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GOVERNMENT AND THE ECONOMY

The Tax Cut.

The Ford Administration has clearly abandoned its feeble attempts to restrict its own inflationary policies, and has gone for broke — literally as well as metaphorically — in expansionist Keynesian policies to try to combat the deepening recession. The money supply is being inflated rapidly once again, to try to stay one step ahead of the "liquidity crunch" that is in the process of driving to the wall inefficient businesses which had overexpanded during the boom. But the major new policy is the Keynesian one of enormous government deficits, now estimated (probably conservatively) at $40 billion. Part of the deficit is to emerge from a substantial cut in income taxes. Immediately, however, the Ford Administration will find itself in a cleft stick; for the very severe nature of the liquidity crunch means that businesses are scrambling for capital in a tight market, and the pouring of $40 billion worth of government bonds onto such a market is going to clobber the private capital market, and greatly intensify the depression. The only way out of **that** bind will be for the Federal Reserve authorities to **create** approximately $40 billion of new money with which the banks will be able to buy the new bonds; and **that** will mean an enormous increase in the inflationary process.

The liberals are supporting an income tax for the wrong, inflationary reasons: the Keynesian theory that consumers will then spend more money, and help lift us out of the recession by their increased spending. In reality, if the deficit is financed through the Federal Reserve, it will, as we've just pointed out, accelerate the inflation. Because of their opposition to inflation, conservatives and many libertarians are opposing the income tax cut, the latter if the cut is not accompanied by an equivalent cut in government spending.

I submit that for libertarians to oppose the income tax cut is disastrous, both on principle and for strategic reasons. Strategically, we would then be supporting a high tax regime which the bulk of Americans hates and clamors against, and would be allowing the ordinarily high-tax liberals to run away with what is a libertarian issue **par excellence.** On principle, taxation is theft, and **any** reduction in taxation whatsoever must be welcomed as allowing producers and individuals to keep more of their own money. Furthermore, in the long run, this can only help the economy by shifting production toward the desires of private consumers. Even on the current recession, furthermore, an income tax cut will help by shifting funds from wasteful government hands into the hands of private savers and investors, whose increased saving will help to ease and speed up the recession-adjustment process. To help the recession, the more the tax cut is geared to increasing saving and investment rather than consumption the better, but the point is that **any** tax cut will have a beneficial effect, morally and economically, in both the long and the short run.

Of course it would be still better if an X billion dollar tax cut were matched by an X billion dollar cut in government spending, but getting the government to cut its spending is politically, at this juncture, a Utopian dream. When was the last year that government spending was actually **reduced**? The answer is lost in antiquity. The point is that given the choices before us, we must take and welcome **any** reduction of government that we can get, anywhere down the line. If the liberals are proposing a large income tax cut, even for the wrong reasons, we should happily make use of this agitation for our own libertarian purposes. After we get the tax cut, we can then agitate for government either to cut its spending, or, at least, to finance its deficit in a non-inflationary manner. Furthermore, looking at the situation strategically, the only way that we might possibly get the government to cut its spending is to reduce taxes first, and then force it to trim its sails on the strength of the general horror at the mammoth size of the deficit. Let us remember Parkinson's Law: expenditures rise to meet income. Then only hope, at this time, of getting government to cut or restrict its expenditures is to cut off its income. An income tax is a giant step in that direction. Libertarians must realize that we are in no position to **plan** an orderly retreat for government, even if that were desirable; government is the enemy, and therefore we must take whatever chunks out of that enemy that circumstances might permit. Hence: hooray for any tax cuts, anywhere, in any area!

Oil Policy.

In the meanwhile, the Ford Administration, seconded by the almost universal clamor of the media, is preparing to aggravate both the inflation and the recession by restricting the supply, and raising the price, of oil and oil products. Restricting the supply of oil will raise prices, and also depress the economy by cutting demand and investment in non-petroleum sectors of the economy. Furthermore, since the Administration proposes to effect the restriction by a massive tax on the import and domestic production of oil, this means that the increased tax revenue from oil will partially offset the good effects of the tax cut, and deepen the recession still further.

The current plan of the Administration is to impose a $3 per barrel tax on the importation of oil, which is supposed to fulfill the Kissinger-Ford goal of a compulsory cut of 1 million barrels per day in the importation of crude oil, a figure which Kissinger admits he chose purely for its "dramatic effect." In this way, the protectionist forces in the oil industry

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are able to return to their cherished policy, ended a couple of years ago by Nixon during the dramatic and short-lived oil "shortage", of restricting imports in order to raise oil prices. In short, while only a year ago we heard that gasoline prices must be kept below free-market levels by the government because "the poor" would be hurt by a price rise, we now hear that the government must artificially **raise** the price of gasoline (by something like 10¢ a gallon), and the poor are heard of no more.

One of the stated aims of oil protectionism is to assure the United States "self-sufficiency" in energy. Such an aim is simply economic insanity. Why not a prohibitory tax on bananas to stimulate hot-house growth of bananas in Florida, and make the U.S. "self-sufficient in bananas"? It is best for all of us, in all countries of the world, to have each country and territorial area, and each of the individuals and firms within such areas, specialize in the production of what each is relatively most efficient at producing, and then selling those products in exchange for the most efficient products of other firms and countries. In short, it is best for all of us to allow the free market, and the international division of labor, to operate across international boundaries ("freedom of trade"). Furthermore, economics shows us that even if another country places artificial barriers on trade, it is still better for us as consumers to allow free trade; any sort of retaliatory tariffs, quotas, or enforced cartels only cut off our noses to spite our faces. Or rather, cut off the noses of American **consumers** in order to confer special privileges to various American businesses. A protective tariff on "widgets" **not only** injures foreign "widget" producers and foreign consumers; it **also** injures American consumers by preventing them from purchasing cheaper widgets, in short, from using their income and resources most efficiently. Furthermore, productive resources in the U.S. are kept by U.S. government coercion from leaving the industry at which they are inefficient (widgets) and moving to other industries where they are more competitive with foreign producers.

