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The Libertarian Welfare State

Robert Hockett

Robert Hockett reviews Robert Frank's book The Darwin Economy: Liberty, Competition, and the Common Good *(Princeton University Press, 2011).*

AMERICANS LONG HAVE BEEN TAKEN WITH LIBERTY. Yet we tend to be quicker to affirm this core value than we are to unpack it, work through its implications, and thereby limn liberty's—or liberties'—limits.

One result of this "shoot from the hip" tendency is a failure by many antagonists in ideological contests to notice that all sides, in fact, favor "liberty," while disagreeing over little if anything more than whose (or which) liberties trump whose. Many self-styled "libertarians," for example, seem to think their values clash with the values of those they call "liberals." What do they make, then, of the fact that the Latin root liber—"free"—forms the core of the words "liberal" and "libertarian" alike, and that this is no accident?

Widening the scope of our query a bit, what do our libertarians, and now liberals as well, make of *liber*'s role in the word "libertine," a word that we use to denote those who elide quickly from legitimate freedom to illicit excess—that is, to the "disorderly" or "dissolute"? And how does it happen that liberty figures, along with the complementary value to which Americans refer under the rubric of "justice" and the French under the rubric of *égalité*, in the pledges and slogans of American and French patriots alike? Are the French and the self-

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described libertarians, or the Americans and the liberals, really just gassing when they speak of freedom or liberty, while their antagonists alone really *commit* to that value?

Of course not. And this is so even when the sides disagree over precisely what freedom requires in particular contexts.

There is a reason, I think, for these good-faith disagreements about what our commonly shared value of liberty requires. The problem at bottom is that one person's particular freedom or right always entails at least one other person's specific restraints or obligations. Hence you must always provide further specification, in each context of use—whose freedom, to do what, as against whose required restraint, from doing what—before you succeed in saying anything at all with the terms "freedom" or "liberty."

This is what absolutist libertarians, as well as some fundamentalist liberals, tend to miss when they take themselves to be disagreeing about the importance of "liberty," rather than about the relative importance of this liberty as against that liberty.

To possess liberty is to be free. And to be free is to be free to do something or other, or to be free of some restraint or other. But as soon as you agree to this point, you agree that there is a tradeoff. For freedom's always being freedom "to" or freedom "from" imparts to liberty an inevitable conflict—one's being more free in one respect always and everywhere entails others' being less free in other respects.

So liberty involves tradeoffs. You gain "freedom"—the "optimal degree" of freedom—only by relinquishing some, lesser freedoms for other, greater freedoms.

What is it for some freedoms to be "lesser" than others, such that "freedom" on balance is gained when the lesser are traded for "greater" freedoms? A few examples might shed some light here.

Consider first, then, the case of language: By conforming the sounds that you utter and the marks that you put down on paper to certain rules—a form of grammatical regulation—you make yourself understandable to others, as well as to yourself. You thereby expand your sphere of freedom. For you are able to do more when you are able to think articulately and to communicate.[1] In conforming to linguistic rules, then, you trade a trifling freedom—the freedom to emit meaningless grunts or marks on paper at a particular instant—for a weightier one—the capacity to persuade others to join forces with you and thereby lever your efforts and productive potential, and hence your sphere of material freedom.

Contracts, the binding cement of liberal market societies,[2] provide yet another example of this familiar trading off of lesser freedoms for greater freedoms. Parties to contracts are said to "bind" themselves to the terms they negotiate into those contracts. They thereby relinquish their freedom to act in ways contrary to the agreed terms, precisely in order to free up the benefits that collaborative contracting releases. The freedom of contract so dear to liberals and libertarians alike is in this sense the freedom to relinquish some freedoms in exchange for other freedoms that would otherwise not be available.

"Maximizing" liberty, then, involves trading off freedom for freedom because freedom is multidimensional. And disagreements over how to maximize liberty are accordingly disagreements over which dimensions trump which.

Libertarian Welfare

The economist Robert Frank has thought long and hard, over a well-distinguished if still youthful career, about the multidimensionality of freedom—the omnipresent liberty-cost of liberty itself, as we might call it. Hence he finds himself by turns amused and dismayed, as surely do most of us, by the truistic nostrums of the current crop of Ayn Rand–quoting libertarians who have broken out like a plague on the land.

