting for ‘heaven and hell’: the philosophic radical lacked any adequate means by which to induce the would-be thief to

ignore the lure of the off-diagonal pay-off, choosing instead to rigidly adhere to a norm emphasizing the virtue of reciprocity.^{64, 65}

T. Perronet Thompson, however, failed to provide anything closely akin to an adequate rebuttal to Macaulay's pungent critique of philosophic radicalism, simply asserting that the "greatest happiness of the individual ... [is] in the long run to be obtained by pursuing the greatest happiness of the aggregate" (Thompson 1978 [1829b], 187).^{66, 67} Intriguingly, Thompson appeared somewhat unwilling to even cede the possibility that agents might face a non-convex choice situation (Levy 1992; Stiglitz 1994). Macaulay, however, clearly accepted the possibility that individual rationality and collective rationality might on occasion prove somewhat incompatible. Macaulay reiterated the charge that the Greatest Happiness Principle was incentive-incompatible:

They [the Westminster Review] have taken the precept of Christ, and left the motive; and they demand the praise of a most wonderful and beneficial invention, when all that they

⁶⁴ The Edinburgh Review had leveled the charge that Utilitarianism was potentially incentive-incompatible in April 1804: "[A]ctions are performed by individuals, and all the good may be to the individual, and all the evil to the community. There are innumerable cases, in which the advantages to be gained by the commission of a crime are incalculably greater than the evils to which it may expose the criminal. This holds in almost every instance where unlawful passions may be gratified with very little risk of detection. A mere calculation of utilities would never prevent such actions; and the truth undoubtedly is, that the greater part of men are only withheld from committing them by those general impressions of morality, which it is the object of Mr. Bentham's system to supersede" (Edinburgh Review 1804, 14).

⁶⁵ Thompson (1829a, 141) had, however, recognized that the "word *ought*, if it means any thing, must have reference to some kind of interest or motives." Despite having recognized the crux of the incentive-compatibility problem, Thompson could provide no adequate reply to Macaulay's charges. "In the golden rule of Jesus of Nazareth, we read the complete spirit of the ethics of utility. To do as one would be done by, and to love one's neighbour as oneself, constitute the ideal perfection of utilitarian morality" (J. S. Mill 1969 [1861], 218). "Acts are performed, only because there are motives to the performance of them. Of course, injurious acts are performed, only because there are motives to the performance of them" (James Mill 1992, 64).

⁶⁶ Thompson made the following assumptions: 1) the individual maximized over an infinite time-horizon, and 2) the individual had a zero discount rate. Levy (1992) provides an illuminating discussion of the role that these two best-case assumptions have played in the history of political economy.

⁶⁷ "[T]he conduct which leads to the greatest happiness of the aggregate, is in the end the soundest policy for the individual" (Thompson 1978 [1829b], 188).

have done has been to make a most useful maxim useless by separating it from its sanction (Macaulay 1978 [1829c], 221).^{68, 69}

Mill was quite aware that the efficacy of the electoral sorting mechanism proposed in the *Essay* required that representatives optimize over a relatively lengthy time-horizon (see, e.g., Mill 1978 [1820], 75; 1992, 67), with any act of knavery committed at T_0 punishable by electoral defeat at T_1 . Macaulay was less than persuaded, however, arguing that even given the certainty of electoral defeat one might still discount the future so heavily that knavery at T_0 would prove the optimal strategy (Macaulay 1978 [1829c], 217-218).⁷⁰ Thompson's counter to Macaulay – one invoking zero time preference – was clearly an inadequate response (Levy 1992, 254-256).⁷¹ How might the Utilitarian defender of Mill's *Essay* provide a somewhat more adequate reply to Macaulay's challenge, however, than that provided by the *Westminster Review*? At this juncture, Jeremy Bentham's *Auto-Icon* plan enters the fray.

Auto-Icon: Making the Greatest Happiness Principle Incentive-Compatible?

Jeremy Bentham's Auto-Icon (1832) scheme has been subject to undue neglect by the economics literature (see Levy 1992, 164-165; Cowen 2000, 146-149). Indeed, the usual response

⁶⁸ "It may perhaps be said that, in the long run, it is for the interest of the people that property should be secure, and that therefore they will respect it. We answer thus:- It cannot be pretended that it is not for the immediate interest of the people to plunder the rich. Therefore, even if it were quite certain that, in the long run, the people would, as a body, lose by doing so, it would not necessarily follow that the fear of remote ill consequences would overcome the desire of immediate acquisitions. Every individual might flatter himself that the punishment would not fall on him" (Macaulay 1978 [1829a], 119).

⁶⁹ "On religious principles, it is true that every individual will best promote his own happiness by promoting the happiness of others. But if religious principles be left out of the question, it is not true. If we do not reason on the supposition of a future state, where is the motive?" (Macaulay 1978 [1829c], 221).

⁷⁰ The *Edinburgh Review* made a similar charge against Utilitarianism (*Edinburgh Review* 1804, 14).

⁷¹ Like a knave, the "baby runs all risks for the present gratification of a very paltry appetite; but vastly altered is its estimate of things, when the gripes come upon it like an armed man" (Thompson 1978 [1830], 233).

from an economist learning of Bentham's proposal for the first time is one of somewhat amused incredulity: how could Bentham possibly have been serious? Levy (1992), however, suggests that we ought to read *Auto-Icon* as a paradigmatic exercise in the economics of fame (see Adair 1992). Reading *Auto-Icon* as such, one can quite readily make the link between Bentham's scheme and the Mill-Macaulay debate: the judgment provided by posterity can serve to markedly lengthen the time-horizon over which an individual optimizes. Though opportunistic conduct (defection) proves the optimal strategy – supposing, of course, that pay-offs are linked to monetary income alone – in one-shot Prisoner's Dilemma type situations, if we allow the relevant pay-offs to be represented by a vector of both money income and approbation, however, then co-operation might prove one's optimal strategy (Levy 2001).⁷² Moreover, the potential receipt of disapprobation in all future periods (for a repeated game) might serve to induce co-operation in the present; indeed, any act of political knavery in T_0 might earn one's *Auto-Icon* a potentially lengthy stay (T_1 through to T_n) in Bentham's envisaged Temple of Shame at T_1 (the date of one's death).⁷³ Thus, Bentham's *Auto-Icon* plan provides something of a Utilitarian substitute for the Christian afterlife (a pay-off, upon which Macaulay, of course, had placed such weight).

Bentham suggested that "out of *Auto-Icons*, a selection might be made for the Temple of Fame ... Sometimes for honour, sometimes for reproach, will *Auto-Icons* be preserved. Not many

⁷² David M. Levy (personal correspondence, November 22 2001) wrote: "Maybe your thesis is that Macaulay is right ... CPE [constitutional political economy] needs katalactics ... Does Mill take reciprocity for granted in *Government* [1820] the way that General Equilibrium theorists take property rights [for granted] with the "individual rationality" axiom?" It has taken me several months (and some more reading) to see that Levy's conjecture was highly apposite. Approbational mechanisms and katalactic theories of government go hand-in-hand with one another. Ali Khan's lecture at the 2000 Summer Institute for the Preservation of the Study of the History of Economics (organized by David M. Levy) was highly illuminating as regards the best-case thinking of GE theorists to which Levy makes reference. Also see Levy (1992, 21-22). See Mill (1992, 49).

⁷³ "The true check on bad administrations, is in setting before them the risk of present ruin, and of future if not present disgrace. Will the reputation of the conductors of the American and anti-revolutionary wars, be any prize in a lottery a century hence?" (Thompson 1978 [1830], 240).

years ago, the heads of so-called traitors presided over the gate of Temple Bar” (Bentham 1832,

7). Public opinion – the potential receipt of positive approbation – would therefore provide adequate inducement to good behavior:

There would be pilgrimages to Auto-Icons, who had been living benefactors of the human race. ... The Auto-Icons of the virtuous in their silence would be eloquent preachers. “Go thou and do likewise,” would be the lessons they would teach. ... What will be said of my Auto-Icon hereafter? The good report obtained by good conduct will attach to the man after death. ... he must anticipate the judgement of his fellow men (Bentham 1832, 7).

Bentham, however, abjectly failed to address the possibility that failure might arise in the market for future fame, providing no good reason as to why the Greatest Happiness Principle – rather than some alternative moral code – would prove a focal point upon which public opinion could readily coordinate (Schelling 1960).⁷⁴

John Mill took Macaulay’s charge that the Greatest Happiness Principle was incentive-incompatible very seriously (Mill 1969 [1861], 218-219).⁷⁵ Mill placed great faith in ethology, the science of character formation (see, e.g., Robson 1968), suggesting that moral education would help to mitigate the perennial lure of the off-diagonal pay-off. Moral education would inculcate other-regarding feelings in the young, thereby leading them to internalize any externalities that their conduct might otherwise generate:

[B]y the improvement of education, the feeling of unity with our fellow creatures shall be (what it cannot be doubted that Christ intended it to be) as deeply rooted in our character.

⁷⁴ In *On Liberty* (1859), however, and in several of his essays on socialism, J. S. Mill worries a great deal about the potential downside associated with approbational enforcement mechanisms. Mill worries over the possibility for approbational “lock-in”: the possibility that public opinion might coordinate upon a highly sub-optimal set of social norms.

⁷⁵ See e.g., *Of the Ultimate Sanction of the Principle of Utility* (J. S. Mill 1969 [1861], 226-233).

⁷⁶ Mill (1969 [1861], 227) recognized the challenge inherent in Macaulay (1978 [1829c], 217-218): “[W]hy am I bound to promote the general happiness? If my own happiness lies in something else, why may I not give that the preference?”

and to our own consciousness as completely a part of our nature, as the horror of crime is in an ordinarily well brought-up young person (Mill 1969 [1861], 227)."

Moral education would facilitate the transformation of agent-type: *homo economicus* to *non-homo economicus*.⁷⁸ Indeed, James Mill had argued that "Education is like the key-stone of the arch; the strength of the whole depends upon it" (see, e.g., Ball 1992, 193).

A Paradox of Worst-case Thinking?

In J. S. Mill's *Autobiography* (1873), we are told that the younger Philosophic Radicals regarded James Mill's *Essay on Government* (1820) as a "masterpiece of political wisdom" (93).⁷⁹ David Ricardo had an equally favorable view of the *Essay* (Ricardo 1820, 211). The following figure (Levy 2002) will help us to sharpen our understanding of what was at issue in the Mill-Macaulay debate:

⁷⁷ "[L]aws and social arrangements should place the happiness, or (as speaking practically it may be called) the interest, of every individual, as nearly as possible in harmony with the interest of the whole: ... [E]ducation and opinion, which have so vast a power over human character, should so use that power as to establish in the mind of every individual an indissoluble association between his own happiness and the good of the whole" (Mill 1969 [1861], 218). "Men would obtain the habit of abstaining from [e.g., theft] ... and would feel it as little painful to abstain, as at present it is to any well educated person to keep from theft, or those acts which constitute the ill manners of the vulgar" (James Mill 1992, 106). With bad education, "the foundation is laid of the bad character, - the bad son, the bad brother, the bad husband, the bad father, the bad neighbour, the bad magistrate, the bad citizen, - to sum up all in one word, the bad man" (James Mill 1992, 181).

⁷⁸ "The principal error of narrowness with which they [political economists] are frequently chargeable, is that of regarding ... their frequent experience of mankind, as of universal validity; mistaking temporary or local phases of human character for human nature itself; having no faith in the wonderful pliability of the human mind; deeming it impossible, in spite of the strongest evidence, that the earth can produce human beings of a different type from that which is familiar to them in their own age" (Mill 1969, 306)

⁷⁹ "The *Essay on Government*, in particular, has been almost a text-book to many of those who may be termed the Philosophic Radicals" (Mill 1833, CW, I: 594).

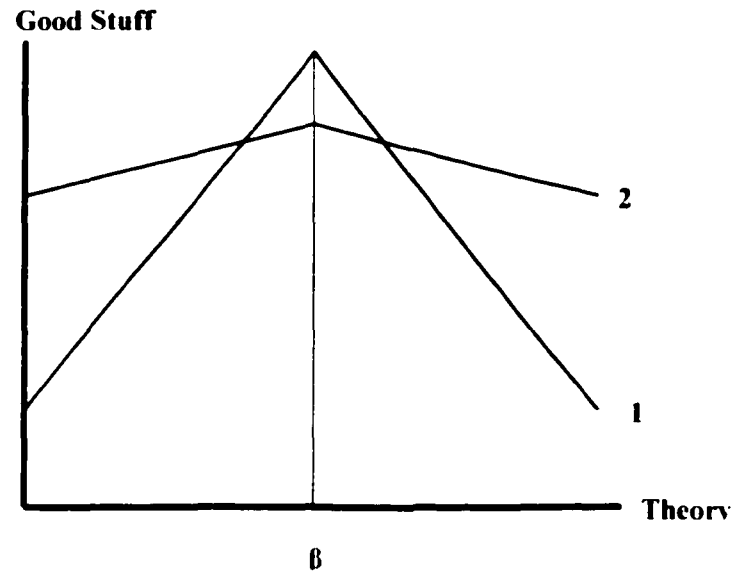


Figure 2: Robust institutions?⁸⁰

Envisage two different sets of ‘constitutional rules of the game’.⁸¹ Let **1** represent monarchy. Let **2** represent democratic institutions. At any state of the world other than that depicted by the neighborhood around β , representative institutions [**2**] generate more “good stuff” (social welfare) than the ‘good stuff’ that is generated by monarchy [**1**]. In the terminology of modern statistics, rules of the game **2** prove more robust than rules of the game **1** (Levy 2002). As we deviate from the idealized state of the world (assumptions of the model) represented by the neighborhood around β , the welfare loss associated with **2** is less than that associated with **1** (Levy 2002). James Mill’s worst-case axioms involve the commitment that since β (other-regarding behavior) fails to accurately characterize the state of the world, representative institutions are preferable to

⁸⁰ Levy (2002, 140) quotes John Tukey: “**The greatest value of a picture** is when it forces us to notice **what we never expected to see.**”

⁸¹ “[A] “constitution” is conceived as the set of rules, or social institutions, within which individuals operate and interact with one another” (Brennan and Buchanan 2000 [1980], 5).

monarchy; there being no limit otherwise, to the rapacity with which a monarchy or aristocracy would plunder the populace (Mill 1978 [1820], 55-78).

Macaulay argued that Mill's democratic conclusions were somewhat incompatible with the worst-case axioms of the *Essay*. Thus, Macaulay suggested that in order for Mill to demonstrate that the rules of the game represented by **2** were superior to the rules of the game represented by **1**, he would have to implicitly invoke his own β -type supposition.⁸² Macaulay argued that herein lay the paradox of worst-case thinking: Mill favored **2** because men were not particularly public-spirited (agent-type was that of *homo economicus*). To implement the set of rules of the game represented by **2**, however, would only improve the state of affairs if men were somewhat rather more public-spirited than Mill worst-case axioms had otherwise given them credit for; thus Macaulay's insistence that Mill's worst-case assumptions were incompatible with the advocacy of representative institutions provided in the *Essay*.

To illustrate Macaulay's charge that Mill readily engaged in best-case thinking when it suited his purpose, I suggest that we examine a certain "infamous" paragraph from Mill's *Essay*. The paragraph in question is that regarding which the young John Mill wrote of as the "worst in point of tendency which he [James Mill] ever wrote" (see, Ball 1980, 92-93).

Best-case Thinking about Voters: Restricted Suffrage as Robust Estimator?

Despite thinking the 'system of representation' a prerequisite for anything akin to good government, James Mill accepted that democratic institutions per se might fail to provide adequate security against the sub-optimality of "bad government" (Mill 1973 [10 Oct.1815], 308). If the electorate were to constitute a 'sinister interest' (Bentham 1989 [1822], 205) they

⁸² That the slope of the loss function associated with **2** is less than that associated with **1**, is an artifact of Mill's best-case (β) assumption.

would simply elect those representatives who were willing to supply them with perquisites (income transfers).⁸³ Thus, the electorate – wholly in keeping with the worst-case axioms employed in the *Essay* – would seek to exploit their fellow men with no less a degree of rapacity than that Mill thought intrinsic to monarchy or aristocracy: the slave-driver equilibrium thereby resulting. Mill argued that universal suffrage would avert that unpleasant possibility: serving to necessarily eliminate any possibility for legislation that was favorable to sinister as against the general interest. Universality of the franchise would serve to induce an artificial identity of interests between “community” and “choosing body” (electorate).⁸⁴ Despite finding universal suffrage attractive, Mill was insistent that the requisite identity of interests could be induced by a somewhat less inclusive voting rule: one restricting the electoral franchise to a particular subset of the populace. In the lingua franca of modern statistics, Mill proposed that the suffrage, even were it restricted to a particular subset of the populace could still provide an adequately robust estimator for the interests of the entire “community” (Levy 1992): “[B]etween these extremes [a high and low property qualification], [is] there ... any qualification which would remove the right of Suffrage from the people of small, or no property, and yet constitute an elective body, the interest of which would be identical with that of the community?” (81). At this juncture, Mill flagrantly made a best-case move, one positing an interdependence of utility functions among men and women:

⁸³ “[T]he interest of the Monarch is essentially a sinister interest” (Bentham 1989 [1822], 205).

⁸⁴ “The Community cannot have an interest opposite to its interest. To affirm this would be a contradiction in terms. The Community within itself, and with respect to itself, can have no sinister interest” (Mill 1978 [1820], 60). Mill (1844 [1821], 155-156) provides a further example of verbal sophistry defining away the possibility of a clash between individual and collective welfare. J. S. Mill allowed his father to have none of it: “The proposition that the electors, when they compose the whole of the community, cannot have an interest in voting against the interest of the community, will be found on examination to have more sound than meaning in it. Though the community as a whole can have (as the terms imply) no other interest than its collective interest, any or every individual in it may” (J. S. Mill 1998 [1861], 362).

[A]ll those individuals whose interests may be indubitably included in those of other individuals, may be struck off [the envisaged electoral register] without inconvenience. In this light may be viewed all children, up to a certain age, whose interests are involved in those of their parents. In this light, also, women may be regarded, the interest of almost all of whom is involved in either that of their fathers or in that of their husbands (Mill 1978 [1820], 79).⁸⁵

Thus, it is in light of this purported interdependence of utility functions that Mill could state with clear conscience: "an interest, identical with that of the whole community, is to be found in the aggregate males" (79).⁸⁶

Mill invokes the best-case supposition of interdependent utility functions to ensure that legislative decision-making places an equal weight on male and female welfare losses. Are men over 40, however, a particularly good proxy for the welfare of women? As we shall see, Macaulay picked up this particular question and ran with it to great effect. Macaulay thought that Mill's electoral body would provide a far from robust estimator for the 'public' interest: interdependent utility functions might well serve to ensure optimal policy choices, but the supposition of such benevolence (or universal love) provides a very weak supposition upon to which to grant men discretionary power over women. Indeed, such an assumption appeared to nullify the worst-case axioms of Mill's *Essay*. A woman engaging in a worst-case thought experiment would hardly hand the representation of her interests on a platter to the opposite sex. The worst-case scenario for a woman would be that of slavery, her interests having fallen into the less-than-merciful hands of a plantation rapist. For Mill to have invoked such an identity of interests between the sexes is remarkable given his favored illustration of the *Essay*'s worst-case axioms, namely, the behavior of a West Indies plantation owner (67-68). Macaulay subjected

⁸⁵ This is the infamous paragraph to which J. S. Mill made reference (see Ball 1980, 92-93). On the question of James Mill, feminism, and the franchise, I refer the interested reader to Ball (1980).

⁸⁶ "The great principle of security here is, that the men of forty have a deep interest in the welfare of the younger men" (Mill 1978 [1820], 80).

Mill's supposition of interdependent utility functions to scathing criticism, charging that Mill had placidly dogmatized "away the interests of one half the human race" (Macaulay 1978 [1829], 116).⁸⁷ "Women have always been, and still are, over the greater part of the globe, humble companions, playthings, captives, menials, beasts of burden" (Macaulay 1978 [1820], 116).

In terms of **Figure 2**, therefore, we can see that Mill's "great principle of security ... that the men of forty have a deep interest in the welfare of the younger men" (1978 [1820], 80), provides the relevant β -type best-case assumption of the *Essay on Government*.⁸⁸

Constitutional Political Economy and the paradox of worst-case thinking?

Is it possible for the constitutional political economist to engage in pure worst-case thinking? Surely so, but only at a price: namely, the willingness to do no more than preach a counsel of despair.⁸⁹ Gordon Tullock appositely states, "the view that the government can be bound by specific provisions is naïve. Something must enforce those provisions, and whatever enforces them is itself unbounded" (Tullock 1987, 87). Tullock clearly recognizes that constitutional political economists have something of a penchant for straying from their worst-case axioms on occasion. Is the constitutional political economist ultimately something of a best-case thinker? In light of Tullock's remarks (1987, 87), it surely ill suits the constitutional political

⁸⁷ William Thompson's *Appeal of One Half the Human Race* (1825) similarly attacked Mill's best-case thinking on this particular topic (see Ball 1980, 110-115). Thompson's analysis is, however, marred by his eagerness to attack industrialization for transforming men and women into "white slaves". Thompson favorably compares the situation of female slaves in the West Indies to the situation of white female factory workers. Levy (2001), although not discussing Thompson, provides an excellent analysis of the 'industrialization as white slavery' debate.

⁸⁸ Macaulay adroitly hoisted Mill with his own petard: "[If] the kind feelings of one half the species be a sufficient security for the happiness of the other, why may not the kind feelings of a monarch or an aristocracy be sufficient at least to prevent them from grinding the people to the very utmost of their power?" (Macaulay 1978 [1820], 116-117).

⁸⁹ "[T]o call a situation hopeless is for practical purposes the same thing as calling it ideal" (Knight 1982 [1939], 55).

economist (of all people) to invoke a supposition of public-spiritedness regarding the agent who is ultimately charged with the task of enforcing the constitutional rules of the game. Does constitutional political economy have something akin to a benevolent-despot assumption (so despised by public-choice theory) at its very heart?

Intriguingly, John Mill argued in a somewhat similar vein to Tullock: "In politics as in mechanics, the power which is to keep the [constitutional] machinery going must be sought for outside the machinery" (Mill 1998 [1861], 182). In Tullock's view (1993, 16), the most "important question" facing public choice theory is that of how to design a self-enforcing (incentive-compatible) set of constitutional rules of the game? Tullock readily admits to having no good answer to that particular question. One can hardly invoke best-case thinking when purporting to answer Tullock's pungent query and still remain in good stead as a worst-case thinker. Of course, the price of remaining true to the worst-case methodological spirit of constitutional political economy may prove far too high: after all, who wants to preach a counsel of despair?

The Constitutional Political Economist as Preacher?