This analysis, of course, applies to oil as well as anything else. An import tax on oil (e.g. tariff), as well as import quotas, injures American consumers and the productivity and health of the American economy for the benefit of American oil producers who cannot compete with imported crude.

The Establishment asserts over and over again that the OPEC countries have artificially and sharply raised the price of crude oil, through a government created and enforced cartel. Granted, but so what? The Establishment concludes that the U.S. must restrict oil imports, thereby raising the price of oil and petroleum products **still further**. Does that make any sense; is the way to combat an artificially raised oil price, for the U.S. to increase oil prices **still further**? Of course, it **does** make sense, from one point of view: from the viewpoint of protectionist American oil interests who want to get in on the cartellizing and restrictionist gravy train.

It is also said that we must tighten our belts and cartelize, because if we don't, the evil Arabs of OPEC **might** eventually place another embargo on oil. But does it make any sense to place our own "embargo" on oil permanently, for fear that the Arabs **might** temporarily do so some time in the future? Furthermore, if it's really the Arabs we're worried about, why are we going to place an equivalent **$2** a barrel tax on **domestic** crude oil production? Clearly, the reason is for purposes of over-all cartellization, of government-coerced price-raising in the oil industry. What is more, the entire Arab scare is an Establishment-created bogeyman. For the U.S. does not import a very large amount of its oil from the Arab countries. It is, on the contrary, the countries of Western Europe that are almost totally dependent on Arab oil imports, and yet it is the U.S. and Henry Kissinger that are trying to induce the reluctant Europeans to go along with the tough anti-Arab oil policy. As Dr. Hollis Chenery correctly points out in the January issue of **Foreign Affairs**, Western Europe can better afford to pay the high price of Arab crude oil, than to "depress their economies by squeezing it out" and by following the Kissinger-Ford policy of anti-Arab-oil protectionism.

The Establishment also has the gall to assert that the higher tax on oil is a "market" policy, since the tax works by restricting supply, and raising price, on the market! It claims that the policy is necessary in order to "conserve" oil, and to stimulate the search for new energy sources in America. In the first place, the high-flown claim of "conservation" is the standard excuse for all monopolizing and cartellization. The free, tax-less market does precisely enough "conserving" of oil on its own; when the Arabs raised the price of crude oil to $10 a barrel, this automatically induced each oil user to cut his purchases, to "conserve" oil, in whatever way was best suited for him. The free price system stimulates precisely as much or as little "conservation" of any resource as is necessary. On the basis of the Establishment reasoning, why not slap a $100 per barrel tax on crude oil, and thereby drive up oil and gasoline prices astronomically? If it wants to, the U.S. government can "conserve" oil forever by making sure that none of it is ever bought and sold; what then would we be conserving the oil for? And as for new energy sources, once again the free market price calls forth the optimum amount of such research. The higher price of $10 a barrel will stimulate as much research as will be economically optimal; once again, how about a $100 a barrel tax which would **really** and wildly stimulate a search for new energy sources?

To search for an explanation for a seemingly loony policy, we can therefore forget about the argument that we must combat restricted oil supplies and a higher price, precisely by restricting and raising the price still further! A more cogent clue is a report in the New York **Times** to the effect that, far from the much-heralded oil "shortage", we now have a welcome (to us consumers) oil **surplus**! Thus, the **Times** (Dec. 19) notes: "A slowdown in world economic activity and continued conservation efforts — whether voluntary or induced by higher priced petroleum products — have combined to create a worldwide oil surplus. Stocks on hand of all three major petroleum products . . . are all considered by industry experts to be more than adequate in the United States and other

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Society Without A State*

By Murray N. Rothbard

I

In attempting to outline how a "society without a State" — i.e. an anarchist society — might function successfully, I would first like to defuse two common but mistaken criticisms of this approach. First, is the argument that in providing for such defense or protection services as courts, police, or even law itself, I am simply smuggling the State back into society in another form, and that therefore the system I am both analyzing and advocating is not "really" anarchism. This sort of criticism can only involve us in an endless and arid dispute over semantics. Let me say from the beginning that I define the State as that institution which possesses one or both (almost always both) of the following properties: (1) it acquires its income by the physical coercion known as "taxation"; and (2) it asserts and usually obtains a coerced monopoly of the provision of defense service (police and courts) over a given territorial area. Any institution, not possessing either of these properties is not and cannot be, in accordance with my definition, a "State". On the other hand, I define anarchist society as one where there is no legal possibility for coercive aggression against the person or property of any individual. Anarchists oppose the State because it has its very being in such aggression, namely, the expropriation of private property through taxation, the coercive exclusion of other providers of defense service from its territory, and all of the other depredations and coercions that are built upon these twin foci of invasions of individual rights.

Nor is our definition of the State arbitrary, for these two characteristics have been possessed by what is generally acknowledged to be "States" throughout recorded history. The State, by its use of physical coercion, has arrogated to itself a compulsory monopoly of defense services over its territorial jurisdiction. But it is certainly conceptually possible for such services to be supplied by private, non-State institutions, and indeed such services have historically been supplied by other organizations than the State. To be opposed to the State is then not necessarily to be opposed to services that have often been linked with it; to be opposed to the State does not necessarily imply that we must be opposed to police protection, courts, arbitration, the minting of money, postal service, or roads and highways. **Some** anarchists have indeed been opposed to police and to all physical coercion **in defense of** person and property, but this is not inherent in and is fundamentally irrelevant to the anarchist position, which is precisely marked by opposition to all physical coercion invasive of, or aggressing against, person and property.

The crucial role of taxation may be seen in the fact that the State is the only institution or organization in society which regularly and systematically acquires its income through the use of physical coercion. All other individuals or organizations acquire their income voluntarily, either (a) through the voluntary sale of goods and services to consumers on the market, or (b) through voluntary gifts or donations by members or other donors. If I cease or refrain from purchasing Wheaties on the market, the Wheaties producers do not come after me with a gun or prison to force me to purchase; if I fail to join the American Philosophical Association, the association may not force me to join or prevent me from giving up my membership. Only the State can do so; only the State can confiscate my property or put me in jail if I do not pay its tax-tribute. Therefore, only the State regularly exists and has its very being by means of coercive depredations on private property.