The original working title of Frank's latest and most sophisticated treatment of liberty and economy to date—"The Libertarian Welfare State"—highlights the liberty tradeoff with as much force as it does irony. The central argument of this important new work—now titled *The Darwin Economy*—is that to be an authentic libertarian is to repudiate most of what goes by the false name of economic "libertarianism." Many of today's libertarians, in other words, are not real libertarians.

The reason is that authentic libertarians contracting together to form a new society from scratch, as Frank convincingly demonstrates, would almost certainly design a polity with much more robust regulatory regimes and social safety nets than those associated with even the more or less Democratic Clinton years in America. Yet today's self-styled libertarians, Frank demonstrates again and again through a remarkable battery of specific examples, seldom if ever so much as notice the inherent liberty-for-liberty tradeoff that all freedoms entail.

The question has never been, Frank notes, whether you should be free, I should be free, or we should be free. He says "yes" to all of those. But to supply that answer, he shows, is to see how little is actually said by today's self-styled libertarians. The nontrifling questions, which the self-styled libertarian seldom so much as notices, let alone grapples with, are what your freedoms should be in relation to me, what mine should be in relation to you, and how we are to maintain the settlement at which we arrive when we work out this tradeoff.

To think carefully about and then carefully answer these questions—to address them together as if solving a system of simultaneous equations—Frank effectively argues, is to lay the broad contours of what he calls the libertarian welfare state. This is a state in which "social Darwinism" means something rather different, and more plausible, than what acolytes of Herbert Spencer had in mind one hundred years ago.[3]

Libertarian Harm

Frank takes as the starting point in his inquiry that venerable libertarian formula offered by J.S. Mill in his celebrated essay "On Liberty."[4] This is the maxim that all should enjoy the maximum possible sphere of freedom consistent with no one's harming anyone else—a formulation that has since come to be known, thanks especially to the philosopher Joel Feinberg, as "the harm principle."[5]

So far, so good, Frank observes. But God and the devil are in the details of "harm." For what is to count as harm of the sort referenced in the harm principle? Is the "harm" involved in enforcing the laws via fines or imprisonment, for example, and hence the enforcement of law itself, to be eschewed in a free society? Surely not, else other harms—the harms wrought by crimes—become abundant.

What, then, is the appropriate baseline of prelegal, prepolitical entitlements in relation to which harm is to be recognized and measured for liberal and libertarian purposes, in order that we might legislate against illegitimate harms in the interest of sustainably maximizing legitimate liberty?[6]

As it happens, early modern political philosophers and contemporary justice theorists have concerned themselves with this very question. And Frank the polymath economist turns out in many ways—advertently or otherwise—often to be both their equal in sophistication and their sorely needed complement in capturing what often has slipped through their nets.

Surely one of the more initially surprising—and yet in retrospect, brilliant—turns in Frank's book is the author's proceeding directly from Mill to . . . Ronald Coase? Yes, Coase. Coase is best known for two pathbreaking articles, each of which initiated at least one new subfield of economics, and both of which jointly earned him the Nobel Prize. Both articles broke new ground by posing surprisingly naive questions that no one apparently had seen fit to ask—questions of a kind that Robert Frank excels at formulating. The answers to questions like these often carry surprisingly deep implications.

The first of Coase's two referenced articles, "The Nature of the Firm," published in 1937, wondered aloud why, where the production of goods and services is concerned, there are more or less perpetual, hierarchically organized firms rather than mere ad hoc networks of contractual relations.[7] The answer at which Coase arrived was that search and transaction costs, which operate in ways similar to frictions in the field of mechanics, rendered these hierarchies and bureaucracies efficient. This laid the groundwork for the new fields of "transaction cost economics" and the "theory of the firm."

The second article for which Coase is best known, and from which Frank takes his own cue in advancing past Mill, drew additional conclusions from the transaction costs insight that emerged from the first article. In this article, "The Problem of Social Cost," published in

1960, Coase noted our tendency to assume that a legally actionable nuisance runs in just one direction.[8] But why, without further argument, Coase queried, simply assume that the source of the putative nuisance should be saddled with the liability?