Virginia political economy has long insisted that economists not place their hopes for the attainment of 'superior' economic and political outcomes in post constitutional (or lower level in-period) politics (thereby implicitly hoping that 'good' or public-spirited political agent-types will prevail at the post constitutional level), arguing that one ought instead to seek the reform of the constitutional rules of the game: seek to change the "*Constitution ...* [rather than] day-to-day policy" (Buchanan 2001, 46, italics added).⁹⁰ Constitutional political economy appears to posit a

⁹⁰ Constitutional political economy displays "little or no concern with replacing "bad," "evil," or "incompetent" politicians with others who may be "good," "kind," or "competent." The emphasis on constitutional reform is neither on persuasion nor on selection of "better" persons to act as agents in

fixity of agent-type,⁹¹ while the rules of the game (constraints), by contrast, are thought somewhat more open to change. The constitutional political economist argues that judicious reform of the rules of the game will prove sufficient to eliminate any given sub-optimality: for example, the tragedy of the commons (Brennan and Buchanan 2000 [1985], 16). Constitutional political economy views “preaching” – e.g., any attempt to simply urge that individuals ought to internalize the negative externalities consequent upon their use of the commons – as surely a far less effectual way to mitigate the commons problem than is the remedy providing for an efficiency-enhancing change in the rules of the game (in the case of the tragedy of the commons, a change in the structure of property rights).⁹²

In light of such considerations, Brennan and Buchanan (2000 [1985], 167) state, “good games depend on good rules more than they depend on good players.” Thus, constitutional political economy appears to view agent-type and the rules of the game as substitutes for one another (at least *prima facie*). At the center of John Mill’s forays into constitutional political economy, however, apparently lies the wholesale rejection of Brennan and Buchanan’s suggestion (2000 [1985], 167). Indeed, Mill repeatedly demurs at such a claim, arguing that high quality players and high quality rules are complements rather than substitutes for one another (Mill 1861, 192-194). Mill suggested that in addition to any necessary reform of the constitutional

governing roles” (Buchanan 2001 [1981], 46-47). Constitutional political economy seeks to set “up rules or constraints within which politicians must operate, rules that will make it a *relatively trivial matter as to the personal characteristics of those who happen to be selected as governors*” (Buchanan 2001 [1981], 47, italics added). “It is folly to think that “better men” elected to office will help us much, that “better policy” will turn things around here. We need, and must have, basic constitutional reform, which must of course be preceded by basic constitutional discourse and discussion” (Buchanan 1979, 181).

⁹¹ “[T]he fundamental character traits [agent-type] of human beings either cannot be, or should not be, manipulated deliberately” (Buchanan 1977, 12).

⁹² See, e.g., Brennan and Buchanan (2000 [1980], 13).

rules of the game, men must also learn to become “good players” (Brennan and Buchanan 2000 [1985], 167) of the game (see Robson 1968).

We suggest that the change in the rules of the game (privatization) that suffices to eliminate the tragedy of the commons be characterized a self-enforcing rule change. The suggested change in the rules of the game (the structure of ownership) is wholly congruent with the posited self-interest of the newly created private landowner: hence the rule change is aligned with agent-type such as to ensure the non-dissipation of available rents (see, e.g., Varian 1993, 559-562). The sub-optimality generated by poor quality constitutional rules of the game, however, although superficially similar in appearance to the tragedy of the commons, is, however, far from so readily as amenable to solution.⁹³ The constitutional rules of the game are not self-enforcing: the enforcement of the constitutional rules is surely dependent upon at least some modicum of other-regarding behavior, whether on the part of the citizenry or the judiciary. Privatization of the commons induces the first-best equilibrium irrespective of agent-type: private and social costs are equated at the margin irrespective of the public-spiritedness (or lack of such) that we might attribute to the individual landowner.⁹⁴ Prior to privatization, however, it is the very

⁹³ Brennan and Buchanan (2000 [1985], 16, italics added) state: “A change in the rules so that the scarce resource is separately and privately owned, along with means for *enforcing and protecting individuals in rights of ownership*, will remove the inefficiency [tragedy of the commons]”. The rule change that eliminates the ‘tragedy of the commons’ provides the landowner adequate incentive to equate the private and social costs of land use. In the case of changing the constitutional rules of the game (or enforcing the rules of the game), however, any individual can expect the private and social costs of their action to systematically diverge.

⁹⁴ I can think of no feasible mechanism for constitutional privatization akin to the solution to the commons problem. See, however, Friedman (1996, 113-114), who suggests that a market in citizenships would help to mitigate political agency problems in exactly the same way that stock markets help to mitigate corporate agency problems. I have heard a suggestion that politicians be paid with shares in the “market portfolio” of CAPM fame. I suggest that we read the following remark by James Mill in such a vein: “The smaller the period of time during which any man retains his capacity of Representative, as compared with the time in which he is simply a member of the community, the more difficult it will be to compensate the sacrifice of the interests of the longer period, by the profits of mis-government during the shorter” (Mill 1978 [1820], 75). The CAPM proposal would lead politicians to internalize any externalities

self-interestedness of the relevant agent-types (*homo economicus*) that creates the rent-dissipation problem. Other-regarding (public-spirited) agents would, by contrast, would likely internalize the relevant externalities, thus eliminating the commons problem without any necessity for change in the rules of the game.

In the case of constitutional reform, however, it appears likely (Hume 1741) that the prevalence of other-regarding agent-types negates the need for any such reform, whereas the prevalence of self-regarding agent-types would surely make constitutional enforcement a rather moot problem:

There are, there have been, many human beings, in whom the motives of patriotism or of benevolence have been permanent steady principles of action, superior to any ordinary, and in not a few instances, to any possible temptations of personal interest. There are and have been, multitudes, in whom the motive of conscience or moral obligation has been thus paramount. There is nothing in the constitution of human nature to forbid its being so in all mankind. Until it is so, the race will never enjoy one tenth-part of the happiness which our nature is susceptible of. I regard any considerable increase of human happiness, through mere changes in outward circumstances [rules of the game], unaccompanied by changes in the state of desires [agent-type], as hopeless; not to mention that while the desires are circumscribed in self, there can be no adequate motive for exertions tending to modify to good ends even those external circumstances. No man's individual share of any public good which he can hope to realize by his efforts, is an equivalent for the sacrifice of his ease, and of the personal objects which he might attain by another course of conduct. The balance can be turned in favour of virtuous exertion, only by the interest of *feeling* or by that of *conscience* – those "social interests," the necessary subordination of which to "self-regarding" is so lightly assumed (Mill 1969 [1833], 15).

Mill argued that without adequate transformation in the quality of the players, any change in the rules of the game such as would "force unprepared populations into [for example] Communist societies, even if a political revolution gave [one] the power to make such an attempt, would end in disappointment" (Mill 1967 [1879], 747). Mill's transformational political economy (see, e.g., Peart and Levy 2001) placed great importance on the potential for moral education to

that would result from legislation. Roll (1977), however, argues that the components of the "market portfolio" can never in practice be identified.

engineer the requisite transformation of agent-type: Mill placing great importance on the necessity to inculcate a moral code emphasizing “sufficient affection” (Hume) towards others amongst the young. Only the widespread adherence to a moral code stressing the importance of social unity would ensure that individuals act to equate the private and social costs of their conduct (see, e.g., Mill 1969 [1861], 226-227; Hollander 1985, 770-824; Levy 1992).

Brennan and Buchanan (see, e.g., Brennan and Buchanan 2000 [1980], 16; Buchanan 2001, 11) justifiably acknowledge Mill as a precursor of their own worst-case constitutional philosophy. Indeed, examples where Mill argues for constitutional constraints on classic Humean worst-case grounds are somewhat legion (see, e.g., Mill 1974 [1843], 891-893): “Feelings of philanthropy, [are] motives never to be mainly relied on, though (except in countries or during periods of great moral debasement) they influence almost all rulers in some degree and some rulers in a very great degree” (891). Mill recognizes that to posit any ubiquity of public-spirited agent-types provides far too unwarranted a supposition upon which to expect that political agents would prove wholly immune to the perennial lure of the off-diagonal: “Although the actions of rulers are by no means wholly determined by their selfish interests, it is chiefly as a security against those selfish interests that constitutional checks are required; and for that purpose, such checks, in England, and the other nations of modern Europe, can in no manner be dispensed with” (893).⁹⁵

⁹⁵ Mill’s worst-case theorizing is readily apparent: “Whether the institution to be defended is slavery, political absolutism, or the absolutism of the head of a family, we are always expected to judge of it from its best instances; and we are presented with pictures of loving exercise of authority on one side, loving submission to it on the other – superior wisdom ordering all things for the greatest good of the dependents, and surrounded by their smiles and benedictions. All this would be very much to the purpose if any one pretended that there are no such things as good men. Who doubts that there may be great goodness, and great happiness, and great affection, under the absolute government of a good man? Meanwhile, laws and institutions require to be adapted, not to good men, but to bad” (Mill, CW, vol. XXI, 287).

Mill clearly accepted the value of worst-case thinking – recognizing the fragility (or non-robustness) of any ‘model’ placing undue faith in the “philanthropy” (or public-spiritedness) of political agents. Despite Mill’s acceptance of the value of worst-case thinking (see, e.g., Mill, CW, vol. XXI, 287), it is important that we realize the degree to which Mill’s later political writings seek to address Macaulay’s pungent 1829 critique of the *Essay on Government* (1820). In particular, I suggest that we read Mill’s *Considerations on Representative Government* (1861) as an attempt to make repairs in the Utilitarian theory of government: an attempt which – while ceding many of Macaulay’s points – somewhat compensates for the wretched defense of the *Essay on Government* that the *Westminster Review* had mounted in 1829. Mill was particularly adamant that constitutional rules of the game and agent-type were complementary to one another.

Though arguing that “feelings of philanthropy” were of insufficient strength as would make constitutional constraints unnecessary, Mill was equally insistent, however, that such feelings had to prove sufficiently prevalent among the populace for the constitution to prove binding upon political agents:

[P]olitical checks will no more act of themselves than a bridle will direct a horse without a rider. If the checking functionaries are as corrupt or as negligent as those whom they ought to check, and if the public, the mainspring of the whole checking machinery, are too ignorant, too passive, or too careless and inattentive to do their part, little benefit will be derived from the best administrative apparatus (Mill 1998 [1861], 194).

John Mill suggested that although his father’s *Essay on Government* viewed the “constitution in the same light (difference of scale being allowed for) as ... [one] would ... [view] a steam plough, or a threshing machine” (1998 [1861], 205), no man would ever “[choose] even an instrument of timber and iron on the sole ground that it is in itself the best” (205). Mill thought it vital that those people by whom the constitutional machinery would “have to be worked, possess the knowledge and skill necessary for its management” (1998 [1861], 205). Mill faulted his father’s *Essay on Government* for its abject failure to explain why the constraints that

were provided by the electoral machinery would prove adequate to temper – if not to wholly avert– the slave driver equilibrium. As Mill pungently put it: “Political machinery does not act of itself” (207).⁶⁶ In his *Considerations on Representative Government* (1861), Mill attempted to identify those qualities that would transform a potentially robust set of constitutional rules of the game into an actually robust set of rules of the game. Mill proposed that agent-type was the key variable upon which any explanation must draw: “[I]f we ask ourselves on what causes and conditions good government ... depends, we find that the principal of them, the one which transcends all others, is the qualities of the human beings composing the society over which the government is exercised” (207).

The young John Mill (1969 [1833], [1838]) had repeatedly attacked the purported universality that was claimed for the Benthamite theory of government (at least as represented by his father’s *Essay on Government*), faulting the theory for its apparent proclivity to treat Malaysian native and English gentleman as the very same creature (agent-type), having equal need for the very same set of political institutions at all times and places. For all that, however, James Mill’s own view was actually far closer to that of his son (1861) than the younger Mill had been willing to admit.⁶⁷

⁶⁶ “[The] good qualities [of the populace] supply the moving force which works the [political] machinery”. Furthermore, the constitutional machinery “has to be worked by men, and even by ordinary men” (Mill 1998 [1861], 207).

⁶⁷ See James Mill’s *Essay on Education* (1992, 139-194): “[I]t is education wholly which constitutes the remarkable difference between the Turk and the Englishman, and even that still more between the most cultivated European and the wildest savage. Whatever is made of any *class* of men, we may then be sure is possible to be made of the whole human race” (Mill 1992, 147). On the vital importance of the assumption of human homogeneity in classical political economy, see Levy (2001).

Robust Institutions: Romance by the Backdoor?

James M. Buchanan has rather aptly characterized public choice theory as the study of politics without romance: public choice theory models political agents as no less motivated by self-interest than are the rest of us (see, e.g., Buchanan 1979, 211). Levy (2002) proposes that we ask the following of any suggested policy change: what assumption (or set of assumptions) must characterize the realized state of the world if the suggested policy [**Z**] is to actually maximize social welfare? Letting **Z** denote market socialism (Lange 1964 [1938]; Lerner 1944), **Z** will maximize social welfare only if our implicit assumption that β (where β stands for public-spiritedness) characterizes the real-world economic planners is accurate. And what if our supposition (or leap of faith, take your pick) of β is, however, grossly inaccurate? At this juncture, the “robustness problem” (Levy 2002) rears its head: “What is the consequence of this failure [of β]? A robust institution is one which puts a bound on the loss from such failure. A nonrobust institution does not have such a bound” (Levy 2002, 135). If our assumption of β is wrong, **Z** (assuming we prove foolish enough to actually implement market socialism) will have disastrous consequences for human well-being. Market socialism [**Z**] is simply not robust in the face of any major deviation from β (see, e.g., Knight 1982 [1940]; Levy 1990; Shleifer and Vishny 1992). Constitutional political economists (e.g., Brennan and Buchanan 2000 [1985]; Brennan and Hamlin 1995; Levy 2002) therefore favor robust political institutions [**RI**] (or sets of rules of the game) over non-robust political institutions [**NRI**].

What would a robust institution actually look like? I propose that we classify particular types of robust institution according to the following taxonomy: those, which are contingently robust [**CRI**], and those, which are non-contingently robust [**NCRI**]. The Stanley Kubrick movie ‘Dr. Strangelove’ provides a useful illustration of a non-contingently robust institution (or rule): a doomsday machine that is programmed to launch an immediate retaliatory attack against a

nuclear strike by the Soviet Union upon the United States (see Friedman 1996, 148-150). The machine is programmed to launch a retaliatory strike irrespective of anyone's wishes post the Soviet strike. The design of the machine serves to eliminate any potential problem of time-inconsistent policy. I cannot imagine any such type of non-contingently robust institution, however, without having recourse to science fiction or some other fantasy genre.

A contingently robust institution [**CRI**] (e.g., constitutional rules constraining the exercise of government power) does not (at least of its own accord) place any limit on the losses resulting from any deviation from the idealized assumptions of a model. Once put into practice a contingently robust set of constitutional rules of the game will serve to limit any potential losses only in conjunction with some other agent or institutional form: the ultimate enforcer of the constitutional contract perhaps (Tullock 1987; 1993).

Constitutional political economy has to date paid far too little attention to the question of constitutional enforcement: too readily assuming that constitutional constraints are non-contingently robust.⁹⁸ This surely is a failing on the part of constitutional political economists: the only realistic choice that we have is that between different types of contingently robust sets of rules of the game. Agent-type (the ultimate enforcer of the rules of the game) and the constitutional constraints are complements rather than substitutes. Constitutional political economy, however, has traditionally (at least *prima facie*) suggested otherwise.

⁹⁸ "We need not predict that each child will fall off the cliff to justify the installation of railings" (Brennan and Buchanan 2000 [1980], 240, italics added). "We may illustrate by analogy. "It is costly to build a fence or to purchase a chain. It is possible to prove that the no-fence, no-chain solution is more efficient than either, *provided* that we model the behavior of our dog in such a way that respects the boundaries of our property" ... [Is the example] really very different from that procedure which argues that tax structure *X* is more "efficient" than tax structure *Y* provided that we model the behavior of government in such a way that it seeks only to further efficiency in revenue collection?" (Brennan and Buchanan 2000 [1980], 225). *Fence* and *chain*, however, are most emphatically examples of a non-contingently robust 'enforcement technology'. Moreover, a dog is the classic example (Buchanan 1979, 94) of Buchanan's *natural animal* (an animal that responds passively to constraints). Man, by contrast, is most emphatically an *artifactual* creature. See Buchanan's highly important essay *Natural and Artifactual Man* (1979, 93-112).

A Paradox of Constitutional Enforcement?

Sir Dennis Robertson made the characteristically whimsical (and indeed, highly insightful) suggestion that the economist sound a warning bark upon hearing of any policy proposal that depends upon the prevalence of 'love' (or general benevolence) for its potential success. I wonder what Sir Dennis would have made of Mill's *Essay*, or would think of constitutional political economy? Brennan and Buchanan (2000 [1980], [1985]) reiterate Robertson's suggestion: arguing that any posited ubiquity of 'love,' at the lower level of in-period politics, does indeed, provide far too fragile a supposition to seriously entertain when choosing among sets of rules at the higher or 'constitutional' level. Assume that one readily accepts (as I largely do) Brennan and Buchanan's worst-case logic. Certain questions immediately come to mind: Why are the constitutional rules of the game binding? Why are the relevant political institutions characterized by robustness? Constitutional political economy must take such questions seriously. One cannot invoke the willingness of a public-spirited populace to provide the public good of constitutional enforcement and still remain in good standing as a worst-case thinker. To invoke universal love as a potential solution to the problem of constitutional enforcement surely merits at minimum a warning bark from Sir Dennis (if not a painful nip on the ankle).

The relevance of the Mill-Macaulay debate to political economy?

We propose that a theorist be designated a best-case thinker when their model presupposes (usually implicitly and without bringing this tacit supposition to the attention of the reader) some particular idealized state of the world (see Levy 2002). The model is designated as fragile if the welfare implications of the model associated with any particular idealized state of the world fail to similarly characterize (within a reasonable bound) the welfare implications of the

same model assuming a deviation (slight or otherwise) from the posited idealized state of the world.

Following the literature on institutional robustness (Levy 2001, 2002; Brennan and Hamlin 1995, 2000) we stipulate that an institution (or set of rules of the game) be considered robust or fragile (non-robust) in accordance with the degree to which the envisaged welfare properties of the relevant institution necessitate the empirical realization of the certain idealized assumptions. For example, Soviet-style economic planning only functions tolerably well if we make the highly heroic assumption that the economic planners are not self-interested (Levy 1990; Shleifer and Vishny 1992). If the welfare properties of model **X** obtain both for state of the world 1 and state of the world 2 (let 1 represent benevolent planners and let 2 represent non-benevolent planners), then we say that **X** is a robust institution. If the welfare properties of the model given 2 are far less than those properties were under 1 we designate **X** as a fragile, or non-robust institution. Models of market socialism that posit a high level of welfare (for the general populace, and not just for the planners) are thus highly fragile in the wake of any deviation from the assumption of public-spirited planners. We shall return to this theme in the next chapter.

In the case of James Mill's *Essay on Government* (1820), Mill maintained that representative institutions would provide a set of robust institutions. Macaulay, by contrast, argued that representative institutions were fragile. Indeed, Macaulay argued that such fragility was surely implied by the very worst-case axioms on which Mill purported to argue the case for the desirability of such institutions. Mill posited the worst-case axiom that government (if unchecked by constitutional mechanisms) was akin to a slave driver (Mill 1978 [1820], 67). Mill argued that the potential for the slave driver equilibrium could be suitably tempered by electoral mechanisms that made the would-be slave driver wholly answerable to those who (given the absence of such electoral mechanisms) he would have otherwise enslaved. Macaulay suggested

that Mill made his model work by abandoning his worst-case axioms as it suited his purpose, or alternatively, by invoking some type of motivational heterogeneity (one surely entailing the abandonment of the premise of Mill's *Essay*). Mill's best-case sleight of hand in the *Essay* was one holding the electorate to be benevolent towards their fellow men (and women). Macaulay argued that motivational homogeneity (the argument on which Mill's *Essay* was premised) implied either the generality of the slave-driver equilibrium, or – so Macaulay maintained – the equal possibility of there being an enlightened and benevolent monarch on the throne.

Why should any of this matter for constitutional political economy in particular, or for political economy in general? Surely the Mill-Macaulay debate is aptly left to the historians of the period? The Mill-Macaulay debate is of importance because best-case moves are ubiquitous in political economy. Examples proliferate, even in the public choice literature, a literature that ostensibly prides itself as being shorn of all delusions of romance when studying politics. Where are the best-case moves in constitutional political economy? I shall discuss such maneuvering in greater detail in chapter four of this thesis, but for now, I simply point to the Tullock paradox: the assumption made by constitutional political economists that the enforcement agent restricts itself to the delegated task of enforcing the rules of the game selected behind the veil of uncertainty (best-case move 1). A possible rejoinder⁹⁹ to this charge of paradox would be to say that judges' monitor and constrain the enforcement agent (best-case move 2), the judiciary being in turn monitored and disciplined by mechanism *X* (best-case move 3). Mechanism *X*, is, of course, likewise constrained by mechanism *Y* and so on. At each stage of the argument we resort to an additional best-case move, one that at best just pushes the original challenge back one step. Such best-case maneuvering is not necessarily a bad thing, provided that we realize we are engaging in such (and candidly admit to it). The alternative to best-case thinking is perhaps that of preaching

⁹⁹ See, however, Tullock (1971).

a counsel of despair, although as Frank Knight once quipped: if the situation is hopeless then it is surely optimal and vice versa (at least within the restricted grammar of economic theory).

**Frank Knight, Worst-case theorizing, and Economic Planning:
Socialism as Monopoly Politics**

Introduction

Peter Boettke and Karen Vaughn (2002, 155-176) have recently drawn attention to the important differences characterizing the respective cases made against socialism by Frank H. Knight, on the one hand, and by Ludwig von Mises and Friedrich Hayek on the other. While Mises and Hayek asserted that the impossibility of economic calculation in the absence of a market for factor inputs was the most important difficulty that would plague any attempt at genuine socialist economic planning (see Steele 1992), Knight remained somewhat agnostic.¹ Indeed, as Boettke and Vaughn (2002) have correctly pointed out, Knight thought that pure economic theory had very little – if indeed anything – to say regarding the likely problems of socialist planning, instead suggesting that the major problems of socialism were most likely to all prove political ones. Whilst I have no quarrel whatsoever with Boettke and Vaughn’s cogent defense of the original Misesian claim that economic calculation under socialism is an impossibility (see e.g., Lavoie 1985, 48-77; Steele 1992, 1-24), I suggest that Boettke and Vaughn inadequately appreciate the subtle worst-case logic that informed Knight’s political critique of socialism. Indeed, the political critique of socialism provided by Knight is somewhat rather more akin to the critique of socialism that F. A. Hayek provided in the *Road to Serfdom* ([1986] 1944) than Boettke and Vaughn suggest.