Neither is it legitimate to challenge this sort of analysis by claiming that in some other sense, the purchase of Wheaties or membership in the A.P.A. is in some way "coercive"; there again, we can only be trapped in an endless semantic dispute. Apart from other rebuttals which cannot be considered here, I would simply say that anarchists are interested in the abolition of this type of action: e.g. aggressive physical violence against person and property, and that this is how we define "coercion". Anyone who is still unhappy with this use of the term "coercion" can simply eliminate the word from this discussion, and substitute for it "physical violence or the threat thereof", with the only loss being in literary style rather than in the substance of the argument. What anarchism proposes to do, then, is to abolish the State, i.e. to abolish the regularized institution of aggressive coercion.

It need hardly be added that the State habitually builds upon its coercive source of income by adding a host of other aggressions upon society: ranging from economic controls to the prohibition of pornography to the compelling of religious observance to the mass

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industrial countries to meet the needs of this winter . . . Europe and Japan are virtually awash in supplies." So here we have a vital clue: the new restrictions and cartellizing of the U.S. are an attempt to combat — **not** high oil prices — but the threat that market forces will break the OPEC cartel and bring about a sharp drop in oil prices. Once again, we are being conned by the Establishment, and both the Democratic and Republican parties are collaborating in the swindle.

Back to Gold.

Inexorably, and in the teeth of extreme reluctance and hostility by the U.S. authorities, gold is forcing its way, step by step, back into the central monetary role that it deserves. After cutting loose from the private gold market (in the "two-tier" system) in 1968, and after cutting the dollar completely from the gold standard in 1971, the Establishment was confident that gold was on the way to being banished forever, to be replaced by the dollar or by a new paper fiat unit, completely controllable by governments. Instead, gold has been forcing its way back, and at each step of the way the Administration has tried to "cover up" by claiming that gold was now one step further **out** of playing an important monetary role. More important even than the Treasury's finally and grudgingly allowing the will of Congress to prevail and allowing the U.S. citizens to buy and own gold, was the December, 1974 agreement at Martinique between the U.S. and France. For decades, the U.S. has been trying to push gold out of the picture by forcing other nations to evaluate it at an absurdly and artificially low price, first $35 an ounce, and lately $42 an ounce. But the enormous rise in the free gold market price in the last few years, in response to the continuing depreciation of paper currencies, put irresistible pressure on all countries to re-evaluate their gold stock at the market price, and thereby to stave off impending financial bankruptcy. Finally, at Martinique, the U.S. made the crucial concession, that "It would be appropriate for any government which wished to do so to adopt current market prices as the basis for valuation of its gold holdings." Typically, the U.S. covered its surrender by asserting, once again, that this was another step toward **ending** the monetary role of gold. Actually, of course, the step was quite the reverse: for now, as country after country upgrades its gold stock to evaluate it at the market price, the monetary role and importance of gold will enormously increase. Not only that: the re-valuation could pave the way for an eventual return to a full-fledged gold standard, i.e. the redeemability of dollars and other currencies in gold, which would not have been possible at the artificially low price. This possible return to gold is precisely what the inflationist U.S. authorities were desperately anxious to prevent.

Following up the Martinique agreement, the French fulfilled the promise of the agreement on January 9 by officially revaluing their gold stock at the roughly market price of $170 an ounce. Can other countries be far behind?

"Libertarian" Economist Note.

Professor Milton Friedman, alleged "libertarian" economist, was asked to comment in a radio interview on President Ford's address on January 13. Friedman endorsed the proposed tax on imported oil in order to put pressure on the OPEC countries. What happened to Friedman's proclaimed belief in unilateral free trade? Devotion to **what** cause has led to Friedman's abandonment of free trade-free market principles **this** time? ◘

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murder of civilians in organized warfare. In short, that the State, in the words of Albert Jay Nock, "claims and exercises a monopoly of crime" over its territorial area.

The second criticism I would like to defuse before beginning the main body of the paper is the common charge that anarchists "assume that all people are good", and that without the State no crime would be committed. In short, that anarchism assumes that with the abolition of the State a New Anarchist Man will emerge, cooperative, humane, and benevolent, so that no problem of crime will then plague the society. I confess that I do not understand the basis for this charge. Whatever other schools of anarchism profess — and I do not believe that they are open to this charge — I certainly do not adopt this view. I assume with most observers that mankind is a mixture of good and evil, of cooperative and criminal tendencies. In my view, the anarchist society is one which maximizes the tendencies for the good and the cooperative, while it minimizes both the opportunity and the moral legitimacy of the evil and the criminal. If the anarchist view is correct, and the State is indeed the great legalized and socially legitimated channel for all manner of anti-social crime — theft, oppression, mass murder — on a massive scale, then surely the abolition of such an engine of crime can do nothing but favor the good in man and discourage the bad.

A further point: in a profound sense, **no** social system, whether anarchist or statist, can work at all unless most people are "good" in the sense that they are not all hell-bent upon assaulting and robbing their neighbors. If everyone were so disposed, no amount of protection, whether State or private, could succeed in staving off chaos. Furthermore, the more that people are disposed to be peaceful and not aggress against their neighbors, the more successfully **any** social system will work, and the fewer resources will need to be devoted to police protection. The anarchist view holds that, given the "nature of man", given the degree of goodness or badness at any point of time, anarchism will maximize the opportunities for good and minimize the channels for the bad. The rest depends on the values held by the individual members of society. The only further point that need be made is that by eliminating the living example and the social legitimacy of the massive legalized crime of the State, anarchism will to a large extent promote peaceful values in the minds of the public.

