Chapter Three
State Policies That Promote Corporate Size and Centralization

Capitalism, if we take it in R.A. Wilson's sense of a political and economic system in which the state intervenes in the market on behalf of capitalists, has been exploitative since the beginning.

It was established at the outset by massive acts of state robbery and restrictions on liberty: the so-called "primitive accumulation" by which the peasantry's property in the land was expropriated, the Laws of Settlement which acted as an internal passport system restricting movement of the working class, the Combination Laws which restricted the bargaining power of labor, and the mercantilism and imperial aggression by which the so-called world market was created. These matters fall too far outside of our focus for detailed examination. A summary of all the uses of force involved in the establishment of capitalism can be found in Chapter Four of *Studies in Mutualist Political Economy.*[1]

Once established on this basis, the system was maintained through various state-enforced legal privileges. This, also, is too far outside the scope of the present chapter to examine in depth. The main forms of privilege that existed before the rise of corporate capitalism in the nineteenth century were the "Four Monopolies" summarized by Benjamin Tucker in "State Socialism and Anarchism," and will be considered in greater depth in our examination of privilege in Chapter Eleven.

Our main concern here is not with this earlier system of privilege, but more specifically with the state's later role in the creation and development of the corporate economy, the concentration of capital, and the centralization of production. We will show what specific policies of the state have promoted the domination of the economy by corporations grown far beyond the point of maximum efficiency.

Our focus in this chapter is primarily on the ways in which the state promotes large corporate interests. But I should mention that in fact the symbiosis works very much both ways: the large corporation tends to promote state interests. The state has a special affinity for the large corporation because it is more "statelike" in structure and internal culture, and it finds it more amenable as well as an instrument of state interests. Benjamin Darrington puts it quite well:

> Large centrally organized firms facilitate the government's task of maintaining its hegemonic position in society. The ability of the government to effectively regulate the economy depends on the existence of economic institutions with organizational structures that can be easily monitored and controlled. The regulation of a large number of small businesses requires greater duplication of effort to inspect financial

[1] Kevin A. Carson, *Studies in Mutualist Political Economy*.

> records, ensure regulatory compliance, and collect taxes. Small organizations are harder to punish for not cooperating with the law because they have less total value to seize and the owners are more likely to fight the government because it is their money and business directly at stake, not to mention the fact that small business [sic] are looked upon more favorably by the general population than seemingly faceless and distant corporations. The equipment used by small enterprises does not lend itself to certification, regulation, and safety testing, and the labor employed does not lend itself to the effective enforcement of laws concerning things like labor negotiations, minimum wage, minimum age, professional licensing, racial and sexual quotas, citizenship requirements, maximum hours, etc. Informal and small scale economic relationships are almost beyond the range of government efforts to enforce its mandates and collect taxes. By making business an agent of policy the state also creates a useful scapegoat for diverting the ire of the public towards the iniquity and exploitation of existing economic relations and positions the state to act as "white knight" to protect the public and avenge the evils and excesses of "private enterprise."[2]

The latter is parallel to the way corporate apologists use "big government" as a bogeyman. In fact the real relationship between big government and big business has always been primarily mutually supportive, and the enmity between them has been manufactured largely for the proles' consumption.

As we shall see below, to some extent it's meaningless even to draw a clear dividing line between the centralized state and the centralized corporate economy. It makes more sense, simultaneously, to see the state as an "executive committee" of the corporate ruling class, largely instrumental to the corporate interests in control of the state apparatus, and to see the corporation as a branch of the state. The latter is especially true in the case of "private" businesses conducting surveillance of their customers on behalf of the state (e.g., "know your customer" laws in the banking industry, hardware and drug stores monitoring purchases of potential methamphetamine components, AT&T's cooperation with warrantless wiretapping, etc.).

I. THE CORPORATE TRANSFORMATION OF CAPITALISM IN THE NINETEENTH CENTURY

The regime of legal privilege described above, predating the corporate transformation of capitalism, took the form primarily of unequal exchange on the individual level, whether it was the sale of labor-power on disadvantageous terms in an unequal labor market, or the purchase of goods on unequal terms because of patents, copyrights and tariffs. The individualist anarchists, habituated to view exchange largely in such individualistic terms, mostly neglected the structural changes in the American economy--

[2] Benjamin Darrington (economics undergrad, Yale University), "Government Created Economies of Scale and Capital Specificity" (2007), pp. 7-8. Paper presented at Austrian student conference.

the tendency toward the concentration of capital and the centralization of production--and the ways that the tariff and intellectual property monopolies promoted these structural changes. In addition, Tucker and the other individualists for the most part ignored the organizational ties between the corporation and the state, the state's increasing assumption of the corporation's operating expenses through direct subsidies, and the state's limitation of competition between large corporations through its cartelizing regulations.

Later in life, when Tucker took note of the trusts, he became pessimistic about the potential for reversing the concentration of economic power through the mere elimination of privilege. He feared that the great trusts had grown so large, and the concentration of wealth so great, that they might be self-perpetuating even without further state intervention.

> Forty years ago, when the foregoing essay was written, the denial of competition had not yet effected the enormous concentration of wealth that now so gravely threatens social order. It was not yet too late to stem the current of accumulation by a reversal of the policy of monopoly. The Anarchistic remedy was still applicable.
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> Today the way is not so clear. The four monopolies, unhindered, have made possible the modern development of the trust, and the trust is now a monster which I fear, even the freest banking, could it be instituted, would be unable to destroy. As long as the Standard Oil group controlled only fifty millions of dollars, the institution of free competition would have crippled it hopelessly; it needed the money monopoly for its sustenance and its growth. Now that it controls, directly and indirectly, perhaps ten thousand millions, it sees in the money monopoly a convenience, to be sure, but no longer a necessity. It can do without it. Were all restrictions upon banking to be removed, concentrated capital could meet successfully the new situation by setting aside annually for sacrifice a sum that would remove every competitor from the field.
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> If this be true, then monopoly, which can be controlled permanently only by economic forces, has passed for the moment beyond their reach, and must be grappled with for a time solely by forces political or revolutionary. Until measures of forcible confiscation, through the State or in defiance of it, shall have abolished the concentrations that monopoly has created, the economic solution proposed by Anarchism and outlined in the forgoing pages – *and there is no other solution* – will remain a thing to be taught to the rising generation, that conditions may be favorable to its application after the great leveling. But education is a slow process, and may not come too quickly. Anarchists who endeavor to hasten it by joining in the propaganda of State Socialism or revolution make a sad mistake indeed. They help to so force the march of events that the people will not have time to find out, by the study of their experience, that their troubles have been due to the rejection of competition. If this lesson shall not be learned in a season, the past will be repeated in the future....[3]

[3] 1926 "Postscript to State Socialism and Anarchism," in *Individual Liberty*

But even then, he seemingly viewed such concentration of wealth as the result of the prior operation of the Four Monopolies, working on an individual level. So his pessimism, arguably, reflected a failure to consider the extent to which the power of large corporations depended on state intervention on a *structural* level, subsidizing and protecting them as organizations. Perhaps, then, we need not be so pessimistic.

As we shall see later in this chapter, Gabriel Kolko showed that the large trusts at the turn of the twentieth century were not able to maintain their market share against more efficient smaller firms. The stabilization of most industries on an oligopoly pattern was possible, in the end, only with the additional help of the "Progressive" Era's anti-competitive regulations. The fact that the trusts were so unstable, despite the cartelizing effects of tariffs and patents, speaks volumes about the level of state intervention necessary to maintain monopoly capitalism. But without the combined influence of tariffs, patents, and railroad subsidies in creating the centralized corporate economy, there would not have been any large corporations even to *attempt* trusts in the first place. The corporate transformation of the economy in the late 19th century--made possible by the government's role in railroad subsidies, protectionism, and patents--was a necessary precondition for the full-blown state capitalism of the 20th century.

The corporate revolution, and the domination of the economy by firms operating on a continental scale, followed the completion of the national railroad system. The corporate economy was made possible by high industrial tariffs and the full-scale subsidy of "internal improvements"--along with corporate personhood, "substantive due process," and the rest of the legal regime growing out of the Fourteenth Amendment. The creation of the latter legal regime was analogous, on a smaller scale, to the legal regime of Bretton Woods and GATT that provided a political structure for global capitalism after WWII.