¹ See Knight (1938c, 867).

Boettke and Vaughn (2002, 156) raise a highly intriguing and important question in their article, recognizing that there is indeed a “real puzzle” as to “why economists ever believed that socialism as an economic system could fulfill all the promises made on its behalf”. While the failure of economists to adequately appreciate the Mises-Hayek critique of socialism surely provides part of the answer to Boettke and Vaughn’s question (see Lavoie 1985), I would conjecture that the pervasiveness of best-case thinking (roughly akin to the benevolent despot assumption so despised by modern public choice theory²) amongst the economics profession during the first half of the 20th century goes a rather long way in explaining the longevity of proposals for socialist planning.³ Indeed, as we shall see, it was Frank H. Knight, rather than Mises and Hayek, who explicitly recognized the vital importance of best-case thinking to the case that economists (along with other social theorists) made for socialism.⁴

Best-case Thinking in the Socialist Calculation Debate

Nowhere in the history of political economy was best-case thinking of greater influence than during the socialist calculation debate of the 1930’s. Indeed, the supposition that the state,

² “[T]he benevolent despot model of politics and government has promoted and sustained monumental confusion in social science, and social philosophy more generally” (Brennan and Buchanan [1985] 2000, 55). Socialists “regularly assume that there will be a revolution in men’s characters as soon as they find themselves working for the community” (Knight 1938a, 244).

³ Boettke and Vaughn suggest “even among economists ... the intellectual dominance of socialist thought displaced the presumptions of nineteenth century liberalism” (2002, 156). Why did such a displacement occur? I conjecture that the very important motivational caveats which had played so vital a role in the analysis of socialism provided by, e.g., J. S. Mill, were wholly ignored by later economists. On Mill’s analysis of socialism, see Hollander (1985, 770-824).

⁴ “Of course, the revolutionist assumes that “human nature” will be completely different after the inauguration of his scheme” (Knight [1941] 1982, 209). Why economists have habitually found best-case thinking so attractive is beyond the scope of this paper. Best-case thinking is, however, at least as old as Plato’s philosopher king, and was particularly influential during the Progressive era. I am indebted to Ross Emmett for these points. David M. Levy wonders with regard to the Progressive era whether only God or God’s agent can adequately engineer the requisite transformation of human nature. See Peart and Levy (2003) for a discussion of eugenics as instance of this remaking by the god-like.

“conceived in the abstract as a benevolent and all-powerful agency – essentially as God rather than realistically as politicians – could order economic affairs rightly without generating new evils or incurring serious social costs” (Knight [1940] 1982, 159) characterizes best-case theorizing (particularly as regards the feasibility of socialism) throughout the history of political economy (see Levy 2002). Frank H. Knight rather pungently pinpoints the major flaw in best-case theorizing:

It can in fact be shown that *if* human beings conformed to appropriate [best-case] specifications, and government likewise – operated by the same or similar men, or by a special race of men, or by angels or Gods – the ends could be even better accomplished under a system of centralized control, i.e., socialism or collectivism ... However, there are very cogent reasons for believing that with men at all as they are – and with governments as they will be, if staffed by such men – neither socialism nor anarchism in any approximation to the ideal pattern is a practical possibility (Knight [1941] 1982, 209).

Knight is prepared to concede – for the sake of argument – that under certain ideal conditions (a posited lack of self-interest on the part of the planners) socialist planning is superior to markets. What, however, if those ideal conditions fail? This is where worst-case thinking enters the fray.⁵ Worst-case theorizing focuses our attention on the performance of institutions when the ideal conditions posited by the best-case theorist fail to hold (e.g., Brennan and Buchanan 1983, [1985] 2000, 53-73; Levy 2002). Worst-case thinking has a long and distinguished history in political economy (e.g., Hume 1985, 42-43; Mandeville 1988, 335).⁶ Despite the relevance of worst-case theorizing to the planning versus markets debate, best-case

⁵ “If we are to believe that the system [socialist planning] could be either democratic or free in any sense, we must believe that the ... central authority would really act as the *responsible agent of the people as a whole*” (Knight 1938a, 250, italics added).

⁶ See e.g., Toma and Toma (1984), Levy (2002). Levy (2002) makes the link between Brennan and Buchanan’s (1983, 2000) worst-case philosophy of constitutional political economy and J.W. Tukey’s worst-case philosophy of mathematical statistics. The classic statement of worst-case thinking is provided by Hume ([1741] 1985, 42-43): “Political writers have established it as a maxim, that, in contriving any system of government, and fixing the several checks and controuls of the constitution, every man ought to be supposed a *knave*, and to have no other end, in all his actions, than private interest.”

theorizing was so pervasive among economists during the socialist calculation debate that both Mises and Hayek – the leading representatives of the anti-central planning side of the debate – have been charged with neglecting to seriously challenge the characteristic best-case assumption made by the market socialist writers: that of public-spirited economic planners (e.g., Buchanan [1969] 1999, 88; Levy 1990). Indeed, James M. Buchanan, although well aware of the all-too genuine difficulties in economic calculation that would surely plague any attempt to implement socialist planning,⁷ has provocatively suggested that the “more significant criticism of socialist economic organization lies in the difficulties of choice making” (1999, 87-88). Buchanan remains virtually unique among those who have written on the socialist calculation debate in maintaining that the debate ought to have placed a far greater emphasis upon motivational questions (see Steele 1992, 414). Indeed, Buchanan has long remained highly skeptical towards the efficiency claims made for market socialist models (e.g., Lange [1938] 1964; Lerner 1944; Bardhan and Roemer 1992) on just such motivational grounds, asking with regard to the stylized assumptions of the Lange-Lerner model why it is that the “socialist [enterprise] managers would behave according to the idealized rules”⁸ (Buchanan 1989, 21)⁸ Moreover, Buchanan has made a justly famous career out of asking exactly this very same question regarding any suggested institutional reform or policy change: Why is it incentive-compatible?⁹

⁷ See e.g., Roberts (1990), Lavoie (1985), Boettke (1990), Steele (1992), Vaughn (1980).

⁸ “The romance of socialism ... is dependent both on an idealized politics and a set of impossible behavioral presuppositions” (Buchanan 1994, 7).

⁹ Brennan and Buchanan (1983, [1985] 2000).

Frank Knight's worst-case insight: Socialism as Monopoly Politics

Frank H. Knight, of course, was James M. Buchanan's teacher at the University of Chicago in the late 1940's.¹⁰ Throughout the 1930's and 1940's, Knight had repeatedly warned that socialist planning would replace the market economy (competitive or otherwise) with one giant de facto monopoly (Knight [1940] 1982, 154-194).¹¹ Knight suggested that socialist planners would maximize their own welfare, even if such satisfaction were to come at the cost of welfare losses throughout the rest of the economy. The modern public choice literature on the economics of socialism (e.g., Levy 1990; Shleifer and Vishny 1992; Boettke and Anderson 1997) reiterates Knight's worst-case claim: Economic planners of the self-interested variety will systematically generate shortages, allowing themselves to extract bribes or other favors (all akin to artificial scarcity rents) from hapless consumers. Rather than allocating resources to maximize social welfare (the traditional assumption of market socialist models), socialist planners will allocate resources such as to maximize the value of their own scarcity rents (Shleifer and Vishny 1992; Boettke and Anderson 1997). This worst-case argument is simply the application of Gordon Tullock's (1967) canonical rent-seeking model to the economics of socialist planning: as such, the argument ought to strike the modern economist as both intuitively appealing and obvious.¹²

¹⁰ "[I]t is as if in rereading Knight I am retracing the sources of my own thoughts, which themselves have somehow emerged without conscious recognition that they are derived from him" (Buchanan 1982, x.)

¹¹ "[C]entral planning, ... obviously means ... in economic terms, a universal monopoly" (Knight [1944] 1982, 431). "To substitute competitive politics for competitive business is to jump out of the frying pan into the fire" (Knight [1934] 1982, 39). "I am personally rather inclined to the belief that to jump from competitive business to the competitive politics of democracy (and I know of no other kind except the *monopoly politics of dictatorship*) is to jump from the frying pan into the fire" (Knight 1935, 205, italics added).

¹² "The first principle of Economics is that every agent is actuated only by self-interest" (Edgeworth [1881] 1967, 16). Buchanan (1991, 17) pungently asks: "Why did economists, who model

Although Frank Knight had repeatedly hinted at the implicit worst-case logic underlying the Levy-Shleifer-Vishny (L-S-V) model in the 1930's and 1940's, thinking that worst-case logic obvious,¹³ he did not, however, view his worst-case insight as having any relevance to the likely outcome of the socialist calculation debate. Indeed, for Knight, the discussion of socialist planning that was provided by economists necessarily precluded "treatment of the essential issues" (Knight 1938a, 242). Economic theory – the pure logic of choice – was, in particular, somewhat ill equipped to solve the "political problems of how to get men of the utmost possible competence and good will into actual charge of the economic order" (Knight 1938a, 243).¹⁴ That Knight's suggestion that we pay a modicum of attention to the likely motivations of the socialist planners proved shocking to economists' sensibilities at the time, should hardly surprise us. Knight was, after all, writing prior to the public choice revolution in economics.¹⁵ We ought, however, to be surprised by the readiness with which all of the leading participants in the socialist calculation debate were willing to accept Abba Lerner's stricture (1937, 267) that "sociological questions" regarding incentives (e.g., the likely

man as *homo economicus* in analysing markets, fail to recognise that incentives remain relevant in all choice settings?"

¹³ Knight thought the basic argument of his 1940 paper to "lie entirely within the field of the obvious, not to say the trite" ([1940] 1982, 154).

¹⁴ This may explain why Knight's insight took some 60 plus years to reappear in the literature.

¹⁵ "It seems extremely difficult for anyone to adopt a socialist position and at the same time be familiar with and accept the analysis of public choice. Here I use *socialist* in the sense that this term was employed in the 1930's, when Lange, Lerner, and others convinced so many of their colleagues that socialism could *work*. No more than a smattering of sophistication in public choice (or in ordinary common sense, for that matter) is required to suggest the absurdity in that position" (Buchanan 1979, 272).

incentive-compatibility of alternative sets of rules of the game) were irrelevant to, not only economics in general, but the socialist calculation debate in particular.¹⁶

The longevity of proposals for socialist planning was (and is), I suggest, a reflection of the eagerness with which economists were (and are) willing to happily embrace the assumption that economic planners were (and are) public-spirited.¹⁷ The public choice literature on market socialism simply relaxes the traditional assumption of benevolent – or public-spirited – planners, thereby throwing into doubt the efficiency claims made for traditional market socialist models. During the actual socialist calculation debate, however, to have dared relax the assumption of public-spirited planners, or, like James M. Buchanan, to have suggested that the set of rules (Lange 1964, 92) the planning authority sought to impose on socialist enterprise managers to ensure “*efficiency* in carrying out the plan” (Lange 1964, 92) might prove incentive-incompatible (Buchanan 1989, 21) would have been to invite the open scorn of colleagues, along with charges that one was engaging in dubious psychological speculation rather than economic analysis (e.g., Lerner 1937, 267; Durbin 1936, 678-679, 1945, 359). It is indeed remarkable to think – from the vantage point of some 60 plus years later – that the most obvious of questions that one might ask regarding market socialism, that concerning the likely incentive-compatibility (or otherwise) of socialist rules of the game, was once viewed by economists as having little relevance to political economy.¹⁸

¹⁶ Dickinson (1933, 240, 245, 249), Durbin (1936, 678-679), Lange ([1938] 1964, 109), Hayek (1935, 2-3), Robbins (1935, 148, 156, 1937, 209).

¹⁷ See Shleifer and Vishny (1994, 165).

¹⁸ “[Mr.] Durbin refuses to discuss these matters [incentives] in the article ... he is well justified in refusing to accept such criticisms of socialism as depend on these considerations” (Lerner 1937, 267). Contrast Lerner’s remark with the judgment of Lazear: “Incentives are the essence of economics” (Lazear 1989, 152). The switch from ‘incentives are not economics’ to ‘incentives are economics’ is quite remarkable. In many ways, political economy has returned to the emphasis placed by classical political economy on the importance of incentive-compatible rules and institutions (see e.g., Bentham [1830] 1984, 55, 174).

The L-S-V model of socialism explains the pervasive shortages characteristic of Soviet-type economies by reference to the incentives of the economic planners. Any planner (or enterprise manager) has the incentive to systematically generate artificial shortages. The L-S-V model is simply the application of the canonical textbook model of monopoly, plus basic public choice logic, to socialist planning. The planner, in common with any other rational and self-interested chooser will choose the quantity of output that maximizes bribe income. For each unit sold to consumers, the planner has to deliver P (the official price of the good set by the state) to the state treasury. The marginal cost curve that is relevant to the planner's maximization problem is horizontal at P . The planner will select quantity to equate marginal revenue (in bribe income) to marginal cost (equal to P). At this privately optimal – or at least optimal from the vantage point of the planner if not from that of society – quantity, P is below the market clearing price: we have an artificially engineered shortage. The marginal consumer is just willing to pay a total bribe equal to their reservation price (derived from the inverse demand curve) minus P . The residual equal to $P^B Q - PQ$ will accrue to the planner as a pure rent.¹⁹

The planner as a rational self-interested chooser – motivated by the goal of maximizing his personal rents, rather than that of social welfare maximization – will create the usual deadweight loss associated with monopoly. A public-spirited planner, by contrast, would select the output quantity that maximizes social welfare, even though the personal opportunity cost of making such a choice would equal the artificial scarcity rents that were foregone.

That Frank H. Knight was well aware of the worst-case logic implicit in the L-S-V model prior to world war two is clear:

Socialists themselves generally assume that there will be very much more monopoly under socialism, even in particular industries, to say nothing of the fact that all production would be in the nature of the case to be one gigantic monopoly in the hands

¹⁹ Where P^B equals reservation price.

of the government – but of course all are *assumed to be managed in the public interest* (Knight [1940] 1982, 170-171, italics added).

Although Knight had recognized the implicit logic of the L-S-V model, he did not think the insight of his 1940 article – that of socialism as monopoly politics – had anything to do with economic theory per se. Indeed, as Boettke and Vaughn (2002) have documented, Knight thought that economic theory was really little more than the axioms of the pure logic of choice. Thus, Knight thought that economic theory had little – if anything – to say regarding the potential pitfalls of socialist planning (see Boettke and Vaughn 2002)²⁰: “If we abandon considerations of theoretical reasoning in terms of the abstract logic of choice in favor of empirical considerations of sociology and politics ... all character of apriori certainty in ... [our] reasoning is lost” (Knight 1936, 257).²¹ Although the L-S-V model makes creative use of the textbook model of monopoly, Knight, at least while analyzing socialism from the perspective of an economic theorist takes exactly the opposite tack, stating, “in order to predict anything [about the likely welfare properties of socialist planning] ... [one] must first eliminate by assumption the possibility that the government would exploit its position as a monopolist of innumerable essentials of economic life and [fail to] administer its property resources in accordance with the principle of maximum social economy” (Knight 1936, 260).²² Moreover, Knight, once again writing purely as an economist, quite readily accepted the characteristic

²⁰ “The economist, as economist, has nothing to say about any of these questions” (Knight [1940] 1982, 160). Also see Knight (1936, 268).

²¹ “[T]he problems of collectivism are not problems of economic theory, but political problems ... the economic theorist, as such, ... has little or nothing to say about them” (Knight 1936, 255).

²² “The collectivist economy would necessarily economize resources in the use of satisfying wants; and this necessarily means that it would strive, consciously or unconsciously, to allocate its resources among the different want-satisfying uses in accord with the principles of marginalism” (Knight 1936, 255).

market socialist assumption that the employees of the socialist planning bureaucracy would prove “competent and public-spirited” (Knight 1936, 259).²³

Despite having recognized the logic of the L-S-V argument in the 1930’s and 1940’s, Knight chose to put the insight where other economists (for reasons akin to those Knight gave regarding the exact nature of economic theory)²⁴ were somewhat unlikely to take heed: namely in review essays for the *Journal of Political Economy* and a 1940 paper in *Ethics*; indeed, that Knight would accept – or at least while writing as pure economist would prove willing to accept – the assumption of public-spirited planners (e.g., Knight 1936, 259) is all the more remarkable in light of claim that the argument provided in the 1940 paper was “written from the standpoint of economic theory” (Knight [1940] 1982, 154). In that very same paper, however, Knight disavows his earlier claim, stating, “[e]conomic theory, as such, involves no disproof or rejection of socialism. Rather the contrary ... Theoretical analysis [of the market economy] ... reveals many indisputable weaknesses [market failures] which could, *in theory*, be remedied or avoided by an all-powerful, wise and benevolent political authority” (Knight [1940] 1982, 160). For Knight’s critique of socialism, or indeed, for his critique of any other proposal for large-scale social reform, it is the perennial caveat – “*in theory*” – that provides the key to appreciating Knight’s worst-case thinking. Indeed, Knight argues that the main “problem of

²³ This raises an interesting question. Are the Austrian and Public Choice critiques of socialism complements or substitutes? See Cowen (1995, 244): “The incentives argument is not fully compatible with the calculation argument. The incentives argument implies that managers are in fact very good at calculating the proper price from their point of view. Socialist prices are nearly always too low and rarely too high. If calculation were truly a problem, we would expect to see many prices that are too high”. Also see Levy (1990).

²⁴ It is rather intriguing as to why all relevant parties in the calculation debate sign-off on the view that incentives are ‘sociology’, and hence, that economists have little to say on the matter. For Knight, economics cannot resolve the markets-planning debate alone, but is simply one among various inputs into thinking seriously about the problems of planning: “Thus any solution of the problem involves use of facts and principles from the two social sciences of economics and politics – and beyond these of the more fundamental disciplines of history, sociology, etc..” (Knight [1940] 1982, 155).

socialism is the practical one already suggested. It has to do first, with the possibility, and probability of such an authority, or some approximation to it, being created on earth and among human beings, by political process” (Knight [1940] 1982, 160). Thus, although an agnostic regarding the verisimilitude of the Misesian claim that economic calculation under socialism was impossible (see Steele 1992, 101-102), Knight rejected socialist planning on worst-case grounds.²⁵

In light of Knight’s views regarding the nature of economic theory, we can readily infer why Knight thought that a model of socialist failure was not possible,²⁶ or at least, not possible within the realm of technical economic theory.²⁷ Knight viewed economic theory per se as the set of tautologies (a set of highly important and enlightening tautologies) that were descriptive of the marginal conditions typifying an optimal pattern of resource allocation (e.g., Knight [1939] 1982, 68-69). For Knight, economic theory – always understood as the pure logic of choice – provided a set of apriori propositions that were necessarily true at all times and places.²⁸ Any assumed fixity of ‘human nature’ (e.g., Knight [1921] 1957, 335), however, while

²⁵ “There is another aspect of socialism which is patent enough to any person of good sense (including economists) but which strangely enough is so generally overlooked that it may be mentioned. This is, *that in promoting socialism its devotees are seeking political power for themselves*” (Knight [1940] 1982, 162, italics added). “All political opposition to this programme [Marxism] is assumed as a matter of course to derive from the bourgeois class itself, either directly or through paid agents and dupes. (Non-Marxist economists are allowed to hover more or less between these two classifications, paid agent and dupe.) ... [T]he allegation of selfish interest which is glibly pinned on the opposition applies even more obviously to the promoters of the class war themselves. They are *assumed to be free from any taint of self-interest!*” (Knight [1939] 1982, 117-118, italics added).

²⁶ “One thing economic analysis can do: it can show the character of the economic problems with which socialism proposes to deal” (Knight [1940] 1982, 161).

²⁷ Of course, Knight’s worst-case intuition had all the ingredients of a model (see e.g., Levy 1990; Shleifer and Vishny 1992).

²⁸ “The more general principles of economic theory would be valid under any conditions possible on earth, regardless of the form of society as a whole ... In any possible human life limited resources must be utilized to realize a plurality of ends and must be apportioned among different modes of use. ... That is, the general character of economic theory is not dependent on social forms or institutions or on any historical accidents” (Knight [1940] 1982, 163-164).

somewhat akin to a “relatively absolute absolute” (to invoke a favorite Knightian phrase).²⁹ necessarily lacked the apriori certainty characterizing the pure logic of choice.³⁰ Whilst Knight treated the axioms of the logic of choice as of universal validity (e.g., Knight [1940] 1982, 163-164), he was insistent as regards the highly tentative nature of the predictive hypotheses that were generated by the marriage of the analytical grammar of economic theory to specific motivational assumptions (e.g., Knight [1940] 1982, 157).³¹ To illustrate the point, consider Knight’s remarks on ownership and managerial efficiency:

The contention that the owning entrepreneur, individually subject to loss or the recipient of gain, according to the success of the enterprise, can be replaced by the government, *assumed* to have no such interest without loss of managerial efficiency, surely rests more on the will to believe than it does on inference from experience. But this is not impossible: it *might* work out in that way! It is a political or psychological question, not one of economics” (Knight [1940] 1982, 172).

Knight, whilst willing to accept the potential malleability of agent-type (see e.g., Knight [1921] 1957, 359, [1939] 1982, 84) – recognizing that any posited fixity of agent-type was subject to critical scrutiny – was, however, clearly averse to any plan for wholesale institutional change (e.g., the replacement of markets with socialist planning), the success of which necessitated that agent-type underwent a wholesale transformation (e.g., from *homo economicus* to *non-homo*

²⁹ See Buchanan (1992, 78-79).

³⁰ Knight suggested that socialists started from an “explicit premise which eliminates in advance all rational discussion. To assume that the establishment of socialism will change “human nature” is to destroy all possibility of predicting the future from the past, and one can establish any sort of subsequent social life desired or fancied by simply asserting the appropriate change in human nature” (Knight 1938c, 868).

³¹ “Only within fairly narrow limits, and subject to *explicit hypothetical postulates*, can economic science make any pronouncement as to conditions as they would exist under socialism” (Knight [1940] 1982, 160).

economicus), where in Knight's view, any evidence that the requisite transformation had taken place was non-existent (e.g., Knight 1938a, 244).³²

Economic Planners as Benevolent-Despots?