We cannot of course deal here with the numerous arguments in favor of anarchism or against the State, moral, political, and economic. Nor can we take up the various goods and services now provided by the State, and show how private individuals and groups will be able to supply them far more efficiently on the free market. Here we can only deal with perhaps the most difficult area, the area where it is almost universally assumed that the State must exist and act, even if it is only a "necessary evil" instead of a positive good: the vital realm of defense or protection of person and property against aggression. Surely, it is universally asserted, the State is at least vitally necessary to provide police protection, the judicial resolution of disputes and enforcement of contracts, and the creation of the law itself that is to be enforced. My contention is that all of these admittedly necessary services of protection can be satisfactorily and efficiently supplied by private persons and institutions on the free market.

One important caveat before we begin the body of this paper: new proposals such as anarchism are almost always gauged against the implicit assumption that the present, or statist, system works to perfection. Any lacunae or difficulties with the picture of the anarchist society are considered net liabilities, and enough to dismiss anarchism out of hand. It is, in short, implicitly assumed that the State is doing its self-assumed job of protecting person and property to perfection. We cannot here go into the reasons why the State is bound to suffer inherently from grave flaws and inefficiencies in such a task. All we need do now is to point to the black and unprecedented record of the State through history: no combination of private marauders can possibly begin to match the State's unremitting record of theft, confiscation, oppression, and mass murder. No collection of Mafia or private bank robbers can begin to compare with all the Hiroshimas, Dresdens, and Lidices and their analogs through the history of mankind.

This point can be made more philosophically: it is illegitimate to compare the merits of anarchism and statism by starting with the present system as the implicit given and then critically examining only the anarchist alternative. What we must do is to begin at the zero point and then critically examine **both** suggested alternatives. Suppose, for example, that we were all suddenly dropped down on the earth **de novo**, and that we were all then confronted with the question of what societal arrangements to adopt. And suppose then that someone suggested: "We are all bound to suffer from those of us who wish to aggress against their fellow men. Let us than solve this problem of crime by handing all of our weapons to the Jones family, over there, by giving all of our ultimate power to settle disputes to that family. It that way, with their monopoly of coercion and of ultimate decision making, the Jones family will be able to protect each of us from each other." I submit that this proposal would get very short shrift, except perhaps from the Jones family themselves. And yet this is precisely the common argument for the existence of the State. When we start from the zero point, as in the case of the Jones family, the question of "who will guard the guardians?" becomes not simply an abiding lacuna in the theory of the State but an overwhelming barrier to its existence.

A final **caveat**: the anarchist is always at a disadvantage in attempting to forecast the shape of the future anarchist society. For it is impossible for observers to predict voluntary social arrangements, including the provision of goods and services, on the free market. Suppose, for example, that this were the year 1874, and someone predicted that eventually there would be a radio manufacturing industry. To be able to make such a forecast successfully, does he have to be challenged to state immediately how many radio manufacturers there would be a century hence, how big they would be, where they would be located, what technology and marketing techniques they would use, etc.? Obviously, such a challenge would make no sense, and in a profound sense the same is true of those who demand a precise portrayal of the pattern of protection activities on the market. Anarchism advocates the dissolution of the State into social and market arrangements, and these arrangements are far more flexible and less predictable than political institutions. The most that we can do, then, is to offer broad guidelines and perspectives on the shape of a projected anarchist society.

One important point to make here is that the advance of modern technology makes anarchistic arrangements increasingly feasible. Take, for example, the case of lighthouses, where it is often charged that it is unfeasible for private lighthouse operators to row out to each ship to charge it for use of the light. Apart from the fact that this argument ignores the successful existence of private lighthouses in earlier days, e.g. in England in the eighteenth century, another vital consideration is that modern electronic technology makes charging each ship for the light far more feasible. Thus, the ship would have to have paid for an electronically controlled beam which could then be automatically turned on for those ships which had paid for the service.

II

Let us now turn to the problem of how disputes — in particular, disputes over alleged violations of person and property, — would be resolved in an anarchist society. First, it should be noted that all disputes involve two parties: the plaintiff, the alleged victim of the crime or tort, and the defendant, the alleged aggressor. In many cases of broken contract, of course, each of the two parties alleging that the other is the culprit is at the same time a plaintiff and a defendant.

An important point to remember is that **any** society, be it statist or anarchist, has to have **some** way of resolving disputes that will gain a majority consensus in society. There would be no need for courts or arbitrators if everyone were omniscient, and knew instantaneously **which** persons were guilty of any given crime or violation of contract. Since none of us are omniscient, there has to be some method of deciding who is the criminal or lawbreaker which will gain legitimacy, in short whose decision will be accepted by the great majority of the public.

In the first place, a dispute may be resolved voluntarily between the two parties themselves, either unaided or with the help of a third mediator. This poses no problem, and will automatically be accepted by society at large. It is so accepted even now, much less in a society imbued with the anarchistic values of peaceful cooperation and agreement. Secondly and similarly, the two parties, unable to reach agreement, may decide to submit voluntarily to the decision of an arbitrator. This agreement may arise either after a dispute has arisen, or be provided for in advance in the original contract. Again, there is no problem in such an

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arrangement gaining legitimacy. Even in the present statist era, the notorious inefficiency and coercive and cumbersome procedures of the politically run government courts has led increasing numbers of citizens to turn to voluntary and expert arbitration for a speedy and harmonious settling of disputes.