A. The Nineteenth Century Corporate Legal Revolution.

The American legal framework was transformed in the mid-nineteenth century in ways that made a more hospitable environment for large corporations. Among the changes were the rise of a general federal commercial law, general incorporation laws, and the status of the corporation as a person under the Fourteenth Amendment. The cumulative effect of these changes on a national scale was comparable to the later effect, on a global scale, of the Bretton Woods agencies and the GATT process: a centralized legal order was created, prerequisite for their stable functioning, coextensive with the market areas of large corporations.

The federalization of the legal regime is associated with the recognition of a general body of federal commercial law in *Swift v. Tyson* (1842), and with the application of the Fourteenth Amendment to corporate persons in *Santa Clara County v. Southern Pacific*

Railroad Company (1886).

It was originally held under American constitutional law that there was no general body of federal commercial law--only case law developed pursuant to the specific and limited delegated powers of Congress. The diversity of citizenship jurisdiction of the federal courts--their jurisdiction over disputes between citizens of different states, included in the grab-bag of comity provisions in Article IV--was not pursuant to the federal government's power to regulate commerce, but was simply intended to promote comity between the states. Cases in diversity jurisdiction were to be decided, not on the basis of any general federal commercial law, but on the basis of the law of the state in which the tort or contract took place. Until *Swift v. Tyson*, this state law was taken to include the case law which explicated it. *Swift v. Tyson* held that the law of the state consisted only of statute law; as Justice Story argued,

> in the ordinary use of language, it will hardly be contended that the decision of courts constituted laws. They are, at most, only evidence of what the laws are, and are not, of themselves law.

The federal judiciary, therefore, was governed in its diversity jurisdiction only by state statutes, and not state case law. The federal judiciary was free to develop its own body of judge-made common law--to judge according to "the general principles of commercial law"--in deciding diversity cases.[4] The state courts, at best, were to be treated, as the King's Bench and other royal courts had been in the early decades after independence: as sister courts whose decisions deserved respect as learned explications of the common law, but carried no binding authority. As Horwitz argued, Story's opinion was a throwback to the understanding of the common law as "found, not made," a general body of principles accessible to reason, which had almost entirely collapsed by that time in the face of the modern understanding of positive law.[5]

The Santa Clara decision[6] was followed by an era of federal judicial activism, in which state laws were overturned on the basis of "substantive due process." The role of the federal courts in the national economy was similar to that of the contemporary World Trade Organization on a global scale, with an "international" tribunal having the power to override the laws of local jurisdictions which were injurious to corporate interests. This is not, please note, a defense of such local legislation when it interferes with legitimate property rights and freedom of contract. But such libertarian centralism--an "international" legal regime that spares private actors the transaction costs of negotiating their own terms under the rules of local sovereignties, by superimposing an overarching

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[4] In Morton Horwitz, *The Transformation of American Law 1780-1860* (Cambridge and London: Harvard University Press, 1977), p. 245.
[5] Ibid. p. 246.
[6] 118 U.S. 394 (1886), http://caselaw.lp.findlaw.com/scripts/getcase.pl?navby=CASE&court=US&vol=118&page=394.

sovereignty--is of dubious legitimacy.

And in practice, the "due process" and "equal protection" rights of corporations as "juristic persons" have been made the basis of protections against legal action aimed at protecting the older common law rights of flesh and blood persons. For example local ordinances to protect groundwater and local populations against toxic pollution and contagion from hog farms, to protect property owners from undermining and land subsidance caused by coal extraction--surely indistinguishable in practice from the tort liability provisions of any just market anarchy's libertarian law code--have been overturned as violations of the "equal protection" rights of hog factory farms and mining companies.

> Four years ago, Robertson and the other [Clarion County Pennsylvania] supervisors were debating an ordinance to restrict the spreading of toxics-laden sewage sludge on local fields—a major issue in an area that has become a destination for waste from Pittsburgh. The supervisors knew that messing with big business could come at a price: Three years earlier, another Pennsylvania township had passed an anti-sludge ordinance, only to be sued by a sludge hauler called Synagro, which argued that the township had infringed on its rights under the 14th Amendment, passed after the Civil War to guarantee "equal protection" to all....
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> After *Santa Clara*, federal judges began granting more and more rights to nonliving "persons." In 1922, the Supreme Court ruled that the Pennsylvania Coal Co. was entitled to "just compensation" under the Fifth Amendment because a state law, designed to keep houses from collapsing as mining companies tunneled under them, limited how much coal it could extract....
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> BY THE LATE 1990S, fear and anger over sludge application in rural Pennsylvania—fueled by the deaths of an 11-year-old who got sick after riding his dirt bike through a sludge-treated field, and a 17-year-old who fell ill after exposure to sludge at a farm—was running high. Thomas Linzey found himself fielding calls from local officials desperate for ways to battle the "biosolids" applicators, as well as the corporate hog farms whose stench sickened people for miles around. Municipalities had been used to keeping those nuisances at bay with their own waste ordinances; but in 1997, in response to agribusiness lobbying, the state began enforcing a law that invalidated the local rules. Residents packed schools and fire stations to air their grievances. "These are the people with the shitkickers and the John Deere hats," Linzey says. "These are the people who salt the roads in the wintertime and fix the roads in the summertime. We had rural farmers coming to community meetings with the Declaration of Independence in their back pockets."

In response to local regulation of toxic sludge, the Pennsylvania Chamber of Business and Industry's newsletter sounded the alarm over a "stronger force than evil space invaders: the radical agenda of militant environmentalists that seems to have taken possession of the township supervisors." One corporation sued, claiming that the township's restrictions violated its rights with regard to "equal protection, due process, taking without just compensation, and rights guaranteed under the commerce clause." Last year, agribusiness took the fight to the state Legislature, supporting a law under which the state attorney general could sue any local government for passing an ordinance that "prohibits or limits a normal agricultural operation."[7]

The phrase "normal agricultural operation," by the way, foreshadows a later theme in this chapter: the ways in which the federal regulatory state has preempted and overriden older common law standards of liability, replacing the potentially harsh damages imposed by local juries with a least common denominator of regulatory standards based on "sound science" as determined by industry.

More important than either of the above changes, however, is the general change in corporate law: a move toward general incorporation laws at the state level, and the rise of corporate entity status[8] under both state and federal law.

Robert Hessen has argued that general incorporation under statute law provides no benefits that could not be achieved by simple private contract.[9]

Piet-Hein Van Eeghen, however, raises the question of whether the entity status of the corporation, distinct from any or all of the individual stockholders, could be established solely by private contract.

> While it is common to list various typical corporate features, such as entity status, limited liability and perpetuity, there is really only one defining feature: entity status. Entity status means that certain legal rights and duties are held by the corporation as a separate, impersonal legal entity. In the case of the private business corporation, entity status implies that title to the firm's assets is held by the corporation in its own right, separate from its shareholders.
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> Illustrative of the fact that the corporate form of private enterprise deviates from traditional forms of private property, entity status renders the legal position of both corporate shareholders and managers (directors) awkward and ambiguous. As for corporate shareholders, they are commonly regarded as the owners of the corporation, but they are owners only in a limited sense. Shareholders do not have title to the assets of the corporate firm, but merely possess the right to appoint management and to receive dividends as and when these are declared; title to the firm's assets reverts

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[7] Barry Yeoman, "When Is a Corporation Like a Freed Slave?" *Mother Jones*, November-December 2006. <http://www.motherjones.com/news/feature/2006/11/when_is_a_corporation_like_a_freed_slave.html>.
[8] The evolution of legal theory regarding the corporate entity status is discussed at length by Morton Horwitz in *The Transformation of American Law, 1870-1960: The Crisis of Legal Orthodoxy* (New York and Oxford: Oxford University Press, 1992), pp. 65-107.
[9] Robert Hessen. *In Defense of the Corporation* (Stanford, Calif.: Hoover Institution, 1979).

back to shareholders only when its corporate status is terminated. The lack of ownership rights over assets is illustrated by the fact that, in contrast to partners in an unincorporated partnership, corporate shareholders cannot lay claim to their share of the assets of the corporate firm nor do they have the right to force their co-partners to buy them out. Corporate shareholders can liquidate their investment only by selling their shares to third parties. In short, the ambiguity in the legal position of shareholders lies in the fact that, while certain traditional ownership rights rest with them (profit accrual and power to appoint agents to manage the firm for them), other traditional ownership rights are exercised by the corporation as a legal entity separate from them (title to the firm's assets).