Frank Knight was clearly a skeptic as regards the best-case thinking engaged in by so many of his fellow economists, recognizing throughout his writings on socialism the important role that the best-case assumption of economic planner as benevolent-despot played in the market socialist literature. Knight, in a 1938 review of A. C. Pigou's *Socialism versus Capitalism* (1937), gently chided Pigou for unduly neglecting the potential agent-type of the planners: "[He] assumes that under socialism control will be effectively concentrated in the hands of some central authority with the utmost competence and *good will* for promoting ... economic efficiency ... There is no question of the character of the controllers!" (Knight 1938a, 242)³³

Knight's 1946 review of Barbara Wootton's *Freedom Under Planning* (1945) argued in a similar vein. Indeed, while Knight thought Wootton's rejection of the textbook ideal of consumer sovereignty rather apposite and merit-worthy, he gently scolded her for similarly idealizing the equally naïve "postulates as to wise and benevolent state paternalism, that

³² For Knight, "political opinion is a matter of wish-thinking and romanticism in overwhelming variety" (Knight [1940] 1982, 155). A characteristic example of this romanticism is the view, "expressed on every hand by the "best minds," in the unlimited possibility of changing human nature through passing laws or remodeling the political constitution" (Knight [1940] 1982, 157).

³³ Pigou failed to compensate for this earlier neglect when reviewing Hayek's *Road to Serfdom* in the *Economic Journal*: "[W]hen the items which enter into private calculations and those which effect social welfare differ markedly, it [the government] must intervene directly" (Pigou 1944, 217). Pigou's review reveals no awareness of the possibility for government failure. Knight's remark that "what a government 'might do' is limited chiefly by the powers of creative fancy in the person drawing the picture" (Knight 1938c, 868) is particularly apposite as regards the market failure literature of the late 1940's and early 1950's.

underlie the arguments for [economic] planning” (Knight 1946, 452).³⁴ suggesting that support for socialist planning largely arose from the “faith” (453) that the planning bureaucracy would carry out its work in a “tolerably competent and disinterested way” (Knight 1946, 453).

Best-case Thinking: short-circuiting the worst-case logic of Socialism?

Why do I place such importance on the two pages written by James M. Buchanan ([1969] 1999) on the socialist calculation debate? Although economists in the Austrian tradition (e.g., Boettke 1990; Lavoie 1985; Vaughn 1980) have praised the subjectivist theory of costs that Buchanan provided in *Cost and Choice* ([1969] 1999), they have yet to pay any real attention to his remark that the “socialist bureaucrat must be *non-Homo Economicus* in the purest sense” (Buchanan [1969] 1999, 88). The Austrian scholarly accounts of the socialist calculation debate (e.g., Boettke 1998, 2000; Lavoie 1985; Steele 1992; Vaughn 1980) focus almost exclusively on the purely technical problems of socialist planning: the impossibility of economic calculation under socialism; indeed, just like Mises,³⁵ the Austrian accounts hold socialist planning impossible irrespective of the particular agent-type that we might choose to

³⁴ Knight urges Wooton to take “notice of the amount of economic intelligence shown by the most enlightened democratic governments in the economic measures they have actually taken in recent history” (Knight 1946, 453). “[T]he situation is summed up in the adage that free traders win the debates but protectionists win the elections” (Knight 1982 [1944], 394). In a 1935 review of Barbara Wooton’s *Plan or No Plan* (1935), Knight draws attention to a passage where Wooton expresses concern that economic planning will fall foul of a “centrifugal tendency” that potentially afflicts “every specialized society”. Knight explains (812) that Wooton is referring to the “danger that special interest groups may organize for the exercise of monopoly power”. This “political” issue, states Knight, is one in comparison with which, the issues that are narrowly “economic ... pale into triviality” (Knight 1935, 812).

³⁵ “The impracticability of Socialism is the result of intellectual, not moral, incapacity. Even angels, if they were endowed only with human reason, could not form a socialistic community. *If a socialist community were capable of economic calculation, it could be set up without any change in men’s moral character*” (Mises 1981, 407, italics added). “Mises’s argument against the practical feasibility of what he calls “socialism” does not hinge upon questions of motivation, but rather claims that, with the best will in the world, humans *are not able* to operate a society on ‘socialist’ lines, because modern industry cannot be successfully guided or administered without the information provided by market prices of factors of production. Mises claims that even where there’s a will, there’s no way” (Steele 1992, 2).

ascribe to the hypothetical socialist planners. Following Buchanan's judgment that the calculation debate relatively overemphasized the "difficulties in economic calculation that prospective socialist decision makers would face" (1999, 87), we shall focus on questions of planner agent-type.

The modern public choice critique of socialist planning (Levy 1990; Shleifer and Vishny 1992) takes agent-type as a given: man is *homo economicus*. Whereas Mises ([1932] 1981) argues that efficient socialist planning is possible (given any agent-type) only if an adequate rebuttal to the economic calculation argument is forthcoming, the public choice critique of socialist planning suggests that, irrespective of the possibility – or otherwise – of socialist economic calculation, socialist planners – given their current agent-type – have very little interest in socially efficient planning. Given agent-type (*homo economicus*), whether planners can engage in successful economic calculation or not is largely immaterial: socialist planners have no incentive to make socially efficient allocative decisions. The fixity of 'human nature' (agent-type) posited by public choice theory appears *prima facie* of greater potency as an argument against socialist planning than does the Austrian economic calculation argument.⁵⁶

Consider Buchanan's rather insightful remark that the only if the economic planners can be trained to make allocative decisions that "do not embody the opportunity costs that they, individually and personally, confront" ([1969] 1999, 88) will socialism "generate efficiency in results" (88). Moral education of the planner serves to mitigate the inefficiencies that are otherwise resultant upon any divergence between the private and social costs of allocative

⁵⁶ "[T]heory and current experience warrant the gravest doubts as to whether the human group in command of a collectivist economy would make any serious effort to find for socio-economic problems solutions of the form taken for granted by Professor Pigou and other liberals" (Knight 1938a, 243). In a 1938 review of Mises's *Socialism: An Economic and Sociological Analysis*, Knight states, "a socialistic government would not try intelligently to function in accord with economic principles in securing maximum satisfaction of the economic needs of the masses ... But such political prediction or prophecy is one thing, and reasoning in terms of economic principles is another" (Knight 1938b, 268).

decisions (Buchanan [1969] 1999, 88). Thus, rent-seeking activity, along with the Tullock-type welfare losses accompanying such activity would not exist (Tullock 1967). Once the agent-type of the socialist planner has been suitably remolded into that of *non-homo economicus*, the planner has no reason to seek income transfers at the expense of the hapless socialist consumer: moral education serves to induce an "as if" general interdependence of utility functions that negates the lure of any potential private rents: your loss of a dollar would be my loss; your gain of a dollar would be my gain (Becker 1976, 234-235). Although income transfers are a pure wash, the socialist planner's utility is decreasing in deadweight losses of the Tullock or Harberger variety.

The posited transformation of planner agent-type causes the worst-case conclusions of the Levy-Shleifer-Vishny model to simply disappear. Where the planner shares the "joys and sorrows" (Hume 1998, 84) of the consumer with an equal degree of "force and vivacity as if originally" their own, the incentive to generate artificial shortages vanishes. Where we suppress such Humean-type benevolence, however, and thus allow the private interest of the socialist planner to systematically diverge from that of the socialist consumer, the conclusions of the L-S-V model return with a worst-case vengeance. Why care about deadweight losses, when I, the imaginary socialist planner, am ahead by a few dollars?

As we have seen, the L-S-V model applies the textbook model of monopoly to the case of socialist planning. Wicked old *homo economicus* (a planner of the self-interested variety) selects quantity to maximize profits (in this case, bribe income extracted from consumers), generating the standard welfare loss.¹⁷ Socialism with self-interested planners generates pervasive inefficiency. Now allow the planners to be of the benevolent rather than self-

¹⁷ We ignore the likely dissipation of planners' rents in the rent-seeking contest to become an economic planner.

interested variety: A planner of this type will choose quantity to maximize social welfare. The personal opportunity cost of making such a choice is T : the potential bribe income that is foregone by the choice to produce Q_1 .³⁸ A benevolent planner cares not who enjoys the surplus T , only that T is realized, finding the deadweight loss accompanying any artificially generated shortages anathema.

Market Socialism and Best-case Thinking³⁹

Whilst Benjamin Lippincott ([1938] 1964) was in full agreement with Knight that the main problem of “a socialist economy is not an economic problem but a political and sociological one” ([1938] 1964, 37), he thought that democratic accountability would help render the economic planners the faithful agents of the citizenry, socialist industry working “in an atmosphere of publicity,” where “records would be open to the public. Few things would make for responsibility more surely than this” (Lippincott [1938] 1964, 34).⁴⁰ Such heady optimism regarding the likely workings of democratic institutions in mitigating the worst-case logic of the L-S-V model of socialism was far from unique to Lippincott. Indeed, Evan Durbin (1945) in similar fashion, blithely rejected Hayek’s worry that socialist planning would lead to serfdom: “[The] responsibility for taking economic decisions is transferred from the private company or group of stakeholders to the representatives of the community sitting upon the Board of a Public Corporation – who are, in their turn, answerable to some Supreme Economic

³⁸ Where Q_1 denotes the socially efficient level of output.

³⁹ “What is there in public choice theory that also gives the lie to the planning advocates? We need only return to the ancient Roman query: Who is to guard the guardians? Planners are also utility-maximizing individuals, and who could predict that planning decisions will be made contrary to the interests of those who make them?” (Buchanan 1979, 272)

⁴⁰ “If [the socialist state] ... were democratic its accounts would almost necessarily be open to public inspection” (Knight [1940] 1982, 169). Durbin (1949, 50): “[A] centrally controlled economy will be an economy with *open eyes*.”

Authority dependent upon a Parliament freely elected by the people” (Durbin, 1945, 361). The market socialist theorists repeatedly engaged in what we might term “nested” best-case thinking, objecting to any given worst-case objection to socialist planning by invoking an additional best-case move, one that, at best, simply pushes the original worst-case challenge to a somewhat higher level.

Lange dismissed the incentives argument by reference to the classic study by Berle and Means (1928) on the separation of ownership and control under capitalism, arguing that such a separation would prove unlikely given the democratic control of production under socialism.⁴¹ Suffice to note, that Lange is, of course, engaging in best-case speculation of a singularly dubious variety. Lange – in common with the other market socialist writers – failed to specify what socialist substitute for the market for corporate control would adequately mitigate agency problems under socialism.⁴² To invoke democratic control was, however, as Knight recognized, to somewhat miss the point.⁴³ Voters, even assuming they were to actually vote, are somewhat

⁴¹ Although stating, “*the real danger of socialism is that of a bureaucratization of economic life*” ([1938] 1964, 109), Lange suggests that planners “subject to democratic control seem preferable to private corporation executives who practically are responsible to nobody” (110). “Viewing society, then, as a want-satisfying machine and applying the single test of efficiency, free enterprise must be justified if at all on the ground that men make decisions, exercise control, more effectively if they are made responsible for the results of the correctness, or the opposite, of those decisions” (Knight [1921] 1957, 358).

⁴² “The concrete issue becomes that of the “responsibility,” or irresponsibility, of officials, and of concrete means for getting officials really to act for the interests of society rather than in their own interests, as individuals or as a “class”” (Knight [1939] 1982, 101-102). The socialization of the corporation substitutes “the public, organized in some political way, for the stockholders” (Knight [1921] 1957, 358). “[T]he salaried manager under a socialist government, whether appointed by a political superior or chosen in some way by a democratic constituency, would really be in a very different position from the president or manager of a present-day corporation. He could not conceivably be so directly accountable to the ultimate entrepreneur, society, as he is now to the ultimate entrepreneur, the small group of “insiders” who are the real owners of the business” (Knight [1921] 1957, 359). I am indebted to Ross Emmett for drawing my attention to Knight’s discussion of agency problems in *Risk, Uncertainty, and Profit*.

⁴³ The “difficulties of any real democracy are increased in large ratio with increasing size of the contemplated unit and also even that even if theoretical democracy could be realized, its meaning to the individual becomes correspondingly attenuated” (Knight [1940] 1982, 191). The “effective voice of an

unlikely to supply the public good of mitigating socialist agency problems in anything approaching an optimal quantity.

The Incentive-compatibility of socialism: The planned society as penitentiary?

Knight clearly recognized that the case made by social theorists for alternative sets of institutions (or rules of the game) was often based on implicit and highly idealized motivational assumptions:

The liberal will admit that much is to be said for an aristocratic constitution of society, including slavery, in an idealized form – if it could be assumed that there is any practicable way of having it in an ideal form. This “if” is enough by itself to give away the whole case (Knight [1946] 1982, 474).⁴⁴

The use of the word “if” played a vitally important role in the arguments that Knight made against would-be social reformers of various stripes. In January 1939, Knight reviewed *The Economics of Socialism* (Lange and Taylor 1938) for the *American Journal of Sociology*. In light of Lerner’s strictures (1937, 267) we can perhaps wryly note the irony in Knight’s reviewing for a sociology journal, what would become the leading text on market socialism. Knight’s review of Lange-Taylor was provocative for two reasons. First, Knight rejected the relevance of the contributions made by Lange and Taylor to the economics of socialist planning because their respective analyses were applicable almost “exclusively to the abstract problems of a stationary economy” (600), and thus failed to grapple with any of the truly serious problems of dynamic economic adjustment that were likely to plague the workings of socialist planning (also see Knight [1940] 1982, 174, 189). Second, Knight made the following highly

individual in free and rational group discussion necessarily decreases rapidly as the size of the group increases, and soon becomes infinitesimal or a matter of accident” (Knight [1944] 1982, 419). Also see Knight ([1921] 1957, 359-361; [1939] 1982, 95; [1944] 1982, 422) on democracy and agency problems.

⁴⁴ On the role played by best-case thinking in the 19th century debate between economists and apologists for racial slavery, see Levy (2001).

intriguing remark regarding market socialist models: “Even if one assumes that the social ideal is a model penitentiary, these problems [the serious problems of socialism or collectivism] are political, not economic” (Knight, 1939, 600)⁴⁵. In the history of economics, only one theorist – as far as I am aware – is famous for, among other things, having designed just such an ideal penitentiary: Jeremy Bentham’s Panopticon scheme (see Semple 1993). Bentham thought that the transparency inherent to the Panopticon scheme helped to provide a set of relatively incentive-compatible rules of the game. Similarly, considerations of transparency were of great importance for the underpinnings of Bentham’s advocacy of representative political institutions.⁴⁶ Bentham thought that transparency rendered a relatively easy solution to the principal-agent relationship between citizen and government, worrying that any opaqueness in the workings of government facilitated rampant opportunism on the part of public functionaries. Transparency plays an equally important role in Bentham’s Panopticon scheme. The design of the Panopticon prison enabled the Warden to monitor the actions of prisoners at all times,⁴⁷ allowing any malfeasance to be identified and punished. The Panopticon scheme was designed to make the penitentiary, although in reality built of stone and mortar, as easy to monitor as would be the case were it actually built of glass (Semple 1993).⁴⁸ Although the warden can

⁴⁵ Knight made a strikingly similar remark in 1940: “[T]he type of society advocated by Utopians and radical reformers usually bears a striking resemblance to a model penitentiary or asylum of some sort. One must question both whether that is a mode of life which men would like (or pronounce good) and the likelihood that under the conditions of the real world the asylum would be or would continue to be a model one” (Knight [1940] 1982, 167).

⁴⁶ Approbational mechanisms provide an important constraint against the likely misuse of political power in the accounts provided by Bentham ([1830] 1984, 174) and Mill (1992, 88-90, 106). The effectiveness of approbational constraints are weakened in the absence of transparency: There is an approbational tragedy of the commons.

⁴⁷ The “power of inspection is rendered so complete, that the prisoner may be, and cannot know but that he is, under the eyes of his keepers, every moment of his time” (Mill 1992, 199).

⁴⁸ Transparency was of vital importance to Benthamite constitutional political economy.

monitor the inmates, the inmates, however, cannot similarly observe the warden.⁴⁹ The design of the Panopticon prison is akin to a one-way mirror. This, of course, raises the worst-case question as to who, or what, provides a constraint against the potential for malfeasance on the part of the warden?⁵⁰

We do not have to search very far to find a parallel for the Panopticon prison in the market socialist literature. H. D. Dickinson (1933, 1939) famously proposed that under socialism, the entire economy would operate, “so to speak, within glass walls” (Dickinson 1939, 9, 20).⁵¹ Although the transparency provided by Dickinson’s envisaged “glass walls” allows the planners to monitor the economy, what happens if the ‘economy’ cannot similarly monitor those agents who are to carry out the economic planning? Where transparency is only of the one-way type, there is a rather important informational asymmetry between planners and citizenry. Who therefore, is to constrain the self-interest of the economic planners? The usual market socialist response to that particular question was, as we have seen above, to invoke some type of democratic accountability: Any political agency problems would be mitigated because representative institutions⁵² would hold the economic planners strictly accountable for their actions (see e.g., Lippincott [1938] 1964; Durbin 1945). The importance of transparency to the

⁴⁹ On the Panopticon scheme, see Semple (1993) and Mill (1992, 197-224).

⁵⁰ Although the Warden cannot be observed by the prisoners, the Warden is subject to monitoring by the public: “No misconduct towards the prisoners, on the part of their principals, can remain unknown to the public, who may obtain a regular admittance into the inspection tower, and regulated communication with the prisoners” (Mill 1992, 199).

⁵¹ The ‘Economy’ is rendered a wholly transparent set of institutions.

⁵² “The theory of representation is a large and vague subject. The theoretical function of an “agent” varies from doing exactly what his principal would do, to act for him purely as a matter of convenience, to acting as a custodian and judge of his principal’s interests, or the means of achieving interests of any degree of remoteness and generality up to selecting his wife, or saving his life, or even his soul. In a democracy, officials are theoretically the agents of the group as a unit, which they represent” (Knight [1944] 1982, 418).

market socialist writers can hardly be understated.⁵³ H. D. Dickinson's envisaged "Supreme Economic Council" (1933, 239) had the "right of inspection and audit of the entire [economic] system" (239), with the requisite transparency induced by the "fullest publication of output, costs, sales, stocks, and other relevant statistical data" (239). "All enterprises" work "as it were within glass walls" (239), with the ignorance of "economic opportunities" eliminated by the "publicity of a planned economic system (245). Remarkably, Dickinson wrote:

The beautiful systems of economic equilibrium described by Bohm-Bawerk, Wieser, Marshall and Cassel are not descriptions of society as it is, but prophetic visions of a socialist economy of the future (Dickinson 1933, 247).

In equilibrium, agents would have perfect information: Transparency, therefore, cannot help but obtain, the "glass walls of the socialist economy" (249) serving to ensure that there "would be no danger" that "independent bodies of entrepreneurs with interests opposed to the social interest" would engage in rent-seeking activities under the guise of, for example, the argument that favors protective tariffs to help "infant-industries" (249).⁵⁴ Dickinson's best-case thinking is clearly apparent.⁵⁵

I suggest that Knight had recognized the important similarities between the design of the Panopticon prison and the planned society (1939, 600). Indeed, Knight pursued the analogy

⁵³ The market socialist analysis of transparency and accountability is wholly retrogression from the transparency of the Panopticon. Mill (1992) analyzes a variety of rational-choice type mechanisms that serve to induce adherence on the part of the Warden (the agent) to the wishes of the public (the ultimate principal): e.g., (1992, 212-219).

⁵⁴ "Only in a socialist community, where production can be carried on in the full light of statistical measurement and publicity, is it possible to realize the true principles of economic valuation" (Dickinson 1933, 246).

⁵⁵ Dickinson (1933, 237) wrote "until recently, the question of incentives has occupied the front place in discussions on the possibility of collectivist socialism", only to dismiss the question, suggesting that the "spectacle" of the "collectivist state actually working (even though imperfectly) ... in Soviet Russia, the Soviet attempts at "prodigious feats of economic reconstruction" making the "incentive argument ... less convincing" (1933, 237). On the Soviet experience, see Boettke (1990). Dickinson argues that "socialist costing" will eliminate any divergence between private and social marginal costs (1933, 245-246).

between the two at far greater length in 1944: “Any government which had the task of managing the economic life of a modern nation, to say nothing of the world, would have to be a dictatorship and to repress the primary freedoms of thought, communication and association” (Knight [1944] 1982, 431). Knight might well be describing certain aspects of the Panopticon scheme writ large (see Mill 1992, 220-222). Moreover, Knight’s remarks “would be true even if [the government] ... were staffed with people who personally abhorred power – and the contention that power would fall into the hands of such people will appeal only to the most romantic credulity” (Knight [1944] 1982, 431).

At this juncture, Knight’s worst-case thinking came into its own. Knight rejected the idea that democracy would adequately mitigate political agency problems under socialism.⁵⁶ Knight argued that democracy was incompatible with economic planning, making an argument somewhat akin to that which Hayek would later make in chapter 10 of the *Road to Serfdom*:

A very little examination of the political aspect of socialism will show that the difficulties of making competition work are multiplied many fold by throwing all the details of economics organization and management into the arena of politics. Reflection will also show that a government which controls the economic life of a modern nation must ruthlessly suppress opposition, and all conduct likely to lead to serious opposition. Hence it must suppress freedom of discussion and be a dictatorship. Even if the persons in power did not want this it would be necessary, to keep the machine going and secure even minimum efficiency; and it is hardly imaginable that people who did not like power could get into the control positions (Knight [1941] 1982, 242).⁵⁷

⁵⁶ “What is necessary is a development of political machinery and of political intelligence in the democracy itself to a point where men in responsible positions would actually feel their tenure secure and dependent only on their success in filling the position well. ... The essential problem is wisely to select such responsible officials and promote them strictly on a basis of what they accomplish, to give them a “free hand” to make or mar their own careers. This is the lesson that must be learned before the democratization of industry will become a practical possibility. If we substitute for business competition, bad as it is, the game of political demagoguery as conventionally played ... the consequences can only be disastrous” (Knight [1921] 1957, 360-361).

⁵⁷ “The authorities of a collectivist state would have to have unlimited power, and *security of tenure*, and would have to exercise their power ruthlessly to keep the machinery of organized production and distribution running. They would have to enforce orders ruthlessly and suppress all disputation and argument about policies” (Knight 1938c, 868-869). Also see Knight (1952, 414-415).

The incompatibility of democracy with the requirements of economic planning would necessitate that the planners abolish the constraint provided by democracy.⁵⁸ Whereas Bentham's Panopticon scheme envisaged a plethora of mechanisms that would serve to constrain any likely malfeasance on the part of the Warden, socialist planning, would, of necessity, have to do away with any similar types of constraints upon the discretionary power of the planning bureaucracy. Transparent planning was, for Knight, a chimera.⁵⁹

Boettke and Vaughn (2002, 166) suggest that it is "not exactly clear what ... [Knight] believed would constitute a good political argument" against socialism.⁶⁰ I would argue, however, precisely the opposite: Knight hinted at the way in which selection effects would generate the transformation of the socialist polity from a democratic to a dictatorial political order, suggesting these selection effects would sort into positions of discretionary power within the socialist administration precisely those individuals who had a comparative advantage in wielding such power:

It seems to me certain: (a) that the governing personnel in a socialistic state would be in a position to perpetuate themselves in power if they wished to do so; (b) that they would be compelled to assume permanence of tenure and freedom from the necessity of seeking frequent re-election, as a condition of administering the economic life of a modern nation, even if they did not wish to do so; and (c) that they would wish to do so – that we cannot reasonably imagine political power on the scale involved falling into the hands of persons of whom this would not be true (Knight [1940] 1982, 166).⁶¹

⁵⁸ See Knight (1938a, 243, 250).