To cite Coase's own example, if a factory adjacent to a doctor's office renders the practice of medicine in that office more difficult, that is assuredly a "nuisance" to the doctor, and to his patients at any rate. But is legally requiring the factory to relocate or else cease and desist from production not also a nuisance—in this case, to the factory owner and the consumers of the factory's products? And, if so, then on what ground shall we decide which nuisance is to be legally recognizable, such that all have a right not to be bothered by it?

Coase went on to offer a prescription for how to settle the question. Frank finds this suggestion quite helpful—I am somewhat more skeptical, and so we'll return to it. For the moment, however, the important point is that Coase poses the question at all. For in so doing, Frank reminds us, Coase was doing precisely what many of today's libertarians conspicuously fail to do.

Coase asks, in effect as a follow-on question to Mill's libertarian "harm principle," what is the harm? Or: where is the harm? Who is harmed? He asks, in other words, for further specification of the sort noted above in introducing this review essay.

We must address this if we are coherently to address the question of when your freedom does not simply encroach upon my freedom, as all freedoms do, but encroaches illegitimately upon it, thereby giving content to Mill's otherwise empty harm principle. This is the question that simple libertarians do not bother to ask, but which coherent libertarians must ask—and answer. Frank in his book does this for them, again and again. The answers at which he arrives jointly constitute the libertarian welfare state.

A Libertarian Social Contract

What is that state, then? In constructing his answer, brick by brick as it were, Frank sketches in broad outline what a polity designed by thoughtful libertarians—of which he considers himself to be one—would look like. In imagining the process of design and construction, in turn, Frank has recourse to that venerable liberal and libertarian device that I mentioned above—the institution of contract.

Frank hereby joins that time-honored company of social contractarians who for centuries have asked what free people designing a new state from scratch would agree upon and then bind themselves to. He is, in other words, writing squarely in the tradition of Hobbes, Grotius, Locke, Rousseau, Harsanyi, Rawls, Kolm, Dworkin, Moulin, and Roemer.[9] And, remarkably—since he does not advertise himself as a contributor to this venerable line of work—he both holds his own with and decisively contributes to the corpus of work that constitutes this influential tradition.

Suppose, Frank suggests, some deluge were to befall us, humanity were then to rescue itself by clambering aboard arks, and in consequence we now would be faced with the opportunity to start the world over again. What sorts of arrangements might thoughtful libertarians make under such circumstances? The answer, Frank suggests, is that they would ultimately construct something very much like the modern welfare state—a state administered by a government duly authorized by the citizenry as a collective agent charged with solving a host of formidable collective action problems.

Social Contracts and Collective Action Problems

To appreciate just how ingenious, and indeed ultimately plausible, Frank's argument is here, it is helpful to remind ourselves of two things. The first is that which we noticed above in introducing the present discussion—namely, that the inherent multidimensionality of liberty is such as to render large freedoms obtainable for the price of small freedoms. Relinquish the freedom not to pay your counterparty on a contract for her performance, and you receive in return her performance. Relinquish your freedom not to perform, if you are the counterparty, and receive in return the contractual payment. And, thereby, per the First Welfare Theorem, maximize both joint and several well-being.

The second thing to remind ourselves of is the nature of collective action problems—problems that turn up in many more places than most seem to realize, including places that Frank in particular has proved remarkably adept at locating.

The hallmark of a collective action problem is its combining two or more individually rational decisions into a collectively irrational, self-defeating outcome. Prisoners' dilemmas and commons tragedies are particularly well known examples. Frank notes others, including arms races and competition for positional goods (those that provide status). There are more examples: bank runs, debt deflations, liquidity traps, "paradoxes of thrift," consumer price hyperinflations, and credit-fueled asset price hyperinflations, better known as "bubbles."[10] (These latter constitute a subclass that self-worsens due to circular "self-fulfilling prophecy" properties.)[11]

In all these cases, it is at least rational for each party to act in a manner that, when all act thus rationally, ends up harming everyone. A corollary is that no individual can, acting alone, change this dynamic. To act contrary to it is individually self-defeating just as everyone's going along with it is collectively self-defeating. Exit the arms race, for example, and your opponent wins; yet both stay in it, and you both waste resources. Don't shed labor in a recession, by way of additional example, and your competitors are more profitable; yet all shed labor and you shrink consumer demand in a manner that cuts into profits yet further. And so on. Damned if you do, together, and damned if you don't, individually.