As for corporate management, their legal position is equally ambiguous. Managers are appointed by directors who are the representatives of shareholders. Ultimately, management is thus the agent for shareholders, managing the corporation as their representative. This, however, is only part of the picture. While management is the agent for shareholders in the sense of being ultimately appointed by and accountable to them, it is also the agent for the corporation itself. After all, in order to manage the corporation's assets, management must legally represent the corporation as the titleholder to these assets. And because the corporation is an impersonal legal entity, agency for the corporation lends a significant degree of autonomy to the position of management, which is precisely why it has proved so difficult to make shareholder control over management more effective, despite the many legislative measures aimed at enhancing management accountability to shareholders. The significant degree of autonomy inherent in the legal position of corporate management was, of course, the main theme of Berle and Means's (1932) seminal work on the corporation. To sum up, the position of management is ambiguous because management acts as agent for two principals, the shareholders and the corporation.

Other typical features of the corporation like limited liability and perpetuity are not independent, original attributes, but are derived from its entity status.

Shareholders possess limited liability because they do not own the corporation's assets and are, consequently, also not liable for claims against these assets. Responsibility for corporate debt rests with the corporation in its own right rather than with them. Corporate creditors cannot, therefore, lay claim to the personal possessions of corporate shareholders, as they can to the personal possessions of partners in an unincorporated partnership. The most shareholders can lose is their initial investment when buying the shares, which happens only when the corporation goes bankrupt and the shares lose their value. Such is the origin of limited liability for shareholders.

The corporate feature of perpetuity can also be traced back to the corporation's entity status. It is because assets are owned by the corporation in its own right rather than by shareholders that the death or departure of shareholders does not affect its continued existence. While unincorporated partnerships need to be legally reconstituted each time partners leave, die, or are added, corporations continue irrespective of who holds their shares. The corporation's entity status thus gives it a life independent of the life of its shareholders, which is the sense in which it is commonly said to possess perpetuity or immortality.[10]

Van Eeghen argues that general incorporation under statute law is a source of special privilege, insofar as it confers what were previously considered the incidents of statehood, and is therefore impermissible from a libertarian standpoint:

> It has, in fact, always been foreign to common law principles to allow private persons the unrestricted freedom to assign their assets to the ownership of impersonal, and thus state-like, legal entities. As Roy (1997, p. 46) notes: "This feature [entity status] conflicts with a basic tenet of the common law of property: it clouds the distinction between personal rights (in personem) and rights in property (in rem)." In spite of his defense of the corporation, a liberal legal scholar like Richard Epstein (1995, p. 273) agrees that limited liability "deviates from the ordinary common law principles of partnership and agency."[11]
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> Originally only state institutions (central, regional, and local government) possessed corporate status, which seems entirely natural and appropriate. If we wish to escape Louis XIV's infamous dictum "l'état c'est moi" ("I am the state")..., the state should indeed be given a legal entity separate from its officials. Only if such a separation exists can state power be vested in the office rather than the person; and only when state power is vested in the office can it be circumscribed by law....
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> If it is agreed that entity status is indeed a typical attribute of the state, then anarchocapitalists who advocate a stateless society have even more reason to oppose private firms taking on state-like attributes such as happens when they acquire corporate status.[12]

Further, Van Eeghen argues, corporate entity status and all its incidents have had the practical effect of enabling all the negative features commonly identified in critiques of corporate power:

> *(a) Increased Speculative Instability*
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> Because incorporation separates ownership from control, shares in a modern corporation can be traded without necessarily affecting the management nor the

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[10] Piet-Hein van Eeghen. "The Corporation at Issue, Part I: The Clash of Classical Liberal Values and the Negative Consequences for Capitalist Practice" *Journal of Libertarian Studies* Vol. 19 Num. 3 (Fall 2005), pp. 52-54 <http://www.mises.org/journals/jls/19_3/19_3_3.pdf>.
[11] Piet-Hein van Eeghen. "The Corporation at Issue, Part II: A Critique of Robert Hesson's In Defense of the Corporation and Proposed Conditions for Private Incorporation" *Journal of Libertarian Studies* Vol. 19 Num. 4 (Fall 2005), p. 39 <http://www.mises.org/journals/jls/19_4/19_4_3.pdf>.
[12] Van Eeghen, "The Corporation at Issue, Part I," pp. 54, 56.

capital position of the firm. As a result, an active market in such shares develops more easily. By contrast, the shares in an unincorporated partnership are less marketable because they are more strongly linked to the risks and responsibilities of managing the firm, which old owners are more reluctant give up and new owners accept. Moreover, partners normally have the right to consultation in ownership transfers, which also reduces the marketability of ownership stakes in unincorporated businesses.

Unfortunately, marketability and the potential for speculative trading are intimately linked. Since incorporation significantly increases the marketability of ownership stakes, it thereby also enhances the opportunities for speculative activity in share markets. In addition, many of the participants in speculative markets are corporations themselves and thus enjoy a degree of risk protection in the form of limited liability. Because the balance between risk and reward is tampered with, speculative activity is artificially stimulated....

(b) Increased Market Concentration and Concentration of Control

Because the corporate form increases the average firm size, it will also *ceteris paribus* increase the degree of concentration in any given market. Furthermore, because incorporation enhances the marketability of shares as well as the ease with which capital can be raised, it also creates better opportunities to gain market share by mergers and take-overs.

Generally speaking, corporate capitalist practice has strayed far from the free-enterprise ideal of market decisions being taken at a decentralized level by countless relatively small suppliers and demanders so that market outcomes are broadly impersonal. The very invisibility and beneficence of the invisible hand is thus under threat.

(c) Increased Strength of the Profit Motive

Since corporate shareholders are normally so diversified that they become an amorphous mass, only the lowest common denominator of their wishes can be attended to, which is to maximize return on investment—the wish which the greatest number of shareholders have in common. Put differently, the profit motive is given additional impetus, because it has to perform the additional function of bridging the gap between management and an estranged ownership. The divorce of ownership from control also stimulates the development of a large, impersonal market in corporate control, which makes it even more difficult for management to moderate the pursuit of profit, as they live under the constant threat of losing their position through take-overs—and recall how take-overs are already made easier by the corporate form. That is why corporate behavior tends to be more strongly profit-driven than people tend to be when acting in their private capacity. An exaggerated materialist bias is thus introduced into the liberal capitalist ethos.[13]

Although Hessen argued that entity status could be established solely by contract, van Eeghen takes issue with that claim. Hessen, van Eeghen argues, "confuse[s] the joint-stock principle with corporate status." Entity status does not consist merely, as Hessen seemed to think, of the shareholders acting "as a unified collective in a court of law"; rather, entity status refers to the corporation as "a legal entity separate from shareholders."

> First, the fact that shareholders have no legal title to the assets of the corporation, even when they seek to exercise such rights collectively (provided the corporation is not thereby broken up), clearly suggests that the corporation is a legal entity separate from the collective of shareholders and that title to these assets rests with the former. Second, if entity status refers to the collective of shareholders and it is the product of private contracting, there should be private contracts between individual shareholders in existence which stipulate their collective ownership in respect of the firm's assets. But these contracts are simply not there....
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> If it is agreed that the corporation is a legal entity separate from shareholders, then Hessen's claim that it can be the product of private contracting is obviously severely weakened if not dismissed. It is clear that private contracting can achieve only *joint ownership* of the contractors' assets (a partnership); it cannot establish a legal entity separate from the natural persons of the contractors themselves to which they assign their assets.
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> The legal status of nonmanaging partners is obviously similar to that of corporate shareholders, in that they can also obtain limited liability, have given up their control over assets and no longer have the right to consultation in ownership transfers. For Hessen this is evidence to suggest that there is a seamless continuum that starts with the straight, unqualified partnership and ends with the corporation, while the modified partnership is positioned somewhere between the two. But there does seem to be a fundamental difference between partnerships and corporations. Whereas in the case of modified partnerships the rights and responsibilities of ownership are rearranged between nonmanaging and managing partners, these rights and responsibilities are partially cancelled for *all* corporate shareholders. There are no longer any managing shareholders in a corporation; instead *all* corporate shareholders are silent partners. From a liberal point of view, such modified partnerships are perfectly in order (e.g., the limited partnership or the Italian *commenda*), provided that *some* partners carry the full rights and responsibilities of ownership and that accountability towards third parties is thus not compromised.[14]

I confess the argument that separate entity status could be established by private

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[13] Ibid., pp. 60-64.
[14] "The Corporation at Issue, Part II," pp. .

contract is not entirely implausible. Van Eeghen's argument from the nonexistence of such private contracts is not, in itself, very convincing. One might argue that the general idea of free contract is quite recent, that it has been given even comparatively free rein only in the past few centuries, and that, even so, the form it has taken in that time has reflected the path dependencies created by a far more statist society. A great many contractual arrangements might be conceivable without the state (see, for example, the work of the Tannehills or of David Friedman)[15] that have never yet come into existence simply because the state still casts such a huge shadow. Arguably, the very availability of statutory provisions for general incorporation has had the effect of crowding out private contractual arrangements. There is nothing inherently nonsensical or repugnant in the idea of a number of private individuals contracting to create a permanent corporate entity separate from any or all of themselves as individuals, or of local free juries choosing to recognize the standing of such entities under the body of libertarian law.