⁵⁹ Knight refers to the "constitutional difficulties of designing the best organization chart for the bureaucracy which is to run the economic system" (Knight 1938a, 250).

⁶⁰ Boettke and Vaughn (2002, 166) suggest that "Knight despised" Hayek's *Road to Serfdom*. Knight (1946, 453), however, wrote of the *Road to Serfdom*: "I agree with his [Hayek's] general thesis, that general replacement of the free-market organization by a predominance of centralized political control will mean the destruction of democracy and freedom and the establishment of a totalitarian social order. This seems as certain as any general political prediction can be, which of course is not comparable to the status of established scientific laws, to say nothing of logical necessity."

⁶¹ Also see Knight (1938a, 242-243; 1938c, 869-870; 1940, 24; 1952, 415)

It is unclear why Boettke and Vaughn (2002, 166) would treat Knight with such a lack of generosity. Indeed, the similarities between Knight's political critique of socialism and that provided by Hayek ([1986] 1944) are legion.⁶²

Conclusion

The best-case theorist picks an idealized state of the world and then proposes a major institutional change (e.g., market socialism), which is only optimal given the empirical realization of the theorist's ideal conditions. Thus, market socialism provides a clear example of best-case thinking. Lange ([1938] 1964) suggested that market socialist price setting would take place in accordance with the principle of "trial and error", envisaging that the economic planners would adjust prices so as to eliminate any excess supplies (negative or positive) of goods. As recognized by public choice theory (e.g., Levy 1990), Lange's model implicitly assumes public-spirited planners. Lange implicitly posits a state of the world where planners seek to maximize social welfare. Lange failed to pay any attention to the type of worst-case considerations (Levy 2002) akin to those hinted at in Friedman's 1947 critique of the Lange-Lerner model (Friedman 1947, 415): Market socialist institutions must be judged by "the extent to which they lend themselves to abuse, i.e., the ease with which they can be used for objectives other than the general welfare." Frank H. Knight would surely concur.

⁶² Indeed, Hayek wrote: "Although this might be unwise, there is nothing bad or dishonorable in approving a dictatorship of the good" (1986 [1944], 100). Hayek doubted, however, that the "good" would remain in power for very long, the "readiness to do bad things ... [becoming] a path to promotion and power" (112). See Boettke (1995) for an excellent discussion of Hayek's critique of socialist planning. Remarkably, Hayek cites Knight's worst-case argument only once in that critique, citing Knight's remark (1938c, 869) that the probability that those in power (the socialist administration) would prove individuals "who would dislike the possession and exercise of power" was "on a level with the probability that an extremely tender-hearted person would get the job of whipping-master on a slave plantation". See Levy (2001, 206-208) for an important discussion of the "kind masters" point and its relevance to 19th century debates over slavery.

**Transparency, incentive-compatibility, and agency:
F. A. Hayek on Market Socialism as a Public-Choice**

Introduction

Peter Boettke (see, e.g., Boettke 1995, 2000; Boettke and Leeson 2002a, 2002b) has recently drawn attention to the important public choice type insights that F. A. Hayek provided in *The Road to Serfdom* (1944). In particular, Boettke disputes any argument alleging that Hayek was somewhat ignorant of public choice arguments regarding government failure: particularly so, in the critique that Hayek provided of socialist economic planning (see, e.g., Higgs 1988-89).¹ “Hayek,” Boettke suggests, was far from “ignorant of public choice problems: [rather] he just alters the analytical treatment of these problems in certain directions that differ from more traditional treatments in the literature” (Boettke 1995, 20). While I have no real quarrel with Boettke’s insistence that Hayek’s work contains various public choice type insights, I do suggest, however, that Boettke inadequately appreciates the degree to which Hayek is most emphatically *not* a fellow traveler of public choice theory. In particular, Boettke appears rather unwilling to acknowledge that Hayek overtly rejects the argument which provides the crux of the modern public choice critique of socialist planning: namely, the recognition that self-interested economic planners will readily take advantage of the fact that socialist planning transforms the entire economy into one gigantic monopoly (see e.g., Levy 1990; Shleifer and Vishny 1992; Boettke

¹ Boettke (1995, 7) cites Robert Higgs: “[R]eading Hayek, one would never know that public choice had been invented. Neither Buchanan nor Tullock nor any of their followers gets a single mention. Nor does Hayek show any awareness of public choice problems.”

and Anderson 1997).² Indeed, Hayek thought the working assumption of public choice theory – that agent-type is aptly modeled as *homo economicus* – a decidedly moot supposition (Boettke 1995, 18).³

That Hayek was somewhat uneasy with the essentials of the modern public choice critique of socialist economic planning is clearly a matter of public record. Twice during the socialist calculation debate, Hayek raises the ‘planning equals monopoly’ point (Hayek 1935, 220; 1986 [1944], 69), only, however, to immediately dismiss any suggestion that socialist planners (or enterprise managers) would behave in accordance with the *homo economicus* postulate. Indeed, Hayek readily accepted the market socialist supposition that socialist planners and industry managers were more accurately characterized by their public-spiritedness than by venality. Rather than adopt a public choice type – or ‘worst-case’⁴ – view regarding the likely

² “Socialists themselves generally assume that there will be very much more monopoly under socialism, even in particular industries, to say nothing of the fact that all production would be in the nature of the case to be one gigantic monopoly in the hands of the government – but of course all are assumed to be managed in the public interest” (Knight 1982 [1940], 170-171).

³ Hayek writes: “*homo oeconomicus* was explicitly introduced, with much else that belongs to the rationalist rather than to the evolutionary tradition, only by the younger Mill” (Hayek 1960, 61). Mill, however, wrote regarding the *homo economicus* assumption: “The principal error of narrowness with which they [political economists] are frequently chargeable, is that of regarding ... their frequent experience of mankind, as of universal validity; mistaking temporary or local phases of human character for human nature itself; having no faith in the wonderful pliability of the human mind; deeming it impossible, in spite of the strongest evidence, that the earth can produce human beings of a different type from that which is familiar to them in their own age” (Mill 1969, 306). Elsewhere, Hayek (1984) attacks Mill for supposing the malleability of agent-type. Lionel Robbins (1961, 71-77) justly criticizes Hayek’s reading of 19th century Utilitarianism. Public choice theory “typically distinguishes itself by the assumption that all the players in the political game are of the *homo economicus* type – ‘egoistic, rational utility-maximisers’, to use Dennis Mueller’s terminology” (Brennan and Hamlin 2000, 18). “What is there in public choice theory that also gives the lie to the planning advocates? We need only return to the ancient Roman query: Who is to guard the guardians? Planners are also utility-maximizing individuals, and who could predict that planning decisions will be made contrary to the interests of those who make them?” (Buchanan 1979, 272)

⁴ The classic statement of worst-case thinking is provided by David Hume ([1741] 1985, 42-43): “Political writers have established it as a maxim, that, in contriving any system of government, and fixing the several checks and controuls of the constitution, every man ought to be supposed a *knave*, and to have no other end, in all his actions, than private interest.” Also see Brennan and Buchanan (1985 [2000]).

motivation of socialist economic planners during the socialist calculation debate.⁵ Hayek instead treated planner agent-type as somewhat more akin to that of *non-homo economicus*: thereby accepting an assumption that was largely indistinguishable from the best-case theorizing⁶ that was so pervasive among Hayek's pro-planning opponents.

Two critiques of socialist economic planning: Austrian and Public Choice

The public-choice critique⁷ of socialist economic planning makes immediate intuitive sense to anyone with a modicum of training in neoclassical price theory. Indeed, as Frank H. Knight had repeatedly warned throughout the 1930's and 1940's, socialist planning would replace the market economy (competitive or otherwise) with one giant de facto monopoly. The public choice critique of socialism suggests that unless we are to posit some magical transformation⁸ of agent-type – with socialist planners becoming *non-homo economicus* (Buchanan 1999 [1969], 88) – socialist economic planning will exacerbate the very same deadweight losses (attributable to monopoly) that market socialist writers (e.g., Lange 1964 [1938], 107-108; Dickinson 1939, 4, 9,

⁵ “It seems extremely difficult for anyone to adopt a socialist position and at the same time be familiar with and accept the analysis of public choice. Here I use *socialist* in the sense that this term was employed in the 1930's, when Lange, Lerner, and others convinced so many of their colleagues that socialism could *work*. No more than a smattering of sophistication in public choice (or in ordinary common sense, for that matter) is required to suggest the absurdity in that position” (Buchanan 1979, 272).

⁶ Best-case thinking is roughly equivalent to the benevolent-despot model of politics. Brennan and Buchanan (2000 [1985], 55) state, “the benevolent despot model of politics and government has promoted and sustained monumental confusion in social science, and social philosophy more generally.”

⁷ The public choice critique of socialism takes Edgeworth's statement as axiomatic: “The first principle of Economics is that every agent is actuated only by self-interest” (Edgeworth 1881, 16). Hayek (1960, 61) appears to disagree. Buchanan's pungent query (1991, 17) is apposite: “Why did economists, who model man as *homo economicus* in analysing markets, fail to recognise that incentives remain relevant in all choice settings?”

⁸ David Hume's remark: “All plans of government, which suppose great reformation in the manners of mankind, are plainly imaginary” (1985, 514) is highly apposite to socialism. James Buchanan (1979) has often stated that public choice theory is the analysis of politics “without romance”.

116; Lerner 1944, 3, 168) once thought provided adequate reason to replace markets with planning.

The socialist calculation debate was ignited in 1920 when Ludwig von Mises declared that rational economic calculation was impossible under socialism (see, e.g., Lavoie 1985; Steele 1992; Vaughn 1980). Mises argued that without a market for factors of production (any such market necessarily precluded by the common ownership of the means of production), socialist planners – lacking market generated prices for capital goods and other inputs – would possess no economically meaningful criteria for adequately estimating the opportunity costs of alternative resource uses (Mises 1935 [1920], 93, 102). Rather intriguingly, Mises averred that socialist economic calculation was impossible irrespective of the particular agent-type that we might attribute to the socialist economic planners.” Thus, though the economic calculation argument (Mises 1935) predicts that any set of socialist shadow prices generated by the planning authority will surely diverge from the set of prices otherwise comprising the hypothetical equilibrium vector of ‘planned’ shadow prices (some shadow prices set too low, while other shadow prices are set too high) – thereby creating pervasive shortages *and* surpluses – the calculation argument does not suggest that any particular ‘bias’ will characterize the empirically realized vector of socialist prices (any such bias, of course, engendering pervasive shortages *or* surpluses. See, e.g., Levy 1990, 215). Indeed, the ‘Austrian’ critique of socialist planning explicitly ignores the incentives of the would-be socialist price-setters, instead focusing on the ‘calculation’ (or

“*The impracticability of Socialism is the result of intellectual, not moral, incapacity. Even angels, if they were endowed only with human reason, could not form a socialistic community. If a socialist community were capable of economic calculation, it could be set up without any change in men’s moral character*” (Mises 1981, 407, italics added). “Mises’s argument against the practical feasibility of what he calls “socialism” does not hinge upon questions of motivation, but rather claims that, with the best will in the world, humans *are not able* to operate a society on ‘socialist’ lines, because modern industry cannot be successfully guided or administered without the information provided by market prices of factors of production. Mises claims that even where there’s a will, there’s no way” (Steele 1992, 2).

'knowledge') problems that would most surely plague any genuine attempt at socialist economic planning.¹⁰

The logic of the public choice critique of socialism, however, centers its analytical attention squarely on the incentives facing the would-be socialist price-setters, thereby – and contra to the logic of the Mises-Hayek critique of planning – predicting that a clear-cut 'bias' will surely exemplify any empirically realized vector of "centrally planned prices" (Levy 1990).¹¹ Whereas the market socialists (e.g., Lange 1964, 70-71; Dickinson 1939, 62-63) had suggested that socialist planners would rapidly adjust prices to eliminate any temporary shortages or surpluses of goods, the public choice critique of socialist planning takes the opposite tack, arguing that the socialist planner – in common with any other rational and self-interested chooser – will choose to systematically generate artificial shortages by pricing goods below their market clearing price, thereby facilitating the extraction of bribes and other favors from quantity constrained consumers (Levy 1990; Shleifer and Vishny 1992).¹² The argument is, of course,

¹⁰ Hayek makes reference to schemes for socialist price-setting which suggest: "on the assumption of a complete knowledge of all relevant data, the values and the quantities of the different commodities to be produced might be determined by the application of the apparatus by which theoretical economics explains the formation of prices and the direction of production in a competitive system. Now it must be admitted that this is not an impossibility in the sense that a determination of prices by such a procedure being logically conceivable in any way invalidates the contention that it is not a possible solution, only proves that the real nature of the problem has not been perceived" (Hayek 1935, 207-208). Why does Hayek assume that the planners will not try to extract maximal surplus from the populace by rigging the vector of prices? Indeed, we can ask what mechanism constrains the Walrasian auctioneer to arrive at the set of price inducing the socially efficient equilibrium? Ali Khan's lecture at the 2000 Summer Institute for the Preservation of the Study of the History of Economics was highly illuminating on this point.

¹¹ The Mises-Hayek critique of socialism suggests that we should expect socialist planning to generate *shortages* and *surpluses* of goods. As Shleifer and Vishny (1992, 238) pungently note, the "most pervasive feature of socialism" is, however, the *general* "shortage of goods".

¹² We follow Shleifer and Vishny (1992, 238-239) in assuming that any officially realized profits are remitted to the state treasury, thus explaining why socialist industry managers do not simply increase the official prices of goods. Equally, we assume that the planning ministry and the socialist industry managers collude to pursue joint 'bribe' maximization. Whereas the price-setters and enterprise managers cannot simply pocket any officially realized profits, they can, however, retain any bribes they receive. Shleifer and Vishny (1993) provide an analysis of the case where the assumption of joint 'bribe'

simply the application of Tullock's canonical theory of rent-seeking (Tullock 1967) to the case of socialist planning. The public choice critique of socialism, whilst recognizing the difficulties in economic calculation that would surely plague any genuine attempt at socialist planning (Buchanan 1999 [1969], 87-89) suggests, however, that incentive problems ought to take primacy as regards the potency of any critique of socialist economic planning. Irrespective of whether planners can engage in successful economic calculation or not, socialist economic planners lack any incentive to generate socially efficient resource allocation decisions.¹³

Hayek's Best-case theorizing: public-spirited economic planners?

To return to our earlier remark regarding Hayek's ready acceptance of the highly romantic motivational assumptions that his pro-planning opponents made (planner agent-type is *non-homo economicus*), we note that Joseph Schumpeter readily charged Hayek with best-case theorizing in a 1946 *JPE* review of *The Road to Serfdom* (1944). Though Schumpeter – somewhat characteristically – was only to hint at many apposite points (see, Levy 1990, 222), he did overtly suggest that the pro and anti-central planning sides in the socialist calculation debate had equally adopted the best-case supposition of public-spirited economic planners (see, e.g., Buchanan 1999 [1969], 87-88; Levy 1990).¹⁴ In particular, Schumpeter made the following

maximization fails to obtain. In this case, the problem of 'downstream monopolists' rears its ugly head and deadweight losses are concomitantly exacerbated. Also see Buchanan and Yoon (2000).

¹³ Mises (1935, 103) writes: "It will be evident, even in a socialist society, that 1000 hectolitres of wine are better than 800, and it is not difficult to decide whether it desires 1000 hectolitres of wine rather than 500 of oil. There is no need for any system of calculation to establish this fact: the deciding element is the will of the economic subjects involved. But once this decision has been taken, the real task of rational economic direction only commences, i.e. economically, to place the means at the service of the end". Surely, however, the ease with which bribes can be extracted from consumers is one margin relevant to the choice of output-mix that a self-interested planner will make. See Shleifer and Vishny (1992, 238).

¹⁴ "[N]ot all relevant points can be made without more plain speaking about group interests than he [Hayek] is willing to resort to. In this respect – perhaps also in others – he might have learned a useful lesson from Karl Marx" (Schumpeter 1946, 270).

intriguing remark: “[H]e [Hayek] and they [the market socialists] proceed from the political sociology – the theory of political behavior and motivation – of J. S. Mill” (Schumpeter 1946, 270). What might Schumpeter have meant by this somewhat oblique reference to Mill’s “political sociology”? Our answer lies in Schumpeter’s *History of Economic Analysis* (1994 [1954]): Schumpeter equating the political economy of Bentham and the Mills with best-case theorizing, suggesting that Utilitarianism was practically little more than the benevolent-despot assumption so despised by modern public choice theory.¹⁵ By implication, Schumpeter (1946, 270) sought to censure Hayek and the market socialists for their inadequate attention to the material self-interest of the would-be socialist planners (see, Levy 1990, 221-223).

Schumpeter’s charge that Hayek was too accepting of the supposition of planners as benevolent-despot rings true. Indeed, can anyone truly gainsay that Hayek – not only in his purely technical contributions to the socialist calculation debate (see, e.g., Lavoie 1985, 171),¹⁶ but similarly in the *Road to Serfdom* – was far too readily accepting of the assumption that planner agent-type was that of *non-homo economicus*? Whilst Hayek certainly did make an all-too brief – albeit somewhat oblique – allusion to the likely self-interest of his market socialist colleagues in the preface to the *Road to Serfdom*,¹⁷ he was clearly loath to openly embrace a worst-case critique

¹⁵ Schumpeter suggested that Utilitarianism had failed to take account of “the facts of political life and of the way in which states, governments, parties, and bureaucracies actually work. ... [I]ts application to political fact spells ... disregard of the essence – the very logic – of political structures and mechanisms, and cannot produce anything but wishful daydreams” (Schumpeter 1994 [1954], 429). Recognizing the prevalence of best-case thinking, Schumpeter charged economists with treating the state as if it were a “superhuman agency for the public good,” thereby neglecting “all the facts about the realities of public administration that modern political science provides” (Schumpeter 1994 [1954], 37).

¹⁶ The relevant papers are collected in Hayek (1948, 119-208).

¹⁷ “I am always told by my socialist colleagues that as an economist I should occupy a much more important position in the kind of society to which I am opposed – provided, of course, that I could bring myself to accept their views” (Hayek 1986 [1944], v). Moreover: “For those who, in the current fashion, seek *interested motives* in every profession of a political opinion, I may, perhaps, be allowed to add that I have every possible reason for *not* writing or publishing this book. It is certain to offend many people with whom I wish to live on friendly terms” (Hayek 1986 [1944], v). Frank H. Knight is characteristically

of socialist economic planning of the type that public choice theory provides. Hayek instead chose in the *Road to Serfdom* (1986 [1944]) to take the motivational presuppositions made by the pro-planning side of the debate at face value, and thereby, rather than providing a worst-case critique of socialist planning,¹⁸ sought instead to demonstrate that the situational logic intrinsic to any attempt at rigorously implementing socialist planning would – despite the public-spiritedness of the planners – surely generate results that were anathema to democratic socialists (see, e.g., Boettke 1995, 11-15).¹⁹ Whilst any detailed consideration of the *Road to Serfdom* is far beyond the scope of this paper, I do suggest, however, that it is quite understandable why Hayek's market socialist colleagues at the LSE (see, e.g., Durbin 1945) would find Hayek's thesis that the 'worst get on top' less than persuasive. Indeed, the logic of the Hayekian account appears somewhat faulty. Why would public-spirited planners seek to rigorously implement planning irrespective of any deadweight losses that planning generates? Surely planners of a 'good' agent-type would

pungent: "All political opposition to this programme [Marxism] is assumed as a matter of course to derive from the bourgeois class itself, either directly or through paid agents and dupes. (Non-Marxist economists are allowed to hover more or less between these two classifications, paid agent and dupe.) ... [T]he allegation of selfish interest which is glibly pinned on the opposition applies even more obviously to the promoters of the class war themselves. They are *assumed to be free from any taint of self-interest!*" (Knight [1939] 1982, 117-118, italics added).

¹⁸ Boettke (1999, xxvi) is incorrect to claim that the "Hayekian form of constitutional political economy – just as is the case with the main scholar of this field in modern times, James Buchanan – was a 'worst case' political economy". Hayek's critique of socialist planning is most emphatically *not* a worst-case critique in the vein of modern constitutional political economy. I wonder how Boettke's claim (1999, xxvi) squares with what Brennan and Buchanan (2000 [1980], xv) and Hayek (1986 [1944], 69) have to say?

¹⁹ "We all wish to live in a community that is as rich as possible, in which consumers' preferences determine the relative output of goods that can be consumed by individuals, and in which there is freedom of discussion and political association and responsible government" (Durbin 1945, 357). "Most of us are socialist in our economics because we are "liberal" in our philosophy, and we believe that it is Professor Hayek who has missed the road to freedom that all humanitarian "liberals" wish to find" (Durbin 1945, 357). "Totalitarianism is neither a consequence of "corruption" nor "historical accident," but rather a logical consequence of the institutional incentives of the attempt to centrally plan an economy" (Boettke 1995, 12). "Hayek was directly challenging the argument that experiments in real existing planning, say in the former Soviet Union, were tainted by "historical accident" and or "bad people", and, therefore, could not be employed to illustrate the difficulties with planning" (Boettke 1995, 12). Hayek's critique appears, however, very much a contingent argument: predicated on a somewhat implausible premise.

simply admit to their mistakes and retreat from planning. The implicit mechanism posited in chapter 10 of the *Road to Serfdom* appears to necessitate the somewhat implausible premise that public-spirited planners lexicographically rank planning higher than any value such as democracy or welfare. We can readily understand why ‘worst-case’ planner agent-types would intransigently continue with socialist planning: namely, planning allows them to get rich (see, e.g., Levy 1990). Public-spirited planners (posited by Hayek), however, are motivated by considerations of social welfare, and thus, would quite readily abandon their faith in planning upon realizing that socialism was a mistake, rather than resorting – as Hayek argued they would in chapter 10 of the *Road to Serfdom* – to ever-greater totalitarian control and machinery in a single-minded – and inevitably failing – attempt to make planning work.²⁰

Worst-case Thinking: Hayek's rejection of the public choice critique of socialist planning

Intriguingly, Hayek had flirted with worst-case thinking in the volume *Collectivist Economic Planning* (Hayek 1935, 220-222),²¹ pondering whether it would prove “in the general interest to plan or rationalize individual industries where this is only possible through the creation

²⁰ Keynes appears to share my judgment: “You [Hayek] will not expect me to accept all the economic dicta in it [*The Road to Serfdom*]. But morally and philosophically I find myself in agreement with virtually the whole of it ... what we need is the restoration of right moral thinking – a return of proper moral values in our social philosophy ... I accuse you of perhaps confusing a little bit the moral and material issues. *Dangerous acts can be done safely in a community which thinks and feels rights, which would be the way to hell if they were executed by those who think and feel wrongly*” (Keynes 1980 [1944], 385-388, italics added). “[T]he very difficulties of a consistent pursuit of central planning make it improbable that any regime would persist very long in this direction: it is likely that such a regime would instead radically modify its “central planning” to make it more compatible with a price system” (Lavoie 1985, 154).