All who fall into these problems are accordingly trapped by them. (Hence the "liquidity trap," which is another well-known example.) They wish to escape but, acting individually, cannot. Hence individually they are unfree.

The solutions to these problems accordingly bring greater freedom to those who act to secure them. But the action in question must be "collective" in these cases. Hence gains in freedom are had, in such cases, only in exchange for the sacrifice of lesser freedoms.

How? In some cases, the trade is effected by a two- or several-party contract, in the way noted above. Arms control agreements between two or a few parties are cases in point. In other cases, the trade is effected by broader contract—even "social contract" of the kind envisaged by the classical liberal political philosophers.

The latter sort of contract is the kind Frank envisages being negotiated and agreed to by those who step off his post-deluge arks. In this case, like those of his classical antecedents, the multiple parties to the contract delegate collective agency to an agent who acts as their fiduciary. Hobbes called it the prince. Locke called it the state. We call it our government and its various instrumentalities.

A government solves the collective action problem that is a credit-fueled asset price bubble, for example, by raising collateral requirements or interest rates economy-wide so as to close the spread between low borrowing costs and high capital gains appreciation rates that renders it rational for individuals to take part in the unsustainable borrowing binge. During a debt deflation such as that which many in the world—including ourselves—are now living through, it does the opposite, or it spends in place of the individuals who find it irrational to do so in the face of possibly lower prices or further diminished employment opportunity in the near future.

Frank's government would act as a collective agent on behalf of all by, among other things, progressively taxing the purchase of luxury goods of the kind that figure into positional goods arms races. This is a classic collective action problem, insofar as each participant in the race would rather the race be ended but cannot end it simply by unilaterally "disarming."

In all such cases, the state is simply that instrument—that duly appointed collective agent—through which we all collectively address the most serious collective action problems that limit our freedom. We free ourselves of the treadmills that these problems constitute. We thereby gain liberty—we become more free. But we do so, as all contracts—"social" or otherwise—and indeed all purchases of greater freedom do, by trading off less valued freedoms—the "freedom" to violate the contract, for example, or to steal from or "free ride" on the labor of others.

Libertarian Collective Action

Frank's libertarian welfare state is the one that libertarian pilgrims would likely select upon stepping off their arks to address mutual challenges of the mentioned variety. It is a "welfare" state, in turn, both because it maximizes the degree to which we fare well when it addresses these problems, and because it turns out to look much like the traditional "welfare state" of times past—the state envisaged by New Dealers and proponents of the Johnsonian "Great Society."

It is the last of these claims that will likely be most surprising to some readers. Hence it will be well to say more about how Frank gets there.

The easiest way to trace Frank's path is to focus on his most emblematic and initially counterintuitive claim, which is that libertarians stepping off the ark actually would choose salary and taxation arrangements that redistribute much income downward from the top of the ladder. How can he possibly believe that? you might ask. Frank's answer is ingenious, well grounded in his earlier theoretical and empirical work,[12] and a critically important addition—a bona fide new contribution—to the grand tradition of rigorous social-contractarian justice theory.

Here is how Frank's argument proceeds. It is a familiar move in the social-contractarian tradition, particularly as carried forth by Harsanyi, Rawls, and, later, Dworkin,[13] to suggest that parties choosing social and economic arrangements from behind a veil of ignorance where they do not yet know their talents—or at least those talents' marketability—would in effect purchase some quantum of insurance against talentlessness and poverty. One then argues that social insurance arrangements of the kind familiar to the traditional welfare state in effect replicate—or "mimic"—some such "hypothetical" but impracticable insurance market.

Much ink continues to be spilt over this familiar methodological conceit.[14] But Frank sidesteps all these arguments by opening an altogether new front in the contest. He does so by first attending to something to which economists, more than political philosophers, tend to accord attention, and then by attending to something to which he in particular has paid close attention over the years.