Even were we to stipulate such an argument, however, it would not get Hessen and his partisans very far. Whether the corporation, as distinguished by its entity status from an ordinary partnership, could come about through private contracting alone, is in my opinion a question involving so much counterfactual speculation as to be unanswerable. But even stipulating that it could doesn't get Hessen very far. He misses the point entirely:

> The actual procedure for creating a corporation consists of filing a registration document with a state official (like recording the use of a fictitious business name), and the state's role is purely formal and automatic. Moreover, to call incorporation a "privilege" implies that individuals have no right to create a corporation. But why is governmental permission needed? Who would be wronged if businesses adopted corporate features by contract? Whose rights would be violated if a firm declared itself to be a unit for the purposes of suing and being sued, holding and conveying title to property, or that it would continue in existence despite the death or withdrawal of its officers or investors, that its shares are freely transferable, or if it asserted limited liability for its debt obligations? ....If potential creditors find any of these features objectionable, they can negotiate to exclude or modify them.[16]

They could negotiate to exclude or modify them a lot more effectively in a system where corporations *had* to be established entirely by private contract, than they can under a system where incorporation is "automatic," as Hessen himself admits. The fact that the state makes the establishment of entity status and all its accidents so much easier, by providing a ready-made and *automatic* venue for incorporation, surely results in a considerable distortion of the market. General incorporation legislation creates a standard procedure for setting up a corporation with entity status, with standard forms to file and automatic recognition to anyone following the prescribed procedure. Thus, the state intervenes to make the corporation the standard form of business organization, and

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16 Robert Hessen, "Corporations," *The Concise Encyclopedia of Economics* (Library of Economics and Liberty) <http://www.econlib.org/library/Enc/Corporations.html>

essentially removes the transaction costs of organizing it.

Leaving aside the broader question of entity status, both Murray Rothbard and Stephan Kinsella have argued that the narrower principle of limited liability for debt could be established by contract, simply by announcing ahead of time that individual shareholders in a firm would be liable only for the amount of their investment. In that case, it would be entirely the voluntary decision of creditors whether or not to accept such terms, and if most creditors found such terms objectionable, the market would punish firms attempting to limit liability by prior announcement in this way.[17] But the very fact that limited liability can be had, not by negotiating it in a private contract on a case by case basis and persuading each group of creditors separately to accept such terms, but merely by filing some standard papers under the general terms of the corporate form provided by statute, distorts the market away from the voluntary nature of limited liability as it would exist under a purely contractual regime. If, under the auspices of the state's code of laws, the limited liability corporation becomes the dominant form of organization, how "voluntary" can the choice of alternatives be from the standpoint of a creditor? As Gregory White, a commenter on Kinsella's article, pointed out:

> ...if you can get a large immunity from debts just by the relatively smaller cost of incorporating, why wouldn't a self-interested investor/owner do so?
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> So once every firm of any substantial size is incorporated, what real 'agreement' (really choice) is there?....
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> Rothbard is saying people should be free to incorporate, and I agree. He's also saying government should have nothing to do with it, including an explicit grant of immunity from debts (by "privilege of limited liability" and charter grants), as I originally said and you rejected.
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> With limited liability to debts granted by government charter, the "right of a free individual" to *effectively* choose the contract is destroyed by implication. In practice they have little choice but to accept the limited liability condition, since it is a government granted privilege that any business person would quickly seize on.
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> ...The legislation distorts the market by destroying some measure of bargaining power on the part of creditors.

In response to Kinsella's claim that the government merely duplicates the effect of private contract ("The government only helps hang a bright neon sign *recognizing that* the shareholders are broadcasting to all third parties: if you deal with us, you can't come after our personal assets"), White responded:

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[17] Stephan Kinsella "In Defense of the Corporation," Mises Economics Blog, October 27, 2005. http://blog.mises.org/archives/004269.asp

> ...[The "sign hanging"] guarantees an immunity, destroying possible terms of negotiation. Without government, the corporation can do no more than ask for agreement (sure, they can "announce" their resolute terms as well as I can announce the sky is green). If you were to say that many contracts, and maybe even most, would end up the same way if it were solely private, I would probably agree. But that won't be the limit. The government distorts the market here -- no question about it. And that distortion plays into natural rights. Some will not be able to recover their own property, where without the distortion, they could have otherwise formed a different contract. It will distort bargaining power in some circumstances. No doubt about it. [18]

Whether or not it could be established by mere contract in a hypothetical scenario, the understanding of the corporate entity status that emerged from the late nineteenth century on was a radical departure from the earlier understanding of the property rights of individual shareholders in a joint-stock corporation. To that extent, the modern corporation with separate entity status really is fundamentally different from the earlier joint-stock corporation. As understood under the earlier doctrine, the property rights of the individual shareholder really were analogous to those of a partner. The understanding is exemplified by the majority opinion in the Dartmouth College case, in which any amendment to a corporate charter, or indeed "any fundamental corporate change," was considered a breach of the shareholder's contract, a "taking" of his property. All such changes had to be consented to unanimously by shareholders, in exactly the same manner as members would consent to the change in terms of a partnership. Under the modern understanding, on the other hand, the corporation is an entity separate entirely from any or all individual shareholders, and governed by a simple majority vote.[19]

In addition, many critics of the corporate form argue that the "corporate veil" dilutes legal responsibility.

It is true that officers and shareholders are technically liable for criminal acts, and not legally exempt for criminal behavior under the corporate form, as Kinsella argued.[20] And as Joshua Holmes pointed out:

> Limited Liability is not at all absolute, as many libertarian detractors seem to imply. In cases of fraud, or where the corporate [sic] does not have sufficient independence from its shareholders, courts will "pierce the veil". When courts pierce the veil, plaintiffs against a corporation can indeed hold the shareholders directly liable. This often happens when the corporation is undercapitalised, that is, when the corporation obviously doesn't have enough assets to cover its liabilities. This happens surprisingly frequently, and more often in torts cases than contracts cases.[21]

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[18] Ibid.
[19] Horwitz, *Transformation of American Law (1870-1960)*, pp. 87-89.
[20] Ibid.
[21] Comment under Kevin Carson, "Corporate Personhood" April 24, 2006.

But as van Eeghen said above, the corporate form is a departure from the common law, in its attenuation of ownership and personal responsibility. Sheldon Richman made a similar observation, raising the issue of

> whether one is at all responsible for what happens with one's property. It's not a matter of merely giving money to the company. Unlike creditors, shareholders supposedly own the corporation, but if their "property" injures someone, they are out of the liability picture altogether. This is a strange notion of property. The real owner is a fictitious person, while the real persons are not real owners. If one has no liability, one has no incentive to pay attention to how "one's property" is being used.[22]

With ordinary forms of property under the common law, the burden of monitoring one's property and avoiding the criminal or tortious use of it by one's hired agents is assumed to lie with the owner. With the corporate form, the owner may not be exempt from liability, but the normal presumption is the reverse.

The corporate veil seems deliberately designed to dilute or obscure personal responsibility. The corporate form provides shareholders with all the benefits of ownership, while freeing them from the normal responsibilities associated with property ownership under the common law. An ordinary property owner is expected to take reasonable care in overseeing it, and exercise reasonable supervision over his hired overseers, or risk being charged with negligence if the property is misused to someone else's harm. The corporate form serves not only to absolve the owners of such responsibility, but to make the exercise of responsible control impossible. It functions, in many ways, as a form of "plausible deniability," increasing the difficulty of assigning blame for malfeasance.