²¹ The publication of *Collectivist Economic Planning* (of which Hayek was editor) in 1935 ignited the English language phase of the socialist calculation debate. Remarkably, no participant in the calculation debate paid any attention to the three pages in which Hayek (1935, 220-222) explores the ‘planning equals monopoly’ insight. Nor does any of the recent literature on the debate – with the exception of Lavoie (1985, 163) who, while skirting the point appears not to notice the public choice implications of Hayek’s insight – even mention Hayek’s remarks.

of a monopoly” (Hayek 1935, 220). Hayek suggests a model of socialist planning where all industries are “completely integrated monopolies.” (220), acknowledging the public choice point that socialist monopoly will generate pervasive deadweight losses (220-221): the “concentration on [making] maximum monopoly profits rather than on making the best use of the available factors” proving the inescapable “consequence of making the right to produce a good itself a “*scarce factor of production*”” (Hayek 1935, 222, italics added). Indeed, Hayek attests monopoly socialism to guarantee the optimal use of only one scarce input: namely, the “possibility of exploiting consumers” (Hayek 1935, 222). Despite grasping the crux of the public choice critique of socialist planning some 55 years prior to the arguments explicit appearance in the literature (Levy 1990), Hayek remarkably disavows the worst-case implication of the ‘planning equals monopoly politics’ insight, suggesting that the socialist industry manager would – unlike *homo economicus* – prove wholly unwilling to exploit any de jure monopoly (229).²²

Hayek similarly alludes to the ‘socialist planning equals monopoly’ insight in the *Road to Serfdom* (1944). Despite recognizing that any “authority directing the whole economic system would be the most powerful monopolist conceivable” (Hayek 1986 [1944], 69), Hayek repudiates the worst-case logic of the argument: “we need probably not be afraid that such an authority would exploit this power in the manner in which a private monopolist would do so ... its purpose would presumably not be the extortion of maximum financial gain” (69-70).²³ That Hayek would so readily make such a giant leap of faith is quite remarkable. Indeed, Hayek’s steady adherence to best-case theorizing raises a somewhat intriguing question: Does Hayek so readily withdraw

²² I wonder if best-case concessions of this type help to explain Schumpeter’s remarks in his 1946 review of Hayek’s *Road to Serfdom*? Also see Buchanan (1989, 21, 1991, 15). Remarkably, neither Levy (1990), Boettke (1995), nor Caldwell (1997) pay any attention to these passages in *Collectivist Economic Planning*.

²³ Hayek clearly accepts that the planners are *non-homo economicus*.

the worst-case insight that socialist planning equals monopoly writ large because he recognizes that the ‘incentives’ and ‘economic calculation’ critiques of socialist economic planning (see, e.g., Cowen 1995) are somewhat incompatible? Perhaps Hayek withdrew the ‘planning equals monopoly’ insight rather than undercut the basic logic of the Mises-Hayek critique of socialist economic planning.^{24, 25}

The Austrian and Public Choice critiques of Socialist Planning: complements or substitutes?

At this juncture, we take note of a highly intriguing question suggested by Tyler Cowen (1995): Are the ‘Austrian’ and ‘public choice’ critiques of socialism complements or substitutes? As suggested by Cowen (1995, 244), the public choice critique of socialist planning appears *prima facie* somewhat inconsistent with the Mises-Hayek economic calculation argument. The public choice critique of socialist planning (the incentives argument) implies that socialist enterprise managers are rather good at calculating the (privately optimal) prices that maximize their own personal income (equal to official salary plus any bribes or favors that are extracted from hapless consumers), thereby suggesting that were a socialist manager to undergo a suitable transformation in agent-type – *homo economicus* to *non-homo economicus* – they would set price

²⁴ Perhaps Cowen’s point is further implied by the remarks that Mises made regarding ‘economic calculation’ in the Soviet Union: “They could resort to economic calculation on the ground of the prices established abroad. Without the aid of these prices their actions would have been aimless and planless. Only because they were able to refer to these foreign prices were they able to calculate, to keep books, and to prepare their much talked about plans” (Mises 1966, 702-703). Did the Soviet Union simply copy Western prices? Although social efficiency might have increased had they done so, what incentive did Soviet planners or enterprise managers have to take regard of social efficiency considerations? See Caplan (2002, 10-11). Planners with good incentives (or better motivation) could ape Western prices and increase social welfare.

²⁵ Boettke (1999, xviii) suggests that in the *Road to Serfdom* Hayek thought it “inevitable that these powerful men [planners] would run the system to their own personal advantage”. As we have seen, however, Hayek (1986 [1944], 69-70) rejected any suggestion that the planners sought to maximize private welfare.

and quantity to maximize social welfare.²⁶ As Cowen (1995, 244) rather pungently states: "If calculation were truly a problem, we would expect to see many prices that are too high. But if managers are capable of setting prices too low, why couldn't managers with better incentives (or perhaps managers with better intentions) set prices at market clearing levels?"²⁷ ²⁸

²⁶ The envisaged motivational transformation serves to eliminate any divergence between the private and social costs associated with the planner's allocative decisions, inducing the planner to care more for the total size of the social surplus rather than for the size of his own share in any surplus. See Buchanan (1962).

²⁷ Levy (1990, 218) and Shleifer and Vishny (1992, 237) provide evidence of the pervasive bias (prices set too low) that was characteristic of Soviet prices.

²⁸ Boettke (personal correspondence) responds that criticisms of socialist planning which planner agent-type miss their target relative to the Austrian critique of planning. Boettke argues that Mises's economic calculation argument precludes any possibility that public-spirited planners might allocate resources to maximize social welfare. Thus, planners allocate resources in accordance with political criteria, at which point, however, public-choice type considerations come into their own. Boettke's logic appears rather flawed. Given planner agent-type (*homo economicus*), political considerations (e.g., maximization of planner rents) take priority over any considerations of social welfare. The planners have very little interest in maximizing social welfare per se (unless, however, they possess some technology facilitating perfect rent extraction), even if they could actually do so. Their inability to calculate – or otherwise – is largely irrelevant: planners – given their agent-type – lack any incentive to "rationally organize production on economic grounds" (Boettke, personal correspondence). Contra Boettke, I contend that the socialist calculation argument takes on the role of 'second level' critique (given agent-type) of socialist planning. The monopoly objection to planning retains its strength irrespective of any possibility of socialist calculation. Planner agent-type is emphatically *not* that of *non-homo economicus*. Indeed, Mises explicitly posits the fixity of agent-type (*homo economicus*) in his attack on socialism (Mises 1981, 157). Remarkably, Boettke (1993, 90-91) cedes that policy "must first and foremost be incentive compatible with basic economic motivations. Policies that are based on notions of public spiritedness and humanitarian goals, but disregard economic motivations are most likely to be doomed to failure." Boettke and Leeson (2002a) ignore what Hayek had to say regarding the importance of agent-type as it applies to socialist planning: "... it would be wholly inconclusive if such a comparison were made between capitalism as it exists (or is supposed still to exist) and *socialism as it might work under ideal assumptions* – or between capitalism as it might be in its ideal form and socialism in some imperfect form. If the comparison is to be of any value for the question of principle, it has to be made on the assumption that either system is realized in the form which is most rational under the *given conditions of human nature* and external circumstances which must of course be accepted (Hayek 1935, 38, italics added). Thus, given Hayek's acceptance that analysis must proceed upon the acceptance of *given* human nature (agent-type), it becomes immaterial whether would-be socialist planners can actually engage in rational economic calculation or not. Irrespective of the possibility – or otherwise – of economic calculation under socialism, Hayek appears to cede that the principal relevant consideration is the fact that socialist planners lack any incentive to allocate resources such as to maximize social welfare. Indeed, given the assumption of *homo economicus* – or the "given conditions of human nature" as Hayek put it – quite the contrary is the case: planners will allocate resources to maximize their own personal well-being, irrespective of any deadweight losses that the resultant pattern of production and distribution might entail.

Market socialism and the Transparency of economic planning

From the vantage point of some 60 plus years later (not to mention the occurrence of the public choice revolution), market socialist models of price setting appear naïve in the extreme. Indeed, Lerner's (1944, 6) remarks that economic planners would "run society in the general social interest" and that economic planning would put an "end to monopoly throughout the economy" (Lerner 1944, 3)²⁹ epitomize the best-case theorizing that was so characteristic of the pro-planning side of the socialist calculation debate. Perhaps the sanguinity of the market socialist response to the 'planning equals monopoly' argument was the necessary consequence of their claim that socialist planning would render the workings of the entire economy wholly transparent.³⁰ The market socialists argued that democratic institutions were adequate to reign in any potential agency problems. Transparency allowed the populace to hold the planning authority accountable for the optimality – or otherwise – of its allocative decisions (e.g., Lippincott 1964 [1938], 34-35). Indeed, transparency allows the democratic assembly to monitor (and to replicate)³¹ the efficiency of the allocative choices made by the planners (see Feigenbaum and Levy 1996). The very transparency of the pure logic of choice under socialist planning serves to

²⁹ Levy (1990) puzzles as to why Lerner would fail to apply the insights that were drawn from his own model of monopoly to the case of socialist planning.

³⁰ "One fundamental difference between socialism and capitalism will be the existence of an authority able to view the economic system as a whole" (Dickinson 1939, 9). Several times, Dickinson states that socialist planning will make the economy operate, "as it were, within glass walls" (9, 20). Lippincott (1964 [1938], 19) favorably cites Dickinson, suggesting that the economy would operate "as it were, in a glass house in which all the details of the mechanism and its working could be followed". Durbin (1949, 50): "[A] centrally controlled economy will be an economy with *open eyes*." "The existence of a dual price system of consumers' goods could scarcely be concealed from the people, especially if there existed an institution (like the Workers' and Peasants' Inspection in the Soviet Union) giving to the rank and file citizen the right to pry into the bookkeeping and into the management of the community's resources" (Lange 1964 [1938], 96-97).

³¹ "It is possible to imagine a Supreme Economic Court whose function would be to safeguard the use of the nation's productive resources in accordance with the public interest" (Lange 1964 [1938], 98). See Tullock (1971), however, for a discussion of the divergence between the private and social costs of high-quality judicial decisions.

constrain the monopoly output solution – and the accompanying deadweight losses – squarely out of the picture. Imperfect information, however, weakens the constraint that democratic accountability otherwise imposes upon the planning authority. Despite the possibility for malfeasance on the part of the planning authority wherever imperfect information rears its ugly head, the market socialist writers failed to provide anything approaching an adequate solution to the agency problem created by the failure of the transparency assumption. Indeed, it was this market socialist evasion of the whole issue of incentive-compatibility which led Milton Friedman (1946, 405) to charge Lerner with preaching to the socialist state: “what at first reading sounds like a concrete proposal ... turns out to be simply an *admonition to the state that it behave correctly and intelligently*” (405), and moreover, that what “looks like a [policy] prescription evaporates into [little more than] an expression of good intentions” (413).¹²

Whilst Lange (1964, 92) recognized the possibility for a clash between the interest of the planning authority (themselves assumed the faithful and disinterested agents of society) and the self-interest of the managers of socialist enterprises, suggesting that the planning authority mitigate any such divergence by imposing a set of rules¹³ on managers that ensure “*efficiency in carrying out the plan*” (92), he failed, however, to adequately address whether or not adherence to these suggested rules was incentive-compatible from the perspective of an enterprise or industry manager (see Buchanan 1989, 21).¹⁴ Remarkably, whilst Lange had readily acknowledged that competitive markets provide adequate incentive for profit-maximizing entrepreneurs “to act much

¹² Lerner (1977, 238) cedes Friedman’s point: “I had originally given no attention to administrative problems, and had almost automatically pictured socialist society as some sort of universal government enterprise which would instruct all the managers, who would be government employees, to follow the marginal cost pricing principle.”

¹³ Lange suggests that the Planning Board impose the following rules upon enterprise managers: (1) choose the combination of factor inputs that minimizes average cost of production (2) select quantity to equate price to marginal cost. See Lavoie (1985, 118-122).

¹⁴ Hayek (1948, 196) assumes that Lange’s rules are incentive-compatible.

as they would have to act were they managers of production in a socialist system”, and that competitive markets enforce “rules of behavior similar to those [which would hold] in an ideal planned economy” (98), he failed to provide any reason as to why socialist institutions were adequate to mitigate the potential for managerial opportunism (see Lavoie 1985, 142-144). Despite recognizing that the allocative logic of markets and planning were characterized by a large degree of formal similarity, Lange simply averred that the welfare properties of markets and planning differed markedly: markets were plagued by monopolies (Lange 1964, 107-108, 120). Lange, however, failed to seriously address the possibility that socialist planning, by transforming the entire economy into one gigantic monopoly would exacerbate efficiency losses.³⁵

To my knowledge, H. D. Dickinson was the only market socialist writer to explicitly address the ‘planning equals monopoly’ critique of socialist planning. Despite recognizing that socialist planning necessitates the “socialist commonwealth” taking on the role of “sole employer and purveyor of goods,” Dickinson – like Hayek in 1944 – disavows any worst-case conclusions that one might draw, suggesting – again like Hayek in 1944 – that planners are sure to refrain from exercising their monopoly power “in the spirit of a monopolist under capitalism” (Dickinson 1939, 234). Dickinson invokes the role that democratic accountability in conjunction with the transparency of the socialist economy plays in ensuring that economic planning remains compatible with “libertarian socialism” (1939, 26).

³⁵ “On a competitive market the parametric function of prices results from the number of competing individuals being too large to enable any one to influence prices by his own action. In a socialist economy, production and ownership of the productive resources outside of labor being centralized, the managers certainly can and do influence prices by their decisions” (Lange 1964 [1938], 80-81).

Best-case theorizing: No sociology please, we're economists!

Every major participant in the socialist calculation controversy quite readily accepted that questions relating to planner agent-type had little – if any – relevance to the outcome of the debate.³⁶ The market socialist writers (e.g., Dickinson 1933, 240, 245; Lange 1964 [1938], 107) eagerly followed Barone (1935 [1908], 265-269) in assuming that the socialist planning authority would necessarily seek to maximize social welfare. The market socialists were rather loath to give serious consideration to ‘agent-type’ critiques of planning on the grounds that “sociological questions” (Lerner 1937, 267; Lange 1964 [1938], 109) regarding the incentive-compatibility or otherwise of socialist institutions (the rules of the game) were not the subject matter of economic theory (see Lavoie 1985, 143-144). Remarkably, it was Hayek (1935, 2-3), however, who had initially relegated incentive/agent-type objections to socialist planning to a position of subsidiary importance. Despite recognizing that such questions posed “real difficulties” (2) for socialism, Hayek – like Peter Boettke (personal correspondence) – downplayed their importance relative to the calculation issue, suggesting that incentive-related difficulties failed to “touch the heart of the problem” (2) with socialist planning: namely, the impossibility of rational economic calculation under socialism (Mises 1935).

Throughout the socialist calculation debate, Hayek was particularly wary of making any suggestion that the motivations of socialist planners were likely to prove anything other than public-spirited in practice (Levy 1990).³⁷ Might not such considerations, however, help us to

³⁶ To my knowledge, Frank Knight (1982 [1940], 154-195) was the only important exception to the generalization made in the text.

³⁷ “A proper understanding of the reasons which tend to incline so many of the intellectuals towards socialism is thus most important ... it is neither selfish interests nor evil intentions but mostly honest convictions and good intentions which determine the intellectuals views” (Hayek 1978 [1949], 184). Compare Hayek’s remarks with the view expressed by Frank Knight: “There is another aspect of socialism which is patent enough to any person of good sense (including economists) but which strangely enough is so generally overlooked that it may be mentioned. This is, *that in promoting socialism its devotees are seeking political power for themselves*” (Knight 1982 [1940], 162, italics added).

understand why Hayek lost the socialist calculation debate? Economists sympathetic to Hayek (e.g., Boettke 1997) would surely demur at this juncture: pointing instead to the fact that Hayek's pro-planning opponents myopically focused their attentions solely on the efficiency properties of equilibrium models. But surely any such focus, however, is equally the result of economists' best-case thinking. Where would-be planners are constrained to do nothing other than maximize social welfare why pay attention to anything bar the marginal conditions necessary for optimality? Despite the accuracy (or lack of such) of these speculations, however, I somewhat rather doubt that the socialist calculation debate might have concluded in any way other than it actually did: namely, with market socialist reigning supreme in the eyes of the economics profession (see, e.g., Lavoie 1985, 10-20). Indeed, I conjecture that best-case thinking had so strong a grip on the mindset of the economics profession during the 1930's that Hayek's defeat in the socialist calculation debate was – irrespective of the particular argumentative strategy (worst-case or best-case) that Hayek might have employed – something of an inevitability.

Conclusion

James M. Buchanan has made a justly famous career out of insisting (among other things) that economists maintain the assumption of motivational homogeneity when modeling private and public choices (e.g., Buchanan 1962). The acceptance of a posited motivational asymmetry, however, was the rule rather than the exception during the socialist calculation debate.³⁸ Do any market socialist objections to "theoretical dogmatism" (e.g., Durbin 1936, 678)

³⁸ To have suggested – in common with Frank Knight in the 30's and 40's, and Levy, Shleifer and Vishny in the 90's – that socialist planners were self-interested would have invited charges of engaging in amateur "sociological" (Lerner 1937, 267) or "psychological" (Durbin 1936) speculation of a decidedly dubious variety.

regarding planner agent-type, however, not cut with equal stringency against the prevalent motivational supposition that private choosers only seek to maximize profit?³⁹

We alluded earlier to Schumpeter's (1946, 270) suggestion that market socialist best-case thinking largely owes its origins to the "political sociology of J. S. Mill". Although Schumpeter sought to trace the prevalence of the benevolent-despot assumption in political economy to Bentham and the Mills, he simply failed to recognize the vitally important role that worst-case thinking played in Utilitarian 'constitutional' political economy. W. H. Hutt, however, in a sorely neglected contribution to the socialist calculation debate cut immediately to the chase: "politics has all the vices of entrepreneurship without its virtues" (Hutt 1940, 432). In common with Schumpeter, Hutt recognizes that models of socialist planning posit public-spirited planners. Unlike Schumpeter, however, Hutt takes the converse view of where Mill fits into the planning versus markets debate, suggesting that the insights of Mill are particularly apposite: "The crucial psychological assumption made by the orthodox is, we feel that which can be briefly summarised in J. S. Mill's terms: ""The influence of a sense of duty, or feelings of philanthropy (are) motives never to be exclusively relied on"" (Hutt 1940, 434).⁴⁰ Despite Hutt's timely reiteration of Mill's warning, however, the assumption of philanthropic planners reigned supreme throughout the socialist calculation debate.

³⁹ Durbin (1936, 678) states, "All difficulties [e.g., incentives] which are not accountancy [calculation] difficulties are not susceptible to theoretical dogmatism. "The calculations will not be made" ... [These] are not problems that the professor of economic theory is competent to discuss."

⁴⁰ Hutt cites Mill: "Although the actions of rulers are by no means wholly determined by their selfish interests, it is as security against those selfish interests that constitutional checks are required" (Hutt 1940, 434).

Best-case Thinking in Constitutional political economy:

Inducing moral aptitude or remaking agent-type?

“Since rule following behavior cannot be legitimately inferred from the existence of a published rule, the analyst must apply choice theory to explain the self-motivated actions that people are likely to take when confronted with the rules under consideration. As soon as a rule is proposed as a substitute for directly self-motivated action, such issues as how to distinguish compliance from disobedience, how to provide sanctions for disobedience and rewards for compliance, and the extent to which the desired actions can be articulated in explicit rules must be examined” (Don Lavoie 1985, 143).

“The constitutionalist insists on the study of rules because he seeks to include all the relevant constraints within the analysis. To leave institutional constraints out of account is no less analytically reprehensible than to assume away limits on the productive capacities of economic agents or to ignore basic scarcity constraints” (Brennan and Buchanan 2000 [1985], 20).

“Tell me not of checks on paper; but tell me of checks founded on self-love” (Patrick Henry 9 June 1788, in *The Complete Anti-Federalist*, Vol 5, Herbert Storing (ed.), University of Chicago Press, 1981).

Introduction

In the preceding two chapters we saw how the market socialists (e.g., Lange 1964 [1938]; Lerner 1944) readily engaged in best-case thinking when it suited their purposes. Are the market socialists, however, alone among political economists in resorting to best-case maneuvering? Gordon Tullock suggests, “the view that the government can be bound by specific provisions [e.g., constitutional constraints] is naïve. Something must enforce those provisions, and whatever enforces them is itself unbounded” (Tullock 1987, 317). F. A. Hayek – like Tullock, a highly distinguished classical liberal political economist – disagrees, suggesting that:

To limit power does *not* require that there be another power to limit it. If all power rests on *opinion* [Hume], and opinion recognizes no other power than one that proves its belief

in the justice of its actions *by committing itself to universal rules* (the application of which to particular cases it cannot control), the supreme power loses its authority as soon as it oversteps these limits (Hayek 1985 [1978], 93-94).

Hayek fails to really evade Tullock's challenge, however, for even if we are to accept the somewhat heroic assumption that the particular set of constitutional rules favored by Hayek provide a focal point (Schelling 1960) upon which public opinion readily coordinates, Hayek still appears to downplay the collective action problems that will surely hamper any attempt by the public to enforce the rules of the game (see, e.g., Olson 1965).

Although the Hayekian political economist might reply that surely the public can delegate the task of constitutional enforcement to some specialized agency, this answer likewise provides an inadequate reply to Tullock's pungent query (e.g., see Tullock 1971). Who is to monitor and constrain the actions of the enforcement agency? It would appear, that – at some ultimate level – it must be the public who enforces the constitutional rules of the game. Constitutional enforcement, however, is a pure public good (see, e.g., Bentham 1817; Cukierman and Meltzer 1986), and will surely fall prey to all the usual problems plaguing the attempted private provision of public goods. There is no good reason why we should expect this particular public good to be supplied in anything other than a sub-optimal quantity.