The first of those things is the familiar phenomenon of scale economies. Larger productive units, and with them larger societies, Frank notes, tend to produce more in the way of wealth out of a given stock of inputs. Hence there is value even to the most talented members of any society in having additional members of that society. Ten talented people will tend to fare better in combination with ninety additional less talented people than they will by themselves. Hence they will find reason to agree, as a condition to those ninety's entering into society with them once leaving the ark, to share some of their subsequent surplus with the other ninety.

The second phenomenon to which Frank attends—in this case, again—is that of positional goods.[15] People at the top of a hierarchy tend to value that status itself. Indeed, typically their relative positions mean more to them than their absolute positions. "Toppers" are able to achieve such status, however, only so long as others are willing to be members of the same groups with them. You cannot reach or stay at "the top" acting alone, any more than all the children of Lake Wobegon can be "above average." For "top" is a relative term, as we noted above "liberty" to be, and just as Coase noted "nuisance" to be.

But since (a) no free individual stepping off the ark need join with anyone else, and since (b) comparatively less-talented people would be free to join with one another and not with more-talented people, it follows that (c) people of the latter sort will have to compensate others should they wish to secure status and other positional goods. Just as there is no such thing as a free lunch, Frank in effect says, so is there no such thing as free positionality at the top of a hierarchy. Et voilà, Frank shows us something that has been there in plain sight all along but which none of us are apt to have noticed. And the implications are far-reaching indeed.

One such very important implication is that redistributive taxation, as Frank observes, can be interpreted as the price paid by toppers for their status in the social hierarchy. Those at the top compensate those at the bottom so as to make it worth their while not to join other groupings in which they would perhaps be less wealthy in absolute terms but more wealthy in relative terms—the latter, again, typically being more important to people. Were the toppers not to make those payments per the terms of our envisaged post-deluge social contract, and accordingly to live only among others who share their degrees of talent, they would suffer a welfare loss. For in their resultant societies they would be merely average. Hence progressive taxation is simply the price that a post-deluge "market" would assign to high status in a hierarchical society that can only be purchased from willing low-status participants-to-be.

What we have here, then, is a very clever argument for why libertarians themselves would sign on to the well-known Rawlsian "difference principle."[16] That, as some readers will recall, is the principle that inequalities are presumptively wrong, and can be justified only if they improve the absolute condition or level of the least advantaged. A conundrum of justice theory ever since Rawls has been how to justify the claim that this principle "would" be affirmed from behind the veil.

As Arrow noted as early as 1974, offering the difference principle as a likely counterfactual choice from behind the veil, if justified on the grounds on which Rawls justifies it, is tantamount to ascribing an infinite degree of risk-aversion to those behind the veil.[17] The variant of individual decision theory implied by Rawls's decision procedure is accordingly what Roemer has labeled, with characteristic understatement, "exotic."[18]

What Frank does is to justify the difference principle by rather less exotic and more plausible means—essentially by flipping it. Rather than claiming that the least advantaged would happily trade off massive degrees of relative advantage for small increments of absolute advantage, as Rawls does, he suggests that the most advantaged would offer significant degrees of absolute advantage in return for the relative advantage that others' joining them in society enables. On this reading, the difference principle states the terms of a contract among libertarians, pursuant to which preening Veblenian peacocks pay others for the privilege of strutting and showing their tails.

Once he has established the positional-libertarian-contractarian credentials of redistributive taxation in this way, Frank goes on to show

how characteristic feature after feature of the modern liberal welfare state can be justified in precisely the same way. Among them are the provision of sundry essentially public goods such as education, health insurance, unemployment insurance, and the like; and the regulation of many externality-imposing public ills, such as environmental degradation and excessive financial speculation. In effect, collective action problems of the kind noted above render adequate private provision of these goods impossible. Hence collective—that is, public—provision would be socially contracted for by rational libertarians themselves in order to maximize their spheres of personal freedom.

In case after case, then, Frank shows convincingly that authentic libertarians recognizing equal spheres of liberty on the part of others and forming a state with them would contract for much that we in the West have taken to be legitimate functions of government since the advent of the modern era. The result is a challenge to vulgar libertarians—and some more sophisticated libertarians as well—that they are apt never to have encountered before. In essence, it is the challenge to show how their own libertarianism, accompanied by recognition of the equal liberty of all, could not entail acceptance of a state welfare apparatus significantly more robust even than we have now.