Corporate officers, under pressure from "the market for corporate control" to increase profit margins (without overmuch scrupulosity on the investors' part as to what means management uses to achieve the result), are put in a double bind. As "quasibill," an astute commenter on my blog, remarked on my review of van Eeghen's articles:

> The reality is that management *does* get directives from the shareholders, in the form of a demand for greater dividends/share prices. Management does respond to this directive, sometimes at the expense of innocent third parties. And management does present this situation as a defense - "I would've been fired had I paid for a proper truck driver for that route!" and often juries/factfinders will buy that defense - implicitly finding that it was the shareholder's demands that caused the negligence.[23]

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http://mutualist.blogspot.com/2006/04/corporate-personhood.html

[22] Ibid.

[23] Ibid.

"Who will rid me of this turbulent priest?" If anyone considers the expression "plausible deniability" overblown, consider this bit of legal advice:

> First, the corporate veil is always disregarded by courts for criminal acts of the officers, shareholders, or directors of a corporation. Further, federal and state tax laws generally impose personal liability on those individuals responsible for filing sales and income tax returns for the corporation.
>
> For most other matters, the corporate veil is most often pierced by courts in situations where the shareholders of a corporation disregard the legal separateness of the corporation and the corporation acts as nothing more than an alter ego for the shareholders' own dealings...
>
> It is essential that minutes be maintained of board and shareholder actions. Corporate minutes are the first line of defense against the IRS, creditors, and other parties making claims against the corporation, particularly if a claim is based on a theory that the corporation should not be taxed as a corporation or afforded limited liability (piercing the corporate veil). Minutes can be the written record of meetings or the unanimous written actions of the directors or shareholders taken without a meeting. Either is acceptable, if properly done. Many closely-held corporations fail to keep even annual minutes, which greatly weakens the position of the corporation and its shareholders, directors, and officers in many circumstances. Regular minutes can also:
>
> - Prevent IRS claims of unreasonable compensation of executives who are shareholders
> - Protect against IRS claims of excess accumulated earnings
> - Create defenses against lawsuits attempting to establish personal liability of directors or officers, by evidencing board business judgment and specific authorization
> - Protect against spurious lawsuits of minority shareholders
> - Establish authority for corporate actions for the benefit of outside parties
>
> Minutes of a meeting should be prepared by the Secretary of the Corporation, signed, and then approved by the Board or shareholders, as the case may be, at the next meeting or in the next action. This will minimize any claim that the written minutes do not accurately reflect the action taken. Minutes should always reflect that proper notice was given or waived, who was present and who was absent, and that a quorum was present. Any abstentions or dissents on a vote should be noted for the protection of the director abstaining or dissenting. In a closely-held corporation, meetings are often held to create minutes rather than to make decisions, but holding formal meetings with parliamentary procedures tends to result in more deliberate and organized decision- making and is recommended if practical.

It is equally important that minutes be limited to material which helps and not hurts the corporation. Resolutions should be set forth. The fact that a report was given or a discussion held on a subject should be noted. Statements made by a director or the actual content of a report or discussion, however, should generally not be included, since these references tend to be damaging more often than not. Claimants of a corporation will many times establish their case on the basis of minutes which were too detailed. It is also important to maintain a climate in which each director feels free to say anything during a board meeting and know that it will be strictly confidential and not later show up in a written record describing the board's deliberations. Generally, only formal resolutions adopted by the Board should be set forth in minutes.

It is advisable to review any other detailed descriptions in minutes with legal counsel before completing them.[24]

In other words, do the minimal amount of documentation to cover your posterior and pay homage to the corporate form, but avoid potentially incriminating specific details as much as possible, so that participants can distance themselves from the decision-making process after the fact.

Although shareholders and corporate officers are liable in theory for malfeasance, in practice the standard is applied far differently to the corporation, and the sole proprietorship, respectively. As "quasibill" points out,

agency law is a major source of liability for sole proprietors, but is arbitrarily cut off in the case of shareholders merely by invoking the statutory grant of incorporation. One can argue that the corporate veil can be pierced, but the standards are not the same; in essence, so long as the shareholder is extremely negligent in how the business is run, he's insulated from responsibility. In contrast, agency law places a burden on a sole proprietor to be responsible about his choice of agents.

[The shareholder is protected], so long as [he] can demonstrate that he "respected the corporate identity." So, as long as he didn't mix and mingle assets, or fail to hold corporate meetings, he's protected from liability. In fact, so long as he colludes with his fellow shareholders, he can make it airtight by demonstrating that after all corporate formalities were followed, they all voted for the same result. In this case, they are all enforcing their own claim to having respected the corporate personality, thereby benefitting all of them equally.

In contrast, a sole proprietor who turned the day to day operation of his business over to a hired manager would be bound by the acts of his agent that were taken in the

[24] "How to Avoid Piercing of Your Corporate Veil." Click&Inc. The Internet's *Only* Customized Incorporation Service for Home & Small Business Owners.

> scope of the agency, period. The sole proprietor is responsible for choosing that person and imbuing him with authority. Especially if he didn't supervise the manager very well and the manager uses the business to defraud customers. It doesn't take much to see that a sole proprietor could be held liable for his negligence in such a situation. In contrast, the shareholders are actually encouraged to take LESS care in how the day to day manager is operating the business. The less care he takes, the more he can claim he respected the corporate personality.
>
> It doesn't mean that he will always be held liable when the agent acts negligently in the scope of the agency, but he can be. And that is more than can be said about shareholders, so long as they obey the rituals set forth in business incorporation statutes.[25]

In countering the argument from the shareholders' moral responsibility, Kinsella is put in the rather awkward position of repudiating much of what Mises said about the entrepreneurial corporation, and giving a great deal of ground to Berle and Means on the divorce of ownership from control. As we shall see in Chapter Seven, Mises repudiated the idea of the managerial corporation, and made a clear distinction between the bureaucratic and entrepreneurial organization. The entrepreneurial corporation, no matter how large, is simply an agent of the owner's will; the owner's will is enforced by the magic of double-entry bookkeeping.

Kinsella, on the other hand, was obliged to attenuate the ownership relationship as much as possible, as theoretical owners, from the workings of the corporation:

> It is bizarre that there is this notion that owners of property are automatically liable for crimes done with their property... Moreover, property just means the right to control. This right to control can be divided in varied and complex ways. If you think shareholders are "owners" of corporate property just like they own their homes or cars--well, just buy a share of Exxon stock and try to walk into the boardroom without permission. Clearly, the complex contractual arrangements divide control in various ways: the managers, etc., really have direct control; subject to oversight by the directors... etc. But even here--to get a loan, the company has to agree to various covenants w/ the bank, that condition its right to use property. Even though the law would not call the bank an "owner" praxeologically it of course has a partial right to control the property. If you have a contract allowing rentacops to patrol the building--hey, they are partial owners too. If you are leasing from a landlord--so do they. If you allow the plumber in to fix the building--he has temporary right of control too. So what?[26]

In a correspondence with Sean Gabb, Kinsella "raise[d] doubts about the effective

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[25] Comment under Stephan Kinsella, "Sean Gabb's Thoughts on Limited Liability," Mises Economics Blog, September 26, 2006 http://blog.mises.org/archives/005679.asp
[26] Comment under Carson, "Corporate Personhood."

control that shareholders have over their companies, and wonders if they should not rather be placed in the same category as employees or lenders or contractors." The answer, Gabb said, is that shareholders are "the natural owners of their companies. They have not lent money to them. They are not providing paid services. They are the owners."[27]

In a subsequent article, Kinsella took up the same question, albeit in somewhat milder terms.

> ...it seems to me the default libertarian position is that an individual is responsible for torts he commits. If you want to hold others liable for this too, you need to show some kind of causal connection between something done by the third person, and the tort committed by the direct tortfeasor. You seem to assume that this connection is present in the case of a shareholder because he is the "true" or "natural" owner of the company's assets. This I think is what troubles me the most--it seems too much of an assertion to me.[28]

Now, at least in theory, there is a big difference between the shareholder, on the one hand, and creditors, managers, and associated other parties, on the other. The shareholder is the residual claimant, the owner of the firm, and the principal; the management are his agents. The creditor's position, as opposed to that of the owner or residual claimant, is only to a "contractually defined absolute return."[29] It was of great importance to Mises to demonstrate that the owner's control of the corporation was real, and that the management were entirely his agents. Kinsella, on the other hand, is apparently so dead set on helping the shareholder to evade the responsibilities of ownership, as to identify ownership with "control," and to argue on that basis that since management is in the most direct position of control, the "ownership" of the shareholders is ambiguous at best.