The Hayekian political economist appears to be caught between the potential Scylla of market failure (constitutional enforcement by the public) and the potential Charybdis of Leviathan (Brennan and Buchanan 2000 [1980]). Moreover, as recognized by Tullock (1971) high-quality judicial decisions are equally public goods. To suggest that a supreme court (or independent judiciary) would enforce the constitutional rules of the game in anything approaching an optimal fashion is to blithely ignore the divergence between the private and social costs of high-quality judicial decision-making. James M. Buchanan's remarks (changed

somewhat in order to illustrate the example of judicial decision-making) regarding the incentive-compatibility of market socialism are rather apposite:

[Even if] the problems of calculation [knowing the optimal set of wealth-maximizing judicial decisions] are disregarded, the [judiciary] ... will generate efficiency in results only if ... [judges] can be trained to make choices that do not embody the opportunity costs that they, individually and personally, confront (Buchanan 1999 [1969], 88).

Perhaps the citizenry will closely monitor the judiciary. Yet another public goods problem rears its ugly head. It ill becomes Hayek, or indeed, any other constitutional political economist, to invoke a supposition of public-spirited judges (or public-spirited citizens), particularly given their reluctance to accept the assumption of public-spirited socialist planners characteristic of the socialist calculation debate.

Intriguingly, Geoffrey Brennan and Alan Hamlin (2000) have recently charged public choice theory with readily indulging in its own particular variant of the benevolent-despot fallacy:

[T]o assume that the central bank, the courts, or any other institutional arrangement will prove superior to political processes on no sounder basis than the observation that political processes are imperfect is to avoid the basic question – in just the same way that assuming a benevolent dictator will solve problems of market failure avoids the basic question. In each case the basic question must be seen as the choice between feasible institutional alternatives, with feasibility understood to carry with it the presumption of some imperfection (Brennan and Hamlin 2000, 104).

I suggest that we read Brennan and Hamlin as alluding to the ‘contingently’ robust nature of constitutional rules (see chapter 1). Constitutional constraints necessarily rely on the populace (or some delegated agency acting at the behest of the populace) for their enforcement. To date, however, public choice theory has proven somewhat unwilling to pay heed to the important distinction between those institutions (or sets of rules of the game) which are characterized by non-contingent robustness and those which are characterized by contingent robustness (Tullock 1993).

The time consistency of choice behind the veil?

Constitutional political economy has traditionally – at least *prima facie* – treated the rules of the game and agent-type as substitutes for one another (see, e.g., Brennan and Buchanan 2000 [1980], 2000 [1985], xvi, 4, 36).¹ To what degree, however, can the rules of the game ever actually substitute for agent-type? If we treat the constitutional rules of the game as a type of non-contingently robust ‘physical’ technology, then clearly the rules of the game adequately substitute for agent-type on all relevant margins. There is little – if any – necessity to worry about the knavish proclivities of political agents given the nature of the rules of the game. Political knaves are simply unable to engage in opportunistic behavior. Suppose, however, that (as was argued to be the case in chapter 1) non-contingently robust institutions are simply unavailable. Any available constitutional constraints (or sets of rules of the game) are necessarily of the contingently robust variety. When the rules of the game are contingently robust, the relationship between rules and agent-type is more aptly characterized as one of complementarity (see, e.g., Macaulay 1829a; Mill 1998 [1861]; Elster 2000).

On what grounds ought we to expect that the rules of the game that are selected behind a Rawlsian ‘veil of ignorance’ (Rawls 1971) or ‘veil of uncertainty’ (Buchanan and Tullock 1962) will prove durable? Why are constitutional choices thought to be any more time consistent than are other non-constitutional choices? Why does some type of constitutional ‘weakness of will’ (Macaulay 1829a; Elster 2000) not serve to make the ex-ante optimal set of rules prove somewhat

¹ “Two broadly defined escape routes have offered hope to scholars and citizens through the ages. One of them is man’s capacity for moral improvement. People may, in a time to be, come to love one another ... The second possible avenue of escape from the “social dilemma” does not require that people become “better” in some basic moral sense. This approach starts with the empirical realities of persons as they exist, moral warts and all ... [H]ope emerges for sustainable social order through the appropriate design, construction, and maintenance of *rules* that set limits on the way in which each person is allowed to order his conduct toward others” (Brennan and Buchanan 2000 [1985], xvi).

sub-optimal ex-post? The problem of post-veil compliance appears intractable absent recourse to some type of best-case thinking.

A non-contingently robust institution would, of course, eliminate any possibility of time inconsistent constitutional choice (Kydland and Prescott 1977). The rules of the game – once selected – would necessarily prove binding for all future time periods. Irrespective of one's post-veil preferences or identity, the set of rules chosen ex-ante are necessarily rendered binding. Any possibility for post-veil opportunism is necessarily precluded by sheer analytic fiat. Constitutional political economy has to date, I suggest, tended to envisage constitutional rules in such non-contingently robust terms. Uncertainty as to one's exact post-veil identity, conjunct with the rational expectation that any chosen rules will prove durable (in result of their non-contingent robustness) in the face of any likely post-veil opportunism serves to induce agreement on a fair set of rules for the game (see Buchanan 1975). This suggests an intriguing paradox.

The expectation that the rules will prove durable does not appear rational. The very reason for selecting rules is to eliminate the possibility of post-agreement 'political' grabbing (e.g., rent-seeking behavior). Given the assumption of durability [**NCRI**], any rent-seeking activity appears somewhat pointless. Any potential rents have either already been subject to capture at the 'veil' stage (and thus, given NCRI are non-contestable) and are capitalized into post-veil asset values, or they can never be generated post-veil for any capture to occur. One possible way to escape the charge of paradox is to accept that the rules are contingently robust. Any such escape, however, comes at a price. While the contestability of rents (due to CRI) may serve to reduce up-front rent-seeking losses (see Sutter 1999), any such contestability surely serves to render constitutional enforcement somewhat more problematic.

With NCRI any rent-seeking activity takes place at the constitutional (veil) stage. There is no enforcement problem post-veil. In the case of CRI, however, rent-seeking occurs at both the

pre and post-constitutional stages (Buchanan 1987). The enforcement problem rears its head with a vengeance at the post-veil stage. Would agents that were quasi risk-averse (Brennan and Buchanan 1983) select rules over discretion at the constitutional stage? If NCRI, surely yes. If the rules are only contingently robust, however, then perhaps they would not. I have no definitive answer to offer, however, to either of these particular questions. While NCRI assumes away all problems relating to constitutional enforcement (the rules selected at stage 1 are binding at stage 2), the selected set of rules may prove to be hated by all citizens at stage 2. Does this possibility serve to shift any distributional conflict to stage 1? In the case of CRI, does the enforcement problem that emerges at stage 2 serve to make stage 1 largely irrelevant?

The Quality of the Constitutional Game: good rules or good players?

Brennan and Buchanan (2000 [1985], 167) have suggested that the quality of the players (agent-type) is of secondary importance to the quality of the constitutional rules of the game. Is this view correct? In some ultimate sense, I suggest that the quality of agent-type appears equally as important (if not more important) than the quality of the rules of the game. Presumably, the hands of a true knave are not easily bound by rules.

Constitutions are surely only as powerful as whatever particular type 'discretion' (human agency) actually stands ready to enforce their content (and which, of course, has the capability to actually do so). If the purpose of a rule is to constrain government discretion, then surely it is government discretion (of the wise and benevolent variety), rather than the rule per se, which provides any check against the misuse of discretionary power. True pre-commitment appears somewhat impossible. One's pre-commitment to a particular course of action is either the result of the state of nature (perhaps akin to a type of non-contingently robust institution), or of some other human agency. If the task of rule enforcement passes to another person, then it is still

human discretion that provides the potency (if any) of the particular rule. There appears to be no escape from the importance of agent-type.

Constitutional political economy and Ulysses: the myth of constitutional ‘mast and rope’

The Ulysses myth provides the masthead for the journal *Constitutional political economy*. Brennan and Kliemt (1990) have noted the incongruence between the journal's masthead and the subject matter that the journal addresses. They fail, however, to discuss what is surely the main difference between the two: the problem facing Ulysses cannot really be characterized as a public goods problem. The rules that are favored by constitutional economists will only tie Leviathan's hands if they are enforced by the public or by some agency acting at the public's behest. Enforcement of the constitutional contract is a public good (Cukierman and Meltzer 1986). Given the *homo economicus* (or worst-case) assumptions of constitutional political economy, we should expect this particular public good to be supplied in a less than optimal quantity. No single individual has any real incentive to take part in the costly task of constitutional enforcement. Given the worst-case axioms of constitutional economics, to invoke public spiritedness or benevolence as a means to explain such enforcement is surely far from satisfactory. Worst-case thinking appears paradoxical (Macaulay 1829a): rules are necessary to prevent disaster, yet such rules, however, can only prevent disaster when the possibility of any such outcome is very unlikely (i.e. when worst-case assumptions do not accurately describe the state of the world). Although constitutional political economy seeks to maintain that the character of the agents who hold political office is of little matter for the quality of policy, this appears – at least *prima facie* – somewhat inaccurate. Constitutional political economy does not eliminate best-case thinking, but rather (I suggest), simply relocates ‘politics with romance’ to the constitutional level.

The constraints that bind Ulysses (the physical technology of rope and mast) once implemented are non-contingently robust. Once bound, Ulysses remains bound (assuming his crew do not release him). Constitutions, however, are not made of physical stuff *per se* (Elster 2000; Boettke 2001). A written constitution, when considered as parchment or paper has no power to constrain anyone. When considered, however, as a focal point (Macaulay 1829a) around which resistance to tyranny may coalesce, such parchment may prove sufficiently strong to bind the hands of any ruler. Moreover, Ulysses is the sole recipient of the pay-offs (negative or positive) that result from the success or failure of the constitutional technology (rope and mast) relevant to his particular choice situation. The stylized example of the Ulysses story fails to adequately reflect the fact that team production is a vital input into the production of constitutional enforcement. William Forster Lloyd (1837) accurately captures the essence of the public goods problem that is characteristic of large-scale team production:

Suppose the case of two persons agreeing to labour jointly, and that the result of their labour is to be common property. Then, were either of them, at any time, to increase his exertions beyond their previous amount, only half of the resulting benefit would fall to his share; were he to relax them, he would bear only one half the loss. ... Similarly, in the case of three partners, they [the incentives to increase one's efforts] would have only one third the force – in the case of four, only one fourth – and in a multitude, no force whatever. For beyond a certain point of minuteness, the interest would be so small as to elude perception, and would obtain no hold whatever on the human mind. ... Each person will view the future consequences, expected to result from an increase or relaxation of his exertions, in the same light as he would any other benefit or injury extending indifferently to the whole community (William Forster Lloyd 1837, 18)

Indeed, Brennan and Kliemt (1990) themselves are fully cognizant of the limitations of the Ulysses myth:

It is one thing to show the rationality of Ulysses' actions, given the assumption that the technology of rope and mast is available and unproblematic. But this assumption effectively sweeps away all questions that relate to the enforcement and maintenance of the rules. ... [T]here is no *external* technology available that is totally effective (or that is not excessively costly): there is no mast, no rope. The tools of enforcement and maintenance must themselves be *socially* constructed – or to use the language of the British moralists, those tools are not *natural* but *artificial* (Brennan and Kliemt 1990, 126).

The central concerns of constitutional political economy (Brennan and Kliemt 1990, 127) are the “selection of rules” that are to apply for future “plays of the game” and the “devising of arrangements to enforce such rules” (127). To date, however, constitutional economists have devoted much analytical effort to the first of these concerns (the selection of rules). Far less effort, however, has been expended on addressing the more problematic question of constitutional enforcement. How many articles in the journal *Constitutional Political Economy* seriously address the enforcement problem? Perhaps even more puzzling, the term “constitutional enforcement” fails to make an appearance in J. M. Buchanan’s *Collected Works*.²

Constitutional Economics and the Katallactic Paradigm

The simple Buchanan-Tullock model of anarchy (Buchanan 1975; Tullock 1972) envisages two agents engaging in mutually advantageous exchange in the state of nature. Each party to the initial constitutional contract agrees to desist from predatory behavior in exchange for a similar undertaking from the other party (Bush 1972). Because time consistency problems – the incentive to renege ex-post – rear their ugly head (Levy 1992) – thereby causing the agreement to collapse and the situation to revert to the sub-optimal anarchic equilibrium – all relevant parties to the contract have a mutual interest in the appointment of a third-party enforcer charged with the task of endowing the contract with a modicum of durability. The original time consistency problem is only solved, however, at the price of creating a new problem: That of ensuring that the

² I ran a search of Buchanan’s *Collected Works* on the Liberty Fund website. Buchanan is, of course, fully aware of the difficulties of constitutional enforcement. See, e.g., Brennan and Buchanan (2000 [1985], xvi, 7, 160-161). “There is ... one *crucial assumption* which clearly underlies the whole constitutional construction – that of *enforceability*” (Brennan and Buchanan 2000 [1980], 13, italics added).

third-party enforcer sticks to the terms of the revised constitutional contract.³ Perhaps the two original agents can enforce their wishes (as principals) upon the potentially recalcitrant agent (Weingast 1995). The transactions costs associated with mutual action are surely not prohibitive in the two-party case. As we add more people to the story, however, we create a large-numbers prisoners' dilemma problem. Provision of the public good of constitutional enforcement surely becomes more problematic in this case.

Gordon Tullock (1993) has suggested that by far the most difficult question facing public choice theorists is that of designing a self-enforcing constitution. A memorable example of such a constitution (set of rules) is provided by the classic 1967 war movie *The Dirty Dozen*. The hapless 'Dozen' (12 convicted military prisoners, many of whom face the death penalty) are given the opportunity to volunteer for what amounts to virtually a suicide mission. Those willing to accept this dangerous undertaking are told that their training will take place under a regime of rules (or constitutional contract) providing for a set of pay-offs characterized by generality (Buchanan 1993). Constitutional political economists, of course, envisage any such generality of pay-offs (Buchanan's generality norm) as eliminating the perennial lure of the off-diagonal pay-offs. The Dozen are informed that escape by any prisoner from the training camp, or any actions that potentially jeopardize the success of the mission will ensure that all twelve convicts are immediately returned to prison for immediate execution of sentence. Many of the Dozen face the death penalty, the remainder – thirty years or so of hard labor. All twelve prisoners have the same preference ranking for the potential pay-offs: Life – or more accurately, a chance of life equal to the probability of surviving the mission – is preferable to the certainty of death (by hanging) or 30 plus years. Each member of the 'Dirty Dozen' has a somewhat positive incentive to monitor and

³ "Once established as sovereign, government may not willingly remain within the limits of its initially delegated authority" (Brennan and Buchanan 2000 [1985], 31).

– where necessary – enforce their mutual adherence to the terms of the ‘constitutional contract’. Although there clearly are incentives for each prisoner to free-ride on the enforcement activities of the other prisoners, the problem is surely not insurmountable. Indeed, the judicious application of violence against a would-be escapee (Victor Franco) ensures the durability of the agreement. In the case of twelve agents, the problem is clearly soluble. Had the number involved been far larger, however – perhaps the ‘Dirty Twelve Million’ – and the contract would surely have proven far more vulnerable to opportunistic behavior on the part of each prisoner.

Best-case Thinking: Does Constitutional Political Economy Stack the Deck in its Favor?

Table 1 below assumes that non-contingent robustness [NCRI] characterizes the rules of the game. Rules are superior to Discretion. The expected pay-off to [R] is -0.6 . The expected pay-off to [D] is -1.3 . Table 2 assumes that contingent robustness [CRI] characterizes the rules of the game. Rules are no longer superior to Discretion. The expected pay-off to [R] is -2.4 . The expected pay-off to [D] is -1.3 .

Table 1: Non-contingently robust rules

<i>State of the World</i>	<i>(P)</i>	<i>Rules</i>	<i>Discretion</i>
WCT	0.7	0	-4
BD	0.3	-2	5

Table 2: Contingently robust rules

<i>State of the World</i>	<i>(P)</i>	<i>Rules [NCRI]</i>	<i>[CRI]</i>	<i>Discretion</i>
WCT	0.7	0	-3	-4
BD	0.3	-2	-1	5

Table 3: Equal probability of contingent and non-contingent rules

<i>State of the World</i>	<i>(P)</i>	<i>Rules [NCRI]</i>	<i>[CRI]</i>	<i>Discretion</i>
WCT	0.7	0	-3	-4
BD	0.3	-2	-1	5

Table 3 assumes that the probability that NCRI characterizes the rules of the game is equal to 0.5. The probability that CRI characterizes the rules of the game likewise equals 0.5. Rules are no longer superior to discretion. The expected pay-off to [R] is -1.5 . The expected pay-off to [D] is -1.3 . While public choice theory views itself as akin to the study of politics without romance, constitutional political economy is simply the study of politics with the romance allowed into the analysis at a higher level (Tullock 1971, 1993). What incentive does a judge (or a representative citizen) have to enforce the constitutional rules of the game?

Table 4 assumes that contingent robustness characterizes the constitutional rules of the game. The rules are ultimately subject to enforcement by a Supreme Court judge (or body of judges). The judge is one of two agent-types: a knave (*homo economicus*) or an angel (*non-homo economicus*). Knaves, of course, never enforce the rules of the game. Angels, by contrast, always do so. There is an equal probability (0.5) that the judge is an angel or a knave. Do rules trump discretion? No, discretion is superior to rules. The expected pay-off to [R] is equal to -1.5 . The expected pay-off to [D] is equal to -1.3 .

Table 4: Contingently robust constitutional rules

<i>State of the World</i>	<i>(P)</i>	<i>CRI [knave]</i>	<i>[angel]</i>	<i>Discretion</i>
WCT	0.7	-3	0	-4
BD	0.3	-2	-1	5

Suppose, however, that the worst-case axioms of constitutional political economy were accurately descriptive of the state of the world with a probability equal to 0.95 or 1. Rules would only prove superior to discretion if we temper our worst-case model with a best-case assumption somewhat akin to that provided by the public-spirited ‘Supreme Court’ judge invoked in table 4. The benevolent-despot assumption (so despised by public choice theory) appears necessary at some stage in a constitutional model (Brennan and Hamlin 2000).

The Dirty Dozen and James Madison: virtue or violence?

In the example of the Dirty Dozen (1967) we saw how the judicious application of violence endowed the generality ‘contract’ into which the Dozen had entered with sufficient robustness to eliminate the lure of the off-diagonal pay-offs (escape). The contract was robust against even the malfeasance of a louse like Victor Franco (memorably portrayed by John Cassavetes). Violence – or the threat of violence – made the contract robust in the small numbers case (even in the example of the Dirty Dozen, however, we must remain aware of the benevolent-despot – the justice system and weaponry of the US military machine – that lurked backstage the entire time). In the large-numbers case, however, it would appear that what we might term ‘constitutional virtue’ is more potent than the threat of violence (Macaulay 1829a; Mill 1998 [1861]). James Madison recognized the necessity of a virtuous citizenry for the success of the Federalist experiment (see Brennan and Hamlin 2000). Agent-type is all-important. The public is the ultimate enforcer of the constitutional rules of the game (Macaulay 1829a; Mill 1998 [1861]). Perhaps Madison’s “virtue” is akin to what Buchanan refers to as a “constitutional attitude”.

The best example of a self-enforcing ‘constitution’ – like the tale of the Dirty Dozen – is provided by military history. The military ‘square-formation’ was used to great success during the Napoleonic wars (see, e.g., Weller 1967; Brennan and Tullock 1982). The ‘square’ provides a

structure of incentives adequate to ensure that no soldier in the formation has any interest whatsoever in deviating from the jointly optimal strategy path: standing one's ground to receive a charge by enemy cavalry. The square formation serves to mutually align the interests of every single member of the square. To remain in formation is to effectively guarantee that one and all survive an enemy cavalry charge unscathed. To break formation, however, is to virtually ensure one's death. The ingenuity of the square lies in its capacity to deftly short-circuit the logic characteristic of a large-numbers prisoner's dilemma game. The square creates a generality of potential pay-offs, thereby eliminating the lure of the off-diagonal pay-offs characteristic of the usual clash between individual and collective rationality. The square aligns individual interest with collective interest (at least against cavalry). Moreover, the genius of the formation is that it allows one to solve one's own prisoner's dilemma type situation while simultaneously creating a similar dilemma for the enemy cavalry. The collective interest of the enemy horse lies in breaking the square. Individual rationality, however, dictates that any single cavalryman refrain from charging home to certain death. Although the square, once in formation, is effectively unbreakable by horse, agent-type is still of the utmost importance. A poor quality officer will give the order to form square too late (if at all), or will order the troops comprising the square back into line (suicidal against cavalry) far too early. Quatre Bras and Waterloo provide the most famous examples of the terrible costs in dead and wounded wrought by an officer (e.g., the Prince of Orange) of poor agent-type (see, e.g., Weller 1967; Cornwell 1995).

Although a square was highly robust against enemy horse, every soldier feared to be caught in square while under fire by enemy artillery. While in square at Waterloo (1815), the ranks of the Inniskilling regiment were decimated by Bonaparte's guns (Weller 1967; Cornwell 1995). There are equally examples, however, where a cavalry charge successfully broke a square. The most famous example of such an occurrence is drawn from the Battle of Garcia-Hernandez in

1812, where the momentum of a single wounded horse and dead rider (the dead are notoriously immune to the lure of the off-diagonal) of the Kings German Legion (Von Bock's dragoons) was sufficient to crush the face (side) of a French infantry square, thereby allowing KGL dragoons to stream into the square en-masse and 'gut' it from the inside-out (Chappell 2000, 37-39).

A major reason for the advocacy of constitutional rules is the desire to eliminate the perennial lure of the off-diagonal pay-offs (Buchanan 1993). The desideratum of constitutional political economy is a set of self-enforcing constitutional rules; a set of rules, the enforcement of which will themselves prove immune to the lure of the off-diagonal pay-offs associated with free-riding or other forms of non-cooperative behavior. A recent episode of the popular television drama *The Sopranos* (the story of the trials and tribulations of a New Jersey Mafia boss) provides an excellent example of how a player in a potentially non-cooperative game can exercise strategic choice over the rules of the game such as to make the co-operative outcome far more probable. Thomas Schelling (1960, 44) famously argued that despite the presence of incentives (e.g., the potential time inconsistency of a promise) to renege on an agreement or promise, a credible and self-enforcing promise might make the agreement de facto enforceable. Schelling provides the example of a kidnapper who would like to release his hapless victim but recognizes that the victim will immediately turn the kidnapper into the police upon release. If the victim, however, had previously committed an act "whose disclosure could lead to blackmail, he may confess it [to the kidnapper]; if not, he might commit one in the presence of his captor, to create the bond that will ensure his silence" (Schelling 1960, 44). The victim's susceptibility to future blackmail serves to eliminate (or drastically temper) the ex-post incentive – the lure of the off-diagonal pay-off – to report the kidnapper to the police. In similar fashion, Tony Soprano attempts to manipulate the future pay-offs resultant upon the potential strategy choices made by his criminal associates. In particular, Soprano recognizes the all-too real possibility that he might face a

prisoner's dilemma type situation at some future date. Soprano is equally aware of the fact that any one of his current associates might potentially testify against him in the future to save themselves from criminal charges (making it too dangerous to operate his business directly). Thus, Soprano decides that in future he'll issue orders only through a "blood relative": His wife's nephew – Christopher Moltisanti.⁴ To that end, Tony provides Moltisanti with the home address of Lt. Detective Barry Haydu (the 'dirty cop' who – on contract to another Mafia family – executed Moltisanti's father). Moltisanti subsequently executes Haydu. Tony effectively manipulated Moltisanti's choice set to eliminate the lure that any potential future off-diagonal pay-off (e.g., a promise of immunity from prosecution – or 'disappearance' into the Federal witness protection program – in exchange for testifying against Tony) might – should the ties of family prove far too weak to ensure his silence – provide to Christopher Moltisanti. Like Schelling's kidnap victim, Moltisanti posts a 'bond' eliminating any incentive to engage in ex-post opportunism.