Conclusion: Coherent Libertarianism

The foregoing observations have barely scratched the surface of Robert Frank's deep, lucid new book. At best they convey some feel for the novelty and profundity of Frank's fresh take on matters of political philosophy and economic policy alike. Happily, however, there is little need here to be more than skeletal and impressionistic. For Frank's arguments and prose style, as in all of his work, are so clear and gracefully presented as to render reading him a nearly effortless and always enjoyable experience.

The present reviewer, then, simply cannot recommend this book too highly. All concerned citizens, and especially those intrigued by the recent outburst of libertarian argumentation in American political dialogues, will do well to read Frank's latest contribution.

None of them—least of all thoughtful libertarians—will ever see libertarianism and its putative clash with the welfare state in the same way again.

Notes

1. Note the Latin root *commune* in "communicate."

2. Note the etymology again, per which "contract" is a cognate of "contraction." Freedom of contract is freedom to rein in—to contract—one freedom in the interest of expanding another freedom.

3. See Herbert Spencer, *Social Statics: The Conditions Essential to Human Happiness Specified, and the First of Them Developed* (London: John Chapman, 1851); *Lochner v. New York*, 198 U.S. 45 (1905).

4. See J.S. Mill, *On Liberty* (1869), available at www.bartleby.com/130/.

5. See Joel Feinberg, *The Moral Limits of the Criminal Law*, 4 vols. (New York: Oxford University Press, 1982–1994).

6. See *Palko v. Connecticut*, 302 U.S. 319 (1937) (opinion of Mr. Justice Cardozo).

7. See Ronald M. Coase, "The Nature of the Firm," *Economica* 4, no. 16 (1937): 386–405.

8. See Ronald M. Coase, "The Problem of Social Cost," *Journal of Law & Economics* 3 (1960): 1–44.

9. See Thomas Hobbes, *Leviathan* (1651); Hugo de Groot, *De Jure Belli ac Pacis* (1625); John Locke, *Second Treatise of Civil Government* (1690); J.-J. Rousseau, *Du contrat social* (1762); John Harsanyi, "Cardinal Utility in Welfare Economics and in the Theory of Risk-Taking," *Journal of Political Economy* 61, no. 5 (1953): 434–35; John Harsanyi, "Cardinal Welfare, Individualistic Ethics, and Interpersonal Comparisons of Utility," *Journal of Political Economy* 63, no. 4 (1955): 309–21; John Rawls, *A Theory of Justice* (Cambridge: Harvard University Press, 1971); Serge-Christophe Kolm, *Justice et équité* (Paris: Edition du Centre national de la recherche scientifique, 1972); Ronald Dworkin, *Sovereign Virtue* (Cambridge: Harvard University Press, 2000); Hervé Moulin, *Cooperative Microeconomics* (Princeton: Princeton University Press, 1995); John E. Roemer, *Theories of Distributive Justice* (Cambridge: Harvard University Press, 1996).

10. See Robert Hockett, "Recursive Collective Action Problems," *Journal of Applied Economics* 5 (2013): 1–45.

11. Ibid.

12. See, e.g., Robert H. Frank, "Positional Externalities Cause Large and Preventable Welfare Losses," *American Economic Review* 95, no. 2 (2005): 137–41.

13. See Dworkin, *Sovereign Virtue;* Harsanyi, "Cardinal Utility"; and Rawls, *Theory of Justice.*

14. See, e.g., Norman Daniels, *Justice and Justification* (Cambridge: Cambridge University Press, 1996).

15. See Frank, "Positional Externalities."

16. See, of course, Thorsten Veblen, *The Theory of the Leisure Class: An Economic*

Study of Institutions (New York: B.W. Huebsch, 1899). On the difference principle, see Rawls, *A Theory of Justice.*

17. See Kenneth J. Arrow, "Some Ordinalist-Utilitarian Notes on Rawls's Theory of Justice," *Journal of Philosophy* 70, no. 9 (1973): 245–63.

18. See Roemer, *Theories of Distributive Justice.*