Kinsella ridiculed the common law concept of absolving an employer from *respondat superior*, on the grounds that his employees were on a "folic."[30] But that makes perfect sense, given the way property ownership was treated under the common law. The property owner was presumed responsible for how his property was used, under normal circumstances, including the presumption of reasonable care in the supervision of those to whom the management of his property was entrusted. A "frolic," as comical as the term may sound to modern ears, was simply an exception to this strong presumption of responsibility, a case in which the owner was held not to be responsible owing to circumstances beyond his reasonable control.

> But consider: the basis for respondeat superior (and I bring this up [because] it

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[27] Sean Gabb "Thoughts on Limited Liability" *Free Life Commentary*, Issue Number 152, 26th September 2006. http://www.seangabb.co.uk/flcomm/flc152.htm
[28] Stephan Kinsella, "Sean Gabb's Thoughts on Limited Liability."
[29] Quasibill comment under Ibid.
[30] Ibid.

seems to me something along the lines of this principle must be employed to hold the shareholder liable for acts of employees) has to do with the employer's practical right or ability to control or direct the actions of the employee (this principle probably underlies the "frolic" exception too). Can we assume that this control is present when we move further back the chain of causation? Say, to the directors, who appoint the managers? Or to the shareholders, who elect the directors? And if practical control is one of the main relevant features that determines whether there is liability, again, why couldn't lenders, employees, suppliers, customers, etc. at least potentially be held liable? In some cases they exert more control and give more "aid and comfort" or "aid and abet" in more visible and substantial ways than a mere shareholder....

> ....You conceive of a shareholder as the "natural" owner of the enterprise. I am skeptical of relying on the conceptual classifications imposed by positive law. To me a shareholder's nature or identity depends on what rights it has. What are the basic rights of a shareholder? What is he "buying" when he buys the "share"? Well, he has the right to vote--to elect directors, basically. He has the right to attend shareholder meetings. He has the right to a certain share of the net remaining assets of the company in the event it winds up or dissolves, after it pays off creditors etc. He has the right to receive a certain share of dividends paid *if* the company decides to pay dividends--that is, he has a right to be treated on some kind of equal footing with other shareholders--he has no absolute right to get a dividend (even if the company has profits), but only a conditional, relative one. He has (usually) the right to sell his shares to someone else. Why assume this bundle of rights is tantamount to "natural ownership"--of what? Of the company's assets? But he has no right to (directly) control the assets. He has no right to use the corporate jet or even enter the company's facilities, without permission of the management. Surely the right to attend meetings is not all that relevant. Nor the right to receive part of the company's assets upon winding up or upon payment of dividends--this could be characterized as the right a type of lender or creditor has.[31]

Kinsella has come a long way from his initial argument that the corporation was simply a contractual device for property owners to pool their property and appoint managers for it as they saw fit, and there is little left of his trail of breadcrumbs. He winds up, as quasibill comments, "intimat[ing] that there is no real owner of corporate property - that an abstraction... [has] property rights."[32]

He does not seem clearly to grasp just how much baby he is throwing out with the bathwater. In legal theory the shareholders are the owner, and corporate managers are the appointed agents of their will, responsible to them in a way that they are not responsible to lenders; so by arguing this Kinsella is in effect conceding much ground to those like Berle and Means and Galbraith who argue that the "private" ownership is a legal fiction,

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[31] Ibid.
[32] Comment under Ibid.

and that the corporation is a quasi-state institution controlled by managers with certain contractually defined obligations--mostly usufructory--to shareholders. Mises' arguments regarding calculation all assume an "entrepreneurial" corporation that is really an extension of the owner's will and judgment; Mises saw the Berle/Means/Galbraith argument as a challenge to be overcome, and his distinction between the bureaucratic and the entrepreneurial large organization is central to his attempt to refute them.

Kinsella's defense of the shareholder based on the lack of control misses the point. He wrote:

> You [quasibill] see a sole proprietor as responsible for employees' torts; yet you think there is an artificial exemption for "joint owners". If they just "stand in the shoes" of a sole proprietor, why aren't they collectively liable?
>
> But a sole proprietor is liable because he directs the actions of the negligent employee, and actually runs the company--sets policies, controls is, manages it. In a joint stock company, the shareholders don't do any of this. They elect the board, which appoints managers. In my view, the managers are more analogous to the sole proprietor than the shareholders are.
>
> ....Hessen here is making the same basic causation point I have made here: that vicarious liability must be relied on to hold someone liable for the servant's actions--and in the case of a sole proprietorship, it is reasonable to do so because the proprietor/master is hiring, training, supervising the servant/employee. But in the case of a joint stock company, the same idea applies only to those sharehlolders who "play an active role in managing an enterprise or in selecting and supervising its employees and agents."
>
> This makes sense to me. Merely being a shareholder is not sufficient. It's having control. I believe most of the corporation opponents have some view that inherently connects liability to property. I think this is confused and wrong. Liability flows from one's actions--from control--from causing the harm to occur....[33]

But claiming the absence of control is not a defense, because it begs the question of whether they *should* have exercised *more* control. The proper question is whether property ownership *ought* to entail some minimal level of oversight and responsibility, and whether one of the benefits of the corporate form (from the owners' perspective) is that it enables the evasion of that responsibility. Arguably, doesn't the very act of delegating control of property in a way that makes one's own direct oversight less feasible, in itself make one liable for any resulting malfeasance by one's agent? Isn't the absentee owner negligent precisely *because* he put himself in a position in which he exercised little or no control over how his agents used his property? Isn't one of the

[33] Comment under Ibid.

virtues of the corporate form, from the owners' perspective, precisely that it entitles them to the profits resulting from management's shady behavior, and enables them to fire managers for failing to produce an adequate level of profit *by any means necessary*, while absolving them from responsibility for the actual means used by management--in short, that it creates plausible deniability?

And as quasibill repeated, the standard of accountability for the actions of one's agents is qualitatively different under a sole proprietorship and a corporation. The sole proprietor is

> the ultimate owner, who has the right to decide that someone else will run the company.... But the manager ultimately derives his authority from the owner, who has non-permanently delegated it to him. This delegation is, in itself, an act that has consequences in the world. For this act, the sole proprietor can be held responsible, including a situation where the sole proprietor hired a dangerous manager because that manager was likely to yield higher profits.
>
> As I've noted, the shareholder's decision to hire a director is, in fact, absolutely immune as long as they follow some statutorily defined rituals. They *are* the ultimate owner involved, and they *are* the one(s) that delegate the right to control to the managers. This delegation *is* an action for which liability can possibly accrue, under a libertarian theory. Under current law, it can't, unless the shareholder disregards a fictitious concept.[34]

So there is an irresolvable contradiction in the Hessen-Kinsella understanding of property rights in the corporation. Such defenders of the corporation start out by defending it as a normal outgrowth of private property rights and the right, by free contract, to make arrangements for governing one's property. But before they're done, they wind up minimizing the property relations between individual shareholders and the corporation. The overall effect is one of deliberate ambiguity, in which the corporation is treated as property in the ordinary sense, or as an instrument of the shareholders' exercise of property rights, only when convenient. There is a contradiction in saying the corporation is merely a contractual arrangement for arranging property, like a partnership, and then minimizing the property relationship or responsibility of any particular property holder. Either the corporation is just another form of partnership, in which case shareholders are the real legal actors, or the corporation is a state-created entity for privatizing profit while attenuating responsibility. It can't be both ways.

Interestingly, some defenders of the corporation have been quite aware of the contradiction. For example, Dwight Jones wrote:

> ....The main value of a corporate charter arises from the fact that powers and

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[34] Comment under Ibid.

> privileges are thereby acquired which individuals do not possess. It is this that makes the difference between a business corporation and a partnership. In the former there is no individual liability.... There is no death.... It is not policy therefore for a corporation to break down its own independent existence by burying its original character in the common place privileges of the individual.... Any mingling of corporate existence with the existence of the shareholders will weaken corporate rights.[35]

Jones defended the attenuation of shareholder liability under the entity form, in terms quite similar to Kinsella. But he perceived much more acutely than Kinsella that this defense comes at a price: it completely rules out any defense of the corporation in which the latter is an ordinary contractual expression of the property rights of the shareholders, in the same sense as a partnership.