Thus, William C. Wooldridge has written that

> "arbitration has grown to proportions that make the courts a secondary recourse in many areas and completely superfluous in others. The ancient fear of the courts that arbitration would 'oust' them of their jurisdiction has been fulfilled with a vengeance the common-law judges probably never anticipated. Insurance companies adjust over fifty thousand claims a year among themselves through arbitration, and the American Arbitration Association (AAA), with headquarters in New York and twenty-five regional offices across the country, last year conducted over twenty-two thousand arbitrations. Its twenty-three thousand associates available to serve as arbitrators may outnumber the total number of judicial personnel . . . in the United States . . . Add to this the unknown number of individuals who arbitrate disputes within particular industries or in particular localities, without formal AAA affiliation, and the quantitatively secondary role of official courts begins to be apparent." *

Wooldridge adds the important point that, in addition to the speed of arbitration procedures **vis a vis** the courts, the arbitrators can proceed as experts in disregard of the official government law; in a profound sense, then, they serve to create a voluntary body of private law. "In other words," states Wooldridge, "the system of extralegal, voluntary courts has progressed hand in hand with a body of private law; the rules of the state are circumvented by the same process that circumvents the forums established for the settlement of disputes over those rules . . . In short, a private agreement between two people, a bilateral "law", has supplanted the official law. The writ of the sovereign has ceased to run, and for it is substituted a rule tacitly or explicitly agreed to by the parties." Wooldridge concludes that "if an arbitrator can choose to ignore a penal damage rule or the statute of limitations applicable to the claim before him (and it is generally conceded that he has that power), arbitration can be viewed as a practically revolutionary instrument for self-liberation from the law . . ." [2]

It may be objected that arbitration only works successfully because the courts enforce the award of the arbitrator. Wooldridge points out, however, that arbitration was unenforceable in the American courts before 1920, but that this did not prevent voluntary arbitration from being successful and expanding in the United States and in England. He points, furthermore, to the successful operations of merchant courts since the Middle Ages, those courts which successfully developed the entire body of the law merchant. None of those courts possessed the power of enforcement. He might have added the private courts of shippers which developed the body of admiralty law in a similar way.

How then did these private, "anarchistic", and voluntary courts insure the acceptance of their decisions? By the method of social ostracism, and the refusal to deal any further with the offending merchant. This method of voluntary "enforcement", indeed, proved highly successful. Wooldridge writes that "the merchants' courts were voluntary, and if a man ignored their judgment, he could not be sent to jail . . . Nevertheless, it is apparent that . . . (their) decisions were generally respected even by the losers; otherwise people would never have used them in the first place . . . Merchants made their courts work simply by agreeing to abide by the results. The merchant who broke the understanding would not be sent to jail, to be sure, but neither would he long continue to be a merchant, for the compliance exacted by his fellows . . . proved if anything more effective than physical coercion." [3] Nor did this voluntary method fail to work in modern times. Wooldridge writes that it was precisely in the years before 1920, when arbitration awards could not be enforced in the courts,

> "that arbitration caught on and developed a following in the American mercantile community. Its popularity, gained at a time when abiding by an agreement to arbitrate had to be as voluntary as the agreement itself, casts doubt on whether legal coercion was an essential adjunct to the settlement of most disputes. Cases of refusal to abide by an arbitrator's award were rare; one founder of the American Arbitration Association could not recall a single example. Like their medieval forerunners, merchants in the Americas did not have to rely on any sanctions other than those they could collectively impose on each other. One who refused to pay up might find access to his association's tribunal cut off in the future, or his name released to the membership of his trade association; these penalties were far more fearsome than the cost of the award with which he disagreed. Voluntary and private adjudications were voluntarily and privately adhered to, if not out of honor, out of the self-interest of businessmen who knew that the arbitral mode of dispute settlement would cease to be available to them very quickly if they ignored an award." [4]

[1] It should also be pointed out that modern technology makes even more feasible the collection and dissemination of information about people's credit ratings and records of keeping or violating their contracts or arbitration agreements. Presumably, an anarchist society would see the expansion of this sort of dissemination of data and thereby facilitate the ostracism or boycotting of contract and arbitration violators.

How would arbitrators be selected in an anarchist society? In the same way as they are chosen now, and as they were chosen in the days of strictly voluntary arbitration: the arbitrators with the best reputation for efficiency and probity would be chosen by the various parties on the market. As in other processes of the market, the arbitrators with the best record in settling disputes will come to gain an increasing amount of business, and those with poor records will no longer enjoy clients, and have to shift to another line of endeavor. Here it must be emphasized that parties in dispute will seek out those arbitrators with the best reputation for both expertise and impartiality, and that inefficient or biased arbitrators will rapidly have to find another occupation.

Thus, the Tannehills emphasize:

> "the advocates of government see initiated force (the legal force of government) as the only solution to social disputes. According to them, if everyone in society were not forced to use the same court system . . . disputes would be insoluble. Apparently it doesn't occur to them that disputing parties are capable of freely choosing their own arbiters . . . They have not realized that disputants would, in fact, be far better off if they could choose among competing arbitration agencies so that they could reap the benefits of competition and specialization. It should be obvious that a court system which has a monopoly guaranteed by the force of statutory law will not give as good quality service as will free-market arbitration agencies which must compete for their customers . . .
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> Perhaps the least tenable argument for government arbitration of disputes is the one which holds that governmental judges are more impartial because they operate outside the market and so have no vested interests . . . owing political allegiance to government is certainly no guarantee of impartiality! A governmental judge is always impelled to be partial — in favor of the government, from whom he gets his pay and his power! On the other hand, an arbiter who sells his services in a free market knows that he must be as scrupulously honest, fair, and impartial as possible or no pair of disputants will buy his services to arbitrate their dispute. A free-market aribter depends for his livelihood on his skill and fairness at settling disputes. A governmental judge depends on political pull." [4]

If desired, furthermore, the contracting parties could provide in advance for a series of arbitrators:

> "It would be more economical and in most cases quite sufficient to have only one arbitration agency to hear the case. But if the parties felt that a further appeal might be necessary and were willing to risk the extra expense, they

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> could provide for a succession of two or even more arbitration agencies. The names of these agencies would be written into the contract in order from the 'first court of appeal' to the 'last court of appeal'. It would be neither necessary nor desirable to have one single, final court of appeal for every person in the society, as we have today in the United States Supreme Court." [5]

Arbitration, then poses little difficulty for a portrayal of the free society. But what of torts or crimes of aggression where there has been no contract? Or suppose that the breaker of a contract defies the arbitration award? Is ostracism enough? In short, how can courts develop in the free-market, anarchist society which will have the power to enforce judgments against criminals or contract-breakers?