In all of the examples above, of course, the pay-offs are largely privatized (and hence, privately appropriable).⁵ The enforcement of constitutional rules, however, is a public good. Brennan and Buchanan pungently note: "What is the constitutional equivalent of the patent law

⁴ As Tony puts it: I want to "bond him to me inseparably." Presumably, any such bonding will create an as-if interdependence of utility functions and generality of pay-offs. See Hume (1998).

⁵ I conjecture that monetary and approbational pay-offs complemented one another to provide adequate incentives for diligence on the part of officers during the Napoleonic wars. I conjecture that the "purchase" system – whereby one could purchase any rank in the British army below that of Major – helped to privatize the pay-offs associated with victory (a public good surely to the army writ large): the potential price at which one's commission might sell was largely a function of the "glory" associated with one's regiment. The siege and fall of Seringapatam (May 1799) provides a useful example of the incentives for victory provided by the opportunity to engage in looting: "Wellington ... stamped out the looting in the city (he hung four looters, a remedy he would employ in the wake of future sieges), but what the common soldier could not take, the senior officers happily plundered for themselves. The East India Company's Prize Agents tallied the Tippoo's treasures at a value of two million pounds (1,799 pounds), and half of that fabulous fortune was declared to be prize money, so that many senior officers became rich men through that single day's work" (Cornwell 1997, 485–486).

... [which] offers incentives for creative effort by all potential inventors? What is the *political-constitutional equivalent of entrepreneurial profits ...?*" (Brennan and Buchanan 2000 [1985], 160).

Constitutional rules of the game: non-contingent physical technology?

Throughout this paper I have repeatedly suggested that constitutional political economists appear to envisage that the rules of the game are somewhat akin to a non-contingent enforcement technology.⁶ The rules of the game are viewed as somewhat akin to a type of non-contingent "constitutional insurance": "Rules may be chosen that place limits on extremes, even at some accurately reckoned cost in value. *We need not predict that each child will fall off the cliff to justify the installation of railings.* Minimax is descriptive of deeply felt human precepts of rationality. We seek to ensure that the best remains a potentiality by guarding against the worst" (Brennan and Buchanan 2000 [1980], 240, italics added). Railings at the edge of a cliff, however, are most emphatically a non-contingent physical technology. A more accurate analogy for constitutional rules, perhaps, would rather be to view the railings at the edge of a cliff as contingent 'railings'. Railings of this type are not physical, made not of steel or iron, but of light (through which no child can pass). Moreover, assume that such light beams are generated by an

⁶ Boettke's excellent study of the Soviet experience (1990, 131) treats the rules of the game as somewhat akin to a machine. Lenin attributed Soviet economic chaos to problems of agent-type: "In the present situation the *key feature is people, the proper choice of people*" (Lenin cited in Boettke 1990, 131). Boettke states, "Lenin subscribed to a variant of the benevolent-despot theory of socio-economic organization ... Lenin was like a manager of a bottle-processing plant who after discovering that the bottles are coming out only half filled with soda pop decides he should change the bottles rather than fix the machine. *It was the machine, that is, the rules, that needed to be fixed, not the people*" (Boettke 1990, 131, italics added). J. S. Mill's remark that in "politics as in mechanics, the power which is to keep the [constitutional] machinery going must be sought for outside the machinery" (Mill 1998 [1861], 182) is particularly apposite. Moreover: "[The] good qualities [of the populace] supply the moving force which works the [political] machinery". Furthermore, the constitutional machinery "has to be worked by men, and even by ordinary men" (Mill 1998 [1861], 207). Boettke (1992) provides an excellent study of the difficulties that poor-quality agent-type poses for economic reform.

underground machine, the power for which comes through wires that are attached to an exercise cycle located in the basement of every home in the land. In order for the machine to work, a certain number (a minimum threshold if you like) of citizens have to pedal their exercise cycles to generate the requisite amount of power. Provision of the power generating the activation of the contingently robust 'constitutional' railings takes on the characteristics of a public good.

Prudence and Virtue: Complements or Substitutes?

Does it all come down to agent-type (wise and benevolent people)? Macaulay is skeptical of the claim that the rules of the game provide an adequate substitute for agent-type:

"Constitutions are in politics what paper money is in commerce. They afford great facilities and conveniences. But we must not attribute to them that value which really belongs to what they represent. They are not power, but symbols of power, and will, in an emergency, prove altogether useless, unless the power for which they stand be forthcoming" (Macaulay 1978 [1829], 207).

Constitutions may serve as focal points, thus facilitating the coalescence of public resistance to tyranny, but still, at least for T. B. Macaulay, constitutional enforcement is always dependent upon human agency. Without any public willingness to enforce the rules of the game the constitution will fail to prevent the abuse of power:

Which is the better able to defend himself; - a strong man with nothing but his fists, or a paralytic cripple encumbered with a sword which he cannot lift? Such we believe, is the difference between Denmark and some new republics in which the constitutional forms of the United States have been most sedulously imitated (Macaulay 1978 [1829], 206-207).

"It is evidently on the real distribution of power, and not on *names and badges*, that the happiness of nations must depend. ... That certain men have been chosen as deputies of the people, - that there is a piece of paper stating such deputies to possess certain powers, - these circumstances in *themselves* constitute no security for good government" (Macaulay 1978 [1829], 206).

Consider our earlier distinction between contingently robust and non-contingently robust institutions (or sets of constitutional rules of the game). David Hume (perhaps the intellectual father of constitutional political economy) has some rather interesting things to say regarding the 18th century disputes between the Court party (Tories) and the Country party (Whigs) which pertain to our distinction:

Is our constitution so excellent [NCRI]? Then a change of ministry can be no such dreadful event; since it is essential to such a constitution, in every ministry, both to preserve itself from violation, and to prevent all enormities in the administration. Is our constitution very bad [neither NCRI nor CRI]? Then so extraordinary a jealousy and apprehension, on account of changes, is ill placed; and a man should be no more anxious in this case, than a husband, who had married a woman from the stews [a prostitute], should be watchful to prevent her infidelity. Public affairs, in such a government, must necessarily go to confusion, by whatever hands they are conducted (Hume 1985 [1741], 178).

Where any “change of ministry can be no such dreadful event,” the constitution can aptly be considered as non-contingently robust: the rules of the game are effectively self-enforcing. Such constitutional machinery ensures that we have no need to worry about the potential misuse of political power, for any such abuse simply cannot occur. Should, however, the constitution prove “very bad,” there is really little hope of any welfare-enhancing reform of the rules of the game. For how is such reform supposed to come about if not through the channel of regular in-period politics: “How are the rules of the game to be changed while the game continues to be played under the old rules?” (Buchanan 1977, 298).

Remaking agent-type?

Does best-case thinking in political economy – whether of the market socialist or constitutional political economy variety – ultimately converge on the question of agent-type? Intriguingly, James M. Buchanan (1977, 12), though a self-proclaimed “philosophical anarchist” (1977, 11), has overtly sought to distance his own worst-case philosophy of constitutional

political economy from the best-case thinking that he views as characteristic of libertarian anarchist writers (e.g., Rothbard 1996): “My practical society ... moves one stage down from the ideal [anarchy] and is based on the presumption that individuals could not attain the *behavioral standards* required for such an anarchy to function” (Buchanan 1977, 11, italics added).⁸ In recognition of this “frailty in human nature,” individuals would agree to “enact laws, and to provide means of enforcement” (1977, 11). Buchanan’s apparent insistence (at least *prima facie*) that the rules of the game can adequately substitute for agent-type is illustrated by his analysis of a ‘Two-Stage Utopia’ (Buchanan 1977, 11-12). Buchanan suggests that the feasibility of ‘Stage 1’ order (idealized anarchy) necessitates the remaking of agent-type – some “modification of human nature” is requisite (1977,12).⁹ David Hume’s famous remark that all “plans of government which suppose great reformation in the manners of mankind, are plainly imaginary” (Hume 1985, 514) is particularly apposite to free-market anarchy. The attainment of ‘Stage 2’ order (government constrained by constitutional rules of the game), by contrast, only requires a change in the rules of the game (institutions).¹⁰ Despite any *prima facie* appearance of treating the

⁸ “In some ultimate sense, anarchy must always represent a utopian ideal for anyone who places a high value on freedom of the individual ... Human nature, as we observe it or even as we might imagine it, forces us to allow both for the emergence of conflicts among claimants and for violations of acknowledged claims. Reality requires that we reduce our sights, even when discussing first-best institutional arrangements, and discard anarchy as a self-sufficient organizing principle” (Buchanan 1977, 288). Buchanan (1979, 273) suggests the incongruence of anarchy with public choice theory: “We can, I think, dismiss the anarchist position readily, whether this be the romantic or the libertarian variety. Public-choice theory deals with persons as utility-maximizing beings, not as disembodied spirits full of love, or even as mindful of each other’s “natural boundaries”” (Buchanan 1979, 273). “The libertarian anarchists who dream of markets without states are romantic fools, who have read neither Hobbes nor history” (Buchanan 1979, 283). “At the opposing end to socialism on the imagined ideological spectrum stands the equally romantic idea of *laissez faire*, the fictional image of the anarcho-capitalists, in which there is no role for the state at all ... It is as difficult to think systematically about this society as it is to think of that society peopled by the “new men” of idealized communism” (Buchanan 2001 [1989], 244).

⁹ “[T]he fundamental character traits [agent-type] of human beings either cannot be, or should not be, manipulated deliberately” (Buchanan 1977, 12).

¹⁰ “It is folly to think that “better men” elected to office will help us much, that “better policy” will turn things around here. We need, and must have, basic constitutional reform, which must of course be preceded by basic constitutional discourse and discussion” (Buchanan 1979, 181).

rules of the game and agent-type as adequate substitutes for one another. Buchanan readily recognizes the possibility that agent-type might preclude the efficacy of the rules of the game: “what happens if I should be forced, however reluctantly, to the presumption that individual human beings, as they exist, are not and may not be capable of taking on ... [the] requisite constitutional attitudes?” (12).¹¹

Buchanan suggests that if the populace proves clearly “incapable of adopting the requisite set of constitutional attitudes,” (1977, 12-13) they are *prima facie* “incapable of evaluating their long-term interests” (13). In other words, the public is somewhat reluctant to engage in non-convex optimization (see Levy 1992): unwilling to give up their current rents in exchange for a higher pay-off at some future date. At this juncture, Buchanan readily cedes that libertarian anarchist and constitutional political economist face the same analytical dilemma (Buchanan 1977, 14). Does the empirical realization (and long-run viability) of any idealized classical liberal political economy (of whatever stripe) ultimately necessitate – just like socialist planning – the remaking of agent-type?

Levy (1992) provides an account of Samuel Taylor Coleridge’s infatuation with Pantisocracy that is highly pertinent to Buchanan’s dilemma. Coleridge argued that to eliminate vice from the world it was necessary to change institutions (the set of incentives). In particular, Coleridge advocated the abolition of property, an institution that was “beyond doubt the Origin of all Evil” (see Levy 1992). Despite an early adherence to the spirit of philosophic-materialism characteristic of classical political economy (see, e.g., Levy 1992, 217-218),¹² Coleridge came to

¹¹ “In this case, my treatment of an idealized constitutionalist-contractarian social order becomes neither more nor less defensible than the discourse of those who go all the way and treat genuine anarchy as an ideal” (Buchanan 1977, 12).

¹² “Only in so far as we can assume that human beings will be essentially the same [in the future] as in the known past under the same conditions, and will vary in the same way under different conditions, can we infer anything whatever about behavior after any change in conditions” (Knight, 1938a, p.245). “If

recognize the somewhat problematic nature of the ‘bootstrapping’ apparently inherent to any attempt at altering the structure of incentives: poor quality institutions (rules of the game) inescapably lead to corrupt individuals, at the same time, however, those very same individuals are thought to possess a degree of public-spiritedness sufficient to change the rules of the game for the better. As Levy recognizes, Coleridge faces Archimedes problem: to move the world, one must stand outside the world (Levy 1992, 218).

Best-case Thinking: making facts bend to systems or making systems bend to facts?

J. S. Mill thought the creation of a new social morality (one somewhat akin to Buchanan’s “constitutional attitude” perhaps)¹⁵ preaching the virtue of social unity an absolute prerequisite if large-scale experiments with ‘libertarian-communist’ institutions were to prove successful (Levy 1992). Such a moral code would place great emphasis on the second condition of Hume’s theory of property (1741): general benevolence towards other creatures (see, e.g., Levy 1992). With the interdependence of utility functions engendered by the new morality, property could be owned in common and managed for the common good: “whenever it ceases to be true that mankind as a rule prefer themselves to others and those nearest to them to those more remote, from that moment Communism is not only practicable, but the only defensible form of society; and will when that time arrives, be assuredly carried into effect” (Mill 1998 [1861], 208-209).

this [not] be the case, there is at once an end of all human science. The whole train of reasonings from effect to causes will be destroyed ... The wildest and most improbable conjectures may be advanced with as much certainty as the most just and sublime theories, founded on careful and reiterated experiments. We may return again to the old mode of philosophising and make *facts bend to systems, instead of establishing systems upon facts*” (Malthus, 1972).

¹⁵ “Without a shared “constitutional mentality,” without some initial common ground from which discourse can proceed, all argument on design comes to naught” (Brennan and Buchanan 2000 [1985], xviii). “But even with some requisite constitutional wisdom, how can reform surmount identifiable self-interest?” (Brennan and Buchanan 2000 [1985], xix).

Mill thought that moral education might serve to engender the requisite transformation of agent-type, serving to remake humanity somewhat more in the image of Harriet Taylor.¹⁴ Moral education, suitably complemented by a set of non-monetary incentives – a vector of approbational shadow prices associated with different types of behavior – would operate to induce each individual to behave as if their agent-type was more akin to that of Harriet Taylor than *homo economicus*. Mill's posthumous *Chapters on Socialism* (1967 [1879]) make quite clear Mill's awareness of the difficulties with which any attempt at remaking humanity in Mrs. Taylor's image is fraught: Mankind is characterized by a highly imperfect degree of moral cultivation (1967 [1879], pp.739-740).¹⁵ The use of moral education as a policy variable with which to engineer the requisite transformation of society faces the following dilemma: the future generation of mankind is necessarily educated by the present (and highly imperfect) generation of mankind. At this juncture, the Coleridge problem (Levy 1992) rears its ugly head: though one apparently needs to remake mankind prior to remaking society, how does one propose to remake mankind when mankind is intrinsically a part of the very society that one thinks is in urgent need of transformation?¹⁶

¹⁴ "The result of our review of the various difficulties of Socialism has led us to the conclusion ... [that such institutions] are at present workable only by the *elite* of mankind, and have yet to prove their power of training mankind at large to the state of [moral] improvement which ... [such institutions] presuppose" (Mill 1967 [1879], 748).

¹⁵ Macaulay had raised the following objection to Utilitarianism some 50 years earlier: "[Mr. Bentham] should reflect that the whole vast world of morals cannot be moved, unless the mover can obtain some stand for his engines beyond it. He acts as Archimedes would have done, if he had attempted to move the earth by a lever fixed on the earth" (Macaulay, 1978 [1829], p.176). Intriguingly, Buchanan states, "I cannot as [Frank] Knight suggests, move the world unaided, and it is morally arrogant of me to imagine myself in a position of power sufficient to enable me to act unilaterally" (Buchanan 1992, 149).

¹⁶ In a letter to Harriet Taylor (21 March, 1849) Mill had written: "I cannot persuade myself that you do not greatly overrate the ease of making people unselfish. Granting that it 'ten years' the children of a community might by teaching be made 'perfect' it seems to me that to do so there must be perfect people to teach them" (Mill 1965 [1849], 1030).

In light of the utmost seriousness with which Mill treats the question of agent-type and the incentive-compatibility (or otherwise) of the rules of the game (institutions) it is all the more remarkable that Ludwig von Mises (a great classical liberal political economist) would repeatedly disparagingly refer to Mill as “the great advocate of socialism” (Mises 1985 [1927], 195). Moreover, Mises appears somewhat more vulnerable to the charge of engaging in flagrant best-case theorizing than does Mill: “Liberal social philosophy ... showed that by maintaining and developing the social bond each individual serves his highest interest, so that the sacrifices made in the fulfillment of social life are only temporary one’s. *He exchanges a smaller direct advantage for considerably greater indirect advantage. Thus duty and interest coincide. This is the meaning of the harmony of interests of which the liberal theory of society speaks*” (Mises 1981, 363, italics added).¹⁷ Mises appears to leave himself wide-open to the same type of charge (incentive-incompatibility) as that which T. B. Macaulay leveled at the Greatest Happiness Principle (the hapless T. Perronet Thompson in particular) during the Mill-Macaulay debate.

The question of agent-type is of particular importance for the political economy of the transition process (whether the suggested transition is from ‘planning to markets’ or from ‘the rent-seeking society’ to the ‘constitutionally constrained polity’): If socialist planners are public-spirited they ought to readily admit that planning was a mistake. Thus, the switch from planning to markets ought to prove a relatively non-bitter pill to swallow: The switch is posited as leading to an increase in social efficiency (by supposition the desideratum of the planners). If the planners are not public-spirited, however, the transition process is fraught with difficulty (see, e.g., Tullock 1975). Planners of the non-public-spirited variety will seek to maintain their existing share of any realized economic surplus. The suggested economic reforms, however, although increasing the

¹⁷ Levy (1992) documents the important role played in the history of economics by the best-case assumption that people have – or ought to have – a discount rate equal to zero. Mises (1966, 363, 674) falls horribly foul of Levy’s strictures.

size of the cake will surely reduce the size of the slices enjoyed by the planners in (at minimum) the short-run, thereby engendering a mighty incentive on the part of such planners to resist reform (see Boettke 1992). The transition from planning to markets is surely a paradigmatic example of the difficulties inherent to non-convex optimization.

When grappling with the issue of non-convex optimization political economists have – throughout the history of political economy – generally invoked something akin to a discount rate of zero (see Levy 1992). Remarkably, Mises (implicitly if not explicitly) invokes that very same supposition to illustrate the efficiency gains associated with the switch from socialist planning (or pervasive interventionist policies) to free markets: To illuminate the classical liberal theory regarding the “harmony of the rightly understood interests of all members of a market society” (Mises 1966, 674). Mises quite explicitly states that by “rightly understood” interests we might as well say interests “*in the long run*” (Mises 1966, 674, italics added). Best-case thinking indeed!

Toward a Civic Religion: engineering the requisite transformation in agent-type?

Brennan and Buchanan (2000 [1985], 165-167) quite candidly admit to their hopes for the emergence of something akin to “a new “civic religion”” (2000 [1985], 166), one that places great emphasis on the “skepticism of the eighteenth century concerning politics and government” will emerge (166).¹⁸ Does the necessity for a new “civic religion” not serve to belie Buchanan’s remark that constitutional political economy displays “little or no concern with replacing “bad,” “evil,” or “incompetent” politicians with others who may be “good,” “kind,” or “competent.” The emphasis on constitutional reform is neither on persuasion nor on selection of “better” persons to

¹⁸ Elsewhere, Buchanan suggests the necessity for the “widespread adoption of a genuine “constitutional attitude,” a proclivity or tendency to examine issues from a constitutional perspective, as opposed to the pragmatic, short-run, utilitarian perspective that seems to characterize ... day-to-day political discussion and action” (Buchanan 2001 [1981], 42).

act as agents in governing roles” (Buchanan 2001 [1981], 46–47). Despite any appearance (at least *prima facie*) that Buchanan views the rules of the game as adequately substituting for agent-type on all relevant margins, agent-type is, for Buchanan at least, anything but a relatively “trivial matter” (Buchanan 2001 [1981], 47).¹⁹ Indeed, Buchanan recognizes that:

As the historical experience of many countries suggests, constitutions can be reformed without being effectively enforced. Perhaps *more important than formal constitutional changes are changes in ethical attitudes that would make attempted reforms workable ...* There must be some general understanding that exploitation implemented through politics is just as immoral as exploitation implemented in the private sector (James M. Buchanan 2001 [1996], 275, italics added).²⁰

Conclusion: Two great political economists

As regards the depth of his analytical concerns, Buchanan is – I suggest – more akin to John Mill than any other political economist of our age. Mill, of course, was the greatest political economist of his age (perhaps of any age). Buchanan, of course, is equally the greatest political economist of our age.²¹

¹⁹ Constitutional political economy places emphasis on “setting up rules or constraints within which politicians must operate, rules that will make it a *relatively trivial matter as to the personal characteristics of those who happen to be selected as governors*” (Buchanan 2001 [1981], 47, italics added).

²⁰ Buchanan echoes the “constitutional wisdom” of T. B. Macaulay. See, Macaulay (1978 [1829], 206–207).

²¹ Buchanan is, of course, well aware of the type of criticisms to which this paper has subjected certain aspects of constitutional political economy. As Brennan and Buchanan pungently note: “Confronted with questions like these, the economist seems likely either to despair or to avoid relevant thought altogether by playing mathematical games” (Brennan and Buchanan 2000 [1985], 161). Buchanan is notorious for his aversion to the relevance of “mathematical games”. Perhaps Sutter (1998) falls foul of Brennan and Buchanan’s strictures. Sutter provides a model where constitutional rules lead knaves to self-select out of the candidate pool. Why go near the honey-pot when the honey is beyond reach? Sutter (1998, 671), however, begs the question: “I do not consider potential problems enforcing a constraint on government: that is, the choice of x [a set of constitutional rules of the game] binds.” Surely a rational knave would realize that the rules of the game are unlikely to prove binding *ex-post* (constitutional enforcement is a public good), however, and hence, will stay in – rather than self-select out of – the candidate pool. Elsewhere, however, Sutter (1997) provides an excellent discussion of the enforcement problem.

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