Even those defending entity status, like Hessen and Kinsella, as an outgrowth of ordinary private contracting akin to the partnership, faced difficulties. The most notable proponent of the "natural entity" doctrine (favored also by Hessen and Kinsella) was Ernst Freund, author of *The Legal Nature of Corporations* (1897). Freund attempted to reconcile the status of the corporation as a representative entity governed by corporate rule, with an individualist understanding of it as the sum of its parts in the same sense as a partnership. Nevertheless, he was somewhat put off by the fact that corporate powers were vested directly in the board of directors. The practical effect, he was forced to admit, was that

> corporate capacity [was] thereby shifted from the members at large to the governing body.... Such an organization reduces the personal cohesion between the [shareholders] to a minimum, and allows us to see in a large railroad, banking or insurance corporation rather an aggregation of capital than an association of persons.[36]

Henry Williams argued, in an 1899 *American Law Register* article, that shareholders "possess[ed] no actual existing legal interest... whatever" in the corporation. They were equivalent in law to "the heirs, or next of kin or residuary legatees of a living person" (and I leave it to the reader to guess who the "living person" is). Their legal rights accrued only at dissolution, and even then their rights were "entirely subsidiary" to those of creditors.[37]

In the same regard, almost directly contrary to Mises' perception, the market for corporate control, far from an instrument of the absolute property rights of the entrepreneur, has been associated with the attenuation of shareholder property rights in the corporation. As we saw above, the modern corporate entity status required a shift to

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[35] Dwight A. Jones, "A Corporation as 'A Distinct Entity,'" 2 Couns. 78, 81 (1892), in Horwitz, *The Transformation of American Law !870-1960*, p. 91.
[36] Quoted in Horwitz, *The Transformation of American Law 1870-1960*, pp. 102-103.
[37] Ibid. p. 103.

majority shareholder control of the corporation, and an end to the earlier understanding (reflected in *Dartmouth*) of the shareholder as possessing absolute property rights analogous to those in a partnership. The result, by the early twentieth century, was a common legal understanding in which "the modern stockholder is a negligible factor in... management," and in which a sharp distinction was made between the status of "investor" and "proprietor."[38] The shift was encouraged by the rise of public securities markets. Until the 1890s, public issues of stock were rare and public trading (outside of railroad stock) almost unheard of. In an environment in which the issuance of stock was still largely private and associated with the formation of joint-stock companies, it was more plausible to regard investment in a corporation as equivalent to buying into a partnership. The creation of public equity markets, in which shares were commonly acquired by those with no direct role in the formation or governance of the firm, and bought on an anonymous market rather than issued directly to the shareholder by the firm, made the cultural holdover far less tenable. It became virtually impossible to maintain with a straight face the earlier "trust fund" doctrine of *Dartmouth* and other decisions, in which the shareholder was a partner with absolute property rights in the governance of the corporation.[39] By the turn of the century, the board of directors was clearly coming to be seen as the agent, not of shareholders, but of the corporation as a separate entity.[40]

Incidentally, I can't resist pointing out that defending the status of corporate management as agents for an imaginary collective entity, an entity with distinct property rights of its own and capable of making contracts in its own name and otherwise acting as principal, puts Austrian economists in a rather odd position, given their usual professions of "methodological individualism."

To sum up, it may be true, as Hessen argued, that something like the corporate form--with entity status and limited liability--could be established by purely private contract. But it's also true, as Gregory White said, that the state artificially lowered the transaction costs of the corporate form compared to alternative models of firm organization, by providing an established and virtually automatic mechanism to facilitate adoption of the corporate form. What's more, it has promoted a particular model of the corporation out of a number of possible alternative corporate models that might have been established by contract. The standard corporate form, established under general incorporation laws, is based on an amalgamation of capital which hires workers. The state artificially privileges this form against, and crowds out, alternative corporate organizational models: for instance, a model in which associated labor is the residual claimant and pays only fixed contractual returns on borrowed capital.

B. Subsidies to Transportation and Communication Infrastructure.

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[38] Ibid. p. 93.
[39] Ibid. pp. 96-98.
[40] Ibid. p. 99.

"Internal improvements" had been a controversial issue throughout the nineteenth century, and were a central part of the mercantilist agenda of the Whigs and the Gilded Age GOP. Indeed, Lincoln announced the beginning of his career with a "short but sweet" embrace of Henry Clay's program: a national bank, a high tariff, and internal improvements. But the government's role in promoting a national railroad system effected a revolution several orders of magnitude greater than anything that had occurred before.

As we shall see below, the failure of the trust movement at the turn of the 20th century reflected the insufficiency of railroad subsidies, tariffs and patents alone to maintain stable monopoly power. But without the government-subsidized "internal improvements" of the nineteenth century, it is doubtful that most national-scale industrial firms would have existed, let alone been able even to attempt trustification. If the neo-Hamiltonianism of the 19th century was not a sufficient condition for the state capitalism of the 20th, it was certainly a necessary one. As Coase pointed out, "[i]nventions which tend to bring factors of production nearer together, by lessening spatial distribution, tend to increase the size of the firm."[41] This applies as well to inventions that lessen the cost of spatial distribution by making transportation cheaper over longer distances. The effect of transportation subsidies is to artificially enlarge market areas, and hence to artificially increase firm size.

Adam Smith argued over two hundred years ago for the fairness of internalizing the costs of transportation infrastructure through user fees.

> It does not seem necessary that the expense of those public works should be defrayed from that public revenue, as it is commonly called, of which the collection and application is in most countries assigned to the executive power. The greater part of such public works may easily be so managed as to afford a particular revenue sufficient for defraying their own expense, without bringing any burden upon the general revenue of society....
>
> When the carriages which pass over a highway or a bridge, and the lighters which sail upon a navigable canal, pay toll in proportion to their weight or their tonnage, they pay for the maintenance of those public works exactly in proportion to the wear and tear which they occasion of them. It seems scarce possible to invent a more equitable way of maintaining such works. This tax or toll too, though it is advanced by the carrier, is finally paid by the consumer, to whom it must always be charged in the price of the goods....
>
> It seems not unreasonable that the extraordinary expense which the protection of any particular branch of commerce may occasion should be defrayed by a moderate tax upon that particular branch; by a moderate fine, for example, to be paid by the

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[41] R.H. Coase, "The Nature of the Firm," 1937.

> traders when they first enter into it, or, what is more equal, by a particular duty of so much percent upon the goods which they either import into, or export out of, the particular countries with which it is carried on.[42]

But that's not the way things work under what the neoliberals like to call "free market capitalism." Spending on transportation and communications networks from general revenues, rather than from taxes and user fees, allows big business to externalize its costs on the public, and conceal its true operating expenses. Chomsky described this state capitalist underwriting of shipping costs quite accurately:

> One well-known fact about trade is that it's highly subsidized with huge market-distorting factors.... The most obvious is that every form of transport is highly subsidized.... Since trade naturally requires transport, the costs of transport enter into the calculation of the efficiency of trade. But there are huge subsidies to reduce the costs of transport, through manipulation of energy costs and all sorts of market-distorting functions.[43]

Every wave of concentration of capital in the United States has followed a publicly subsidized infrastructure system of some sort. The national railroad system, built largely on free or below-cost land donated by the government, was followed by concentration in heavy industry, petrochemicals, and finance. Albert Nock ridiculed the corporate liberals of his time, who held up the corruption of the railroad companies as examples of the failure of "rugged individualism" and "laissez-faire."

> It is nowadays the fashion, even among those who ought to know better, to hold "rugged individualism" and *laissez-faire* responsible for the riot of stock-waterings, rebates, rate-cutting, fraudulent bankruptcies, and the like, which prevailed in our railway-practice after the Civil War, but they had no more to do with it than they have with the precession of the equinoxes. The fact is that our railways, with few exceptions, did not grow up in response to any actual economic demand. They were speculative enterprises enabled by State intervention, by allotment of the political means in the form of land-grants and subsidies; and of all the evils alleged against our railway-practice, there is not one but what is directly traceable to this primary intervention.[44]

The federal railroad land grants, as Murray Rothbard described them, included not only the rights-of-way for the actual railroads, "but fifteen-mile tracts on either side of the line." As the lines were completed, these adjoining tracts became prime real estate and skyrocketed in value. As new communities sprang up along the new routes, every house and business in town was built on land that had to be bought from the railroads. The

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[42] Smith, *Wealth of Nations* pp. 315, 319.
[43] Noam Chomsky, "How Free is the Free Market?" *Resurgence* no. 173 <http://www.oneworld.org/second_opinion/chomsky.html>.
[44] Nock, *Our Enemy, the State*, p. 102.

tracts also included valuable timber land that was made even more valuable by government reservation of potentially competing timber lands.[45]

As we have already seen in a previous chapter, it was the creation of the national railroad system which made possible first national wholesale and retail markets, and then large manufacturing firms serving the national market.