In the wide sense, defense service consists of guards or police who use force in defending person and property against attack, and judges or courts whose role is to use socially accepted procedures to determine who the criminals or tortfeasors are, as well as to enforce judicial awards, such as damages or the keeping of contracts. On the free market, many scenarios are possible on the relationship between the private courts and the police; they may be "vertically integrated", for example, or their services may be supplied by separate firms. Furthermore, it seems likely that police service will be supplied by insurance companies who will provide crime-insurance to their clients. In that case, insurance companies will pay off the victims of crime or the breaking of contracts or arbitration awards, and then pursue the aggressors in court to recoup their losses. There is a natural market connection between insurance companies and defense service, since they need pay out less benefits in proportion as they are able to keep down the rate of crime.

Courts might either charge fees for their services, with the losers of cases obliged to pay court costs, or else they may subsist on monthly or yearly premiums by their clients, who may be either individuals or the police or insurance agencies. Suppose, for example, that Smith is an aggrieved party, either because he has been assaulted or robbed, or because an arbitration award in his favor has not been honored. Smith believes that Jones is the party guilty of the crime. Smith then goes to a court, Court A, of which he is a client, and brings charges against Jones as a defendant. In my view, the hallmark of an anarchist society is one where no man may legally compel someone who is not a convicted criminal to do anything, since that would be aggression against an innocent man's person or property. Therefore, Court A can only invite rather than subpoena Jones to attend his trial. Of course, if Jones refuses to appear or send a representative, his side of the case will not be heard. The trial of Jones proceeds. Suppose that Court A finds Jones innocent. In my view, part of the generally accepted Law Code of the anarchist society (on which see further below), is that this must end the matter, unless Smith can prove charges of gross incompetence or bias on the part of the court.

Suppose, next, that Court A finds Jones guilty. Jones might accept the verdict, either because he too is a client of the same court, because he knows he is guilty, or for some other reason. In that case, Court A proceeds to exercise judgment against Jones. Neither of these instances pose very difficult problems for our picture of the anarchist society. But suppose, instead, that Jones contests the decision; he, then, goes to his court, Court B, and the case is retried there. Suppose that Court B, too, finds Jones guilty. Again, it seems to me that the accepted Law Code of the anarchist society will assert that this ends the matter; both parties have had their say in courts which each has selected, and the decision for guilt is unanimous.

Suppose, however, the most difficult case: That Court B finds Jones innocent. The two courts, each subscribed to by one of the two parties, have split their verdicts. In that case, the two courts will submit the case to an appeals court, or arbitrator, which the two courts agree upon. There seems to be no real difficulty about the concept of an appeals court. As in the case of arbitration contracts, it seems very likely that the various private courts in the society will have prior agreements to submit their disputes to a particular appeals court. How will the appeals judges be chosen? Again, as in the case of arbitrators or of the first judges on the free market, they will be chosen for their expertise and reputation for efficiency, honesty and integrity. Obviously, appeals judges who are inefficient or biased will scarcely be chosen by courts who will have a dispute. The point here is that there is no need for a legally established or institutionalized single, monopoly appeals court system, as States now provide. There is no reason why there cannot arise a multitude of efficient and honest appeals judges who will be selected by the disputant courts, just as there are numerous private arbitrators on the market today. The appeals court renders its decision, and the courts proceed to enforce it if, in our example, Jones is considered guilty — unless, of course, Jones can prove bias in some other court proceedings.

No society can have unlimited judicial appeals, for in that case there would be no point to having judges or courts at all. Therefore, every society, whether statist or anarchist, will have to have some socially accepted cut-off point for trials and appeals. My suggestion is the rule that the agreement **of any two courts** be decisive. "Two" is not an arbitrary figure, for it reflects the fact that there are two parties, the plaintiff and the defendant, to any alleged crime or contract dispute.

If the courts are to be empowered to enforce decisions against guilty parties, does this not bring back the State in another form and thereby negate anarchism? No, for at the beginning of this paper I explicitly defined anarchism in such a way as not to rule out the use of defensive force — force in defense of person and property — by privately supported agencies. In the same way, it is not bringing back the State to allow persons to use force to defend themselves against aggression, or to hire guards or police agencies to defend them.

It should be noted, however, that in the anarchist society there will be no "district attorney" to press charges on behalf of "society". Only the victims will press charges as the plaintiffs. If, then, these victims should happen to be absolute pacifists who are opposed even to defensive force, then they will simply not press charges in the courts or otherwise retaliate against those who have aggressed against them. In a free society that would be their right. If the victim should suffer from murder, then his heir would have the right to press the charges.

What of the Hatfield-and-McCoy problem? Suppose that a Hatfield kills a McCoy, and that McCoy's heir does not belong to a private insurance, police agency, or court, and decides to retaliate himself? Since, under anarchism there can be no coercion of the non-criminal, McCoy would have the perfect right to do so. No one may be compelled to bring his case to a court. Indeed, since the right to hire police or courts flows from the right of self-defense against aggression, it would be inconsistent and in contradiction to the very basis of the free society to institute such compulsion. Suppose, then, that the surviving McCoy finds what he believes to be the guilty Hatfield and kills him in turn? What then? This is fine, except that McCoy may have to worry about charges being brought against him by a surviving Hatfield. Here it must be emphasized that in the law of the anarchist society based on defense against aggression, the courts would not be able to proceed against McCoy if in fact he killed the right Hatfield. His problem would arise if the courts should find that he made a grievous mistake, and killed the wrong man; in that case, he in turn would be found guilty of murder. Surely, in most instances, individuals will wish to obviate such problems by taking their case to a court and thereby gain social acceptability for their defensive retaliation — not for the **act** of retaliation but for the correctness of deciding who the criminal in any given case might be. The purpose of the judicial process, indeed, is to find a way of general agreement on who might be the criminal or contract-breaker in any given case. The judicial process is not a good in itself; thus, in the case of an assassination, such as Jack Ruby's murder of Oswald, on public television, there is no need for a complex judicial process since the name of the murderer is evident to all.

Will not the possibility exist of a private court that may turn venal and dishonest, or of a private police force that turns criminal and extorts money by coercion? Of course such an event may occur, given the propensities of human nature. Anarchism is not a moral cure-all. But the important point is that market forces exist to place severe checks on such possibilities, especially in contrast to a society where a State exists. For, in the first place, judges, like arbitrators, will prosper on the market in proportion to their reputation for efficiency and impartiality. Secondly, on the free market important checks and balances exist against venal courts or criminal police forces. Namely, that there are competing courts and police agencies to whom the victims may turn for redress. If the "Prudential Police Agency" should turn outlaw and extract revenue from victims by coercion, the latter would have the option of turning to the "Mutual" or "Equitable" Police Agency for defense and for pressing

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charges against Prudential. These are the **genuine** "checks and balances" of the free market, genuine in contrast to the phony checks and balances of a State system, where all the alleged "balancing" agencies are in the hands of one monopoly government. Indeed, given the monopoly "protection service" of a State, what is there to prevent a State from using its monopoly channels of coercion to extort money from the public? What are the checks and limits of the State? None, except for the extremely difficult course of revolution against a Power with all of the guns in its hands. In fact, the State provides an easy, legitimated channel for crime and aggression, since it has its very being in the crime of tax-theft, and the coerced monopoly of "protection." It is the State, indeed, that functions as a mighty "protection racket" on a giant and massive scale. It is the State that says: "Pay us for your 'protection' or else." In the light of the massive and inherent activities of the State, the danger of a "protection racket" emerging from one or more private police agencies is relatively small indeed.

Moreover, it must be emphasized that a crucial element in the power of the State is its legitimacy in the eyes of the majority of the public, the fact that after centuries of propaganda, the depredations of the State are looked upon rather as benevolent services. Taxation is generally not seen as theft, nor war as mass murder, nor conscription as slavery. Should a private police agency turn outlaw, should "Prudential" become a protection racket, it would then lack the social legitimacy which the State has managed to accrue to itself over the centuries. "Prudential" would be seen by all as bandits, rather than as legitimate or divinely appointed "sovereigns", bent on promoting the "common good" or the "general welfare". And lacking such legitimacy, Prudential would have to face the wrath of the public and the defense and retaliation of the other private defense agencies, the police and courts, on the free market. Given these inherent checks and limits, a successful transformation from a free society to bandit rule becomes most unlikely. Indeed, historically, it has been very difficult for a State to arise to supplant a stateless society; usually, it has come about through external conquest rather than by evolution from within a society.

Within the anarchist camp, there has been much dispute on whether the private courts would have to be bound by a basic, common Law Code. Ingenious attempts have been made to work out a system where the laws or standards of decision-making by the courts would differ completely from one to another. [5] But in my view all would have to abide by the basic Law Code, in particular, prohibition of aggression against person and property, in order to fulfill our definition of anarchism as a system which provides no legal sanction for such aggression. Suppose, for example, that one group of people in society hold that all redheads are demons who deserve to be shot on sight. Suppose that Jones, one of this group, shoots Smith, a redhead. Suppose that Smith or his heir presses charges in a court, but that Jones' court, in philosophic agreement with Jones, finds him innocent therefore. It seems to me that in order to be considered legitimate, any court would have to follow the basic libertarian law code of the inviolate right of person and property. For otherwise, courts might legally subscribe to a code which sanctions such aggression in various cases, and which to that extent would violate the definition of anarchism and introduce, if not the State, then a strong element of statishness or legalized aggression into the society.

But again I see no insuperable difficulties here. For in that case, anarchists, in agitating for their creed, will simply include in their agitation the idea of a general libertarian Law Code as part and parcel of the anarchist creed of abolition of legalized aggression against person or property in the society.

In contrast to the general law code, other aspects of court decisions could legitimately vary in accordance with the market or the wishes of the clients e.g., the language the cases will be conducted in, the number of judges to be involved, etc.

There are other problems of the basic Law Code which there is no time to go into here: for example, the definition of just property titles or the question of legitimate punishment of convicted offenders — though the latter problem of course exists in statist legal systems as well. [6] The basic point, however, is that the State is not needed to arrive at legal principles or their elaboration: indeed, much of the common law, the law merchant, admiralty law, and private law in general, grew up apart from the State, by judges not making the law but finding it on the basis of agreed upon principles derived either from custom or reason. [7] The idea that the State is needed to **make** law is as much a myth as that the State is needed to supply postal or police service.

Enough has been said here, I believe, to indicate that an anarchist system for settling disputes would be both viable and self-subsistent: that once adopted, it could work and continue indefinitely. **How to arrive** at that system is of course a very different problem, but certainly at the very least it will not likely come about unless people are convinced of its workability, are convinced, in short, that the State is not a **necessary** evil.

*A paper delivered before the American Society for Political and Legal Philosophy, Washington, D. C., on Dec. 28, 1974.

*William C. Wooldridge, **Uncle Sam, the Monopoly Man** (New Rochelle, N.Y.: Arlington House, 1970), p. 101.

[5] **Ibid.**, pp. 103-04.

[6] **Ibid.**, pp. 95-96.

[7] **Ibid.**, pp. 100-101.

[5] Morris and Linda Tannehill, **The Market for Liberty** (Lansing, Michigan: privately printed, 1970), pp. 65-67.

[6] **Ibid.**, p. 68.

[7] E.g. David Friedman, **The Machinery of Freedom** (New York: Harper & Row, 1973).

[8] For an elaboration of these points, see Murray N. Rothbard, **For A New Liberty** (New York: Macmillan, 1973).

[9] Thus, see Bruno Leoni, **Freedom and the Law** (Princeton, N.J.: D. Van Nostrand Co., 1961).

New Rothbard Books!

January 17 is the publication date of the first volume of Murray Rothbard's projected multi-volume history of colonial America, **Conceived in Liberty**. Published by Arlington House and over 500 pages in length, Volume I covers the American colonies during the 17th century. Note: this is **not** an economic history, but a general history dealing with all aspects of the new American colonies: ideological, religious, social, and political, as well as economic. The general focus of the book is — surprise! — on liberty and voluntary social arrangements ("social power") vs. the State. Price is $15.00

Why the need for so many pages on the colonial era? Despite the fact that American history textbooks dismiss the colonial era in 20 or so pages, this period covers almost 170 years, and more if we include the pre-colonial explorations. An enormous number of exciting and important events occurred during these years, and **Conceived in Liberty** brings us the full narrative flavor of the period, the actual events that occurred in their historical cause-and-effect sequence. Furthermore, while many standard textbook "heroes" are debunked and shown to have feet of clay, other, totally forgotten libertarian heroes are rediscovered.

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Also, the Libertarian Review Press (422 First St. S.E., Washington, D.C. 20003) has just reprinted, in booklet form, Murray Rothbard's 1962 essay, "The Case for a 100 Percent Gold Dollar", which had appeared in a totally neglected book by L. Yeager, ed., **In Search of a Monetary Constitution** (Harvard University Press). Needless to say, the topic is far more timely now than it was 13 years ago. Copies of **The Case for a 100 Percent Gold Dollar** may be obtained for $2.00 from the Libertarian Review Press.

"Herein, indeed, lies the chief merit of democracy, when all is said and done: it may be clumsy, it may be swinish, it may be unutterably incompetent and dishonest, but it is never dismal — its processes, even when they irritate, never actually bore."

— H. L. Mencken

The Demise Of Fractional Reserve Banking?

By Karl E. Peterjohn

Fractional reserve banking is in trouble. Last year two major banks, Franklin National and I.D. Herstatt, collapsed. They left behind a trail of liabilities across the international banking system which are still being felt. The cause of these bank failures is likely to repeat itself, while banks taking action to correct their currently weak financial reserve positions may become the targets of scurrilous politicians.

When the Federal Reserve System (hereafter the Fed) expands credit (also known as counterfeiting), this expansion of the money stock takes place through the banking structure. New funds are now available for loans to firms and individuals from the banks. Interest rates decline due to increased funds being available. The banks, anxious to make a profit with these new funds, and following the government's expansion-oriented economic policy, loan the funds to borrowers. Through the fractional reserve structure, an increase in bank deposits of $100 can be multiplied into loans worth many times that value.

Naturally when the credit expansion creates inflation, government policy changes. The Fed stops expanding credit to fight inflation. Since the increase in the supply of loanable funds came from the Fed's money creation, rather than from market action, the supply of loanable funds contracts. Interest rates rise and a credit crunch occurs.

As interest rates rise, investors try to maximize the returns on their savings. Since the banks have loaned out funds for 10 or 20 years at the low interest rates created by the Fed's credit expansion, the credit crunch would force the banks to raise interest rates to attract more savings or liquidate loans. The banks could be forced to pay higher interest rates for savings than the interest the bank is receiving on outstanding loans. To prevent this from happening, and to restrict competition, the banks convinced the Fed to enact Regulation "Q", which limits the maximum interest rate savers can receive from banks.

As interest rates rise, savings flow from banks with their low interest rates to bonds, credit unions, loan companies, and other financial devices which offer higher interest rates for savers. Economists call this process disintermediation. To make sure that the banks can cover loans made at the low interest rate, the government has created a number of agencies, besides the Fed, which will prevent disintermediation from causing bank runs. The Federal Home Loan Bank Board, the Veterans Administration, and the Department of Housing and Urban Development all provide funds to banks to protect low interest loans. In this manner any test of the financial soundness of the Financial Deposit Insurance Corporation is avoided.

As 1975 begins, we have been through the credit expansion-boom-inflation-credit crunch cycle four times in the last fifteen years. The U.S. fractional banking system can't take much more of it. Inflation is consuming capital and the real value of savings at a tremendous pace. Since the returns on stocks are being clobbered by inflation and taxes, the only ready sources of investment funds for most firms are bank loans. However, the Fed's credit expansion is the only new source of loanable funds for the banks. Since the banks are the only ready source of investment funds, the banks are increasingly involved with the firms they make loans to. For this reason a number of superficial economists are pointing out how the banks are "taking over" control of a wide variety of non-financial corporations through loan arrangements. In Great Britain this government loan process has reached the point where the government is making loans outright to industry. Here the government has created the Fed, which uses the banks to make and oversee the loans to firms.

Since so many banks came close to collapse (even the ones not involved in foreign currency transactions) during the last credit expansion-boom-inflation-credit crunch cycle, the Fed issued orders that banks are supposed to increase their reserves. Banks will be less likely to flounder in our next credit cycle if substantial reserve assets are available to protect against the next credit crunch.

The Fed has in the last few weeks been expanding credit rapidly in a belated effort to stem our recession. As the new credit cycle begins with the renewed credit expansion, the banks will be faced with a difficult decision. If the banks go along with the Fed and lower their prime interest rate, lending out all available funds, the spectre of bank failure arises as soon as the Fed decides to switch gears and fight inflation by stopping the flow of new dollars. The resultant credit crunch, where interest rates rise to 15 to 20%, could bring down many banks that are overextended. If this happens, the banks will be blamed for overextending themselves and not following Fed policy.

However, if the banks try to protect themselves by not expanding credit and do keep substantial reserves, the banks are now going against government policy. Many firms unable to get loans, or to get loans at a "fair" interest rate, as well as irate consumers unable to purchase 8% home mortgages, will cry bank conspiracy. Politicians will be able to claim that the banks are thwarting the government's economic policy and preventing economic recovery. The politicians will then have the perfect whipping boy. To prevent being crucified by the politicians, and unwilling to forego interest on loans, most banks will make loans and hope that the Fed will be able to protect them when the credit crunch arrives. It is, for the economy and for the banks a forlorn hope.

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