The next major transportation projects were the national highway system and the civil aviation system. From the earliest days of the automobile-highway complex, when the Model-T met the "good roads" movement in the state legislatures, a modern highway network was synonymous in the public mind with "progress." Of course, as Eric Husman has pointed out, that was just another example of a long-recurring phenomenon: the public hailed subsidized highways as their "progressive" delivery from the monopoly power of railroads; but the subsidized railroads, in their turn, had been celebrated by the public as a force for liberation.

> The same public who first wanted to give land grants and rights of way to railroads and canals in order to get rid of private turnpikes, and then wanted to constrain railroads because the average voter didn't understand the logic of the capital-intensive industry they had spawned, and now didn't like the fact that their regulations created a *de jure* cartel, wanted roads. They joined the Good Roads movement and fought for public subsidies for bicycles and then cars.[46]

Over and over again, the public calls for a new subsidized infrastructure to liberate it from the straitjacket imposed from the previous subsidized infrastructure, while never seeing that it is locked into dependence on the previous infrastructure as the result of the "progressive" policies it supported. But all along, the parties that actually stand to benefit the most are the big business interests that can operate over larger and larger market areas at lower and lower cost, while externalizing their costs on the poor taxpaying suckers who cheer it on as "progress."

The "good roads" movement had had the backing of mercantilist interests from the turn of the century.

> One of the major barriers to the fledgling automobile industry at the turn of the century was the poor state of the roads. One of the first highway lobbying groups was the League of American Wheelmen, which founded "good roads" associations around the country and, in 1891, began lobbying state legislatures.
>
> Many of America's roads were private and funded by tolls. One such early road

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[45] *Power & Market: Government and the Economy* (Menlo Park, Calif.: Institute for Humane Studies, Inc., 1970), p. 52.
[46] Eric Husman, "Running on Glue and Tar," Grim Reader blog, June 3, 2007 <http://www.zianet.com/ehusman/weblog/2007/06/running-on-glue-and-tar.html>.

> was the 45-mile Long Island Motor Parkway, built in 1908 and entirely financed by the racing enthusiast William K. Vanderbilt, Jr. The toll collection plan fell short of expectations, and he gave up his road in 1938 in lieu of back taxes.
>
> The Federal Aid Roads Act of 1916 encouraged coast-to-coast construction of paved roads, usually financed by gasoline taxes (a symbiotic relationship if ever there was one). By 1930, the annual budget for federal road projects was $750 million. After 1939, with a push from President Franklin Roosevelt, limited-access interstates began to make rural areas accessible.[47]

It was this last, in the 1930s, that signified the most revolutionary change. From its beginning, the movement for a national superhighway network was identified, first of all, with the fascist industrial policy of Hitler, and second with the American automotive industry.

> The "most powerful pressure group in Washington" began in June, 1932, when GM President, Alfred P. Sloan, created the National Highway Users Conference, inviting oil and rubber firms to help GM bankroll a propaganda and lobbying effort that continues to this day.[48]

One of the earliest depictions of the modern superhighway in America was the Futurama exhibit at the 1939 World's Fair in New York, sponsored by (who else?) GM.

> The exhibit, sponsored by General Motors and given dazzling miniaturized form by set designer Norman Bel Geddes, provided a nation emerging from its darkest decade since the Civil War a mesmerizing glimpse of the future--a future that involved lots and lots of roads. Big roads. Fourteen-lane superhighways on which cars would travel at 100 mph. Roads on which, a recorded narrator promised, Americans would eventually be able to cross the nation in a day.[49]

The Interstate's association with General Motors didn't end there, of course. Its actual construction took place under the supervision of DOD Secretary Charles Wilson, formerly CEO of GM. During his 1953 confirmation hearings, when asked whether "he could make a decision in the country's interest that was contrary to GM's interest,"

> Wilson shot back with his famous comment, "I cannot conceive of one because for years I thought what was good for our country was good for General Motors, and vice

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[47] Jim Motavalli, "Getting Out of Gridlock: Thanks to the Highway Lobby, Now We're Stuck in Traffic. How Do We Escape?" *E Magazine*, March/April 2002 <http://www.emagazine.com/view/?534>.
[48] Mike Ferner, "Taken for a Ride on the Interstate Highway System," MRZine (*Monthly Review*) June 28, 2006 <http://mrzine.monthlyreview.org/ferner280606.html>.
[49] Justin Fox, "The Great Paving How the Interstate Highway System helped create the modern economy--and reshaped the FORTUNE 500." Reprinted from Fortune. CNNMoney.Com, January 26, 2004 <http://money.cnn.com/magazines/fortune/fortune_archive/2004/01/26/358835/index.htm>.

> versa. The difference did not exist. Our company is too big."[50]

Wilson's role in the Interstate program was hardly that of a mere disinterested technocrat. From the time of his appointment to DOD, he "pushed relentlessly" for it. And the chief administrator of the program was "Francis DuPont, whose family owned the largest share of GM stock...."[51] Corporate propaganda, as so often in the twentieth century, played an active role in attempts to reshape the popular culture.

> Helping to keep the driving spirit alive, Dow Chemical, producer of asphalt, entered the PR campaign with a film featuring a staged testimonial from a grade school teacher standing up to her anti-highway neighbors with quiet indignation. "Can't you see this highway means a whole new way of life for the children?"[52]

The latest installment in this saga is the planned I-69, or so-called NAFTA Superhighway running from Mexico to Canada, intended to be the largest trucking corridor in North America. As is the case with most things with the term "NAFTA" in their titles, most of the mercantilist interests in America have a finger in the I-69 pie--perhaps most notably Rudy Giuliani's law firm.

Whatever the political motivation behind it, the economic effect of the Interstate system should hardly be controversial. Virtually 100% of the roadbed damage to highways is caused by heavy trucks. And despite repeated liberalization of maximum weight restrictions, far beyond the heaviest conceivable weight the Interstate roadbeds were originally designed to support,

> fuel taxes fail miserably at capturing from big-rig operators the cost of exponential pavement damage caused by higher axle loads. Only weight-distance user charges arc efficient, but truckers have been successful at scrapping them in all but a few western states where the push for repeal continues.[53]

So only about half the revenue of the highway trust fund comes from fees or fuel taxes on the trucking industry, and the rest is externalized on private automobiles. Even David S. Lawyer, a skeptic on the general issue of highway subsidies, only questions whether highways receive a net subsidy from general revenues over and above total user fees on both trucks and cars; he effectively concedes the subsidy of heavy trucking by the gasoline tax.[54]

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[50] Edwin Black, "Hitler's Carmaker: How Will Posterity Remember General Motors' Conduct? (Part 4)" History News Network, May 14, 2007 <http://hnn.us/articles/38829.html>.
[51] Ferner, op. cit.
[52] Ibid.
[53] Frank N. Wilner, "Give truckers an inch, they'll take a ton-mile: every liberalization has been a launching pad for further increases - trucking wants long combination vehicle restrictions dropped,"*Railway Age*, May 1997 <http://findarticles.com/p/articles/mi_m1215/is_n5_v198/ai_19460645>.
[54] David S. Lawyer, "Are Roads and Highways Subsidized ?" March 2004 <http://www.lafn.org/~dave/trans/econ/highway_subsidy.html>.

As for the civil aviation system, from the beginninbg it was a creature of the state. The whole physical infrastructure was built, in its early decades, with tax money.

> Since 1946, *the federal government has poured billions of dollars into airport development.* In 1992, Prof. Stephen Paul Dempsey of the University of Denver estimated that *the current replacement value of the U.S. commercial airport system-* virtually all of it developed with federal grants and tax-free municipal bonds-*at $1 trillion.*
>
> Not until 1971 did the federal government begin collecting *user fees* from airline passengers and freight shippers to recoup this investment. In 1988 the Congressional Budget Office found that *in spite of user fees paid into the Airport and Airways Trust Fund, the taxpayers still had to transfer $3 billion in subsidies per year to the FAA* to maintain its network of more than 400 control towers, 22 air traffic control centers, 1,000 radar-navigation aids, 250 long-range and terminal radar systems and its staff of 55,000 traffic controllers, technicians and bureaucrats.[55]

(And even aside from the inadequacy of user fees, eminent domain remains central to the building of new airports and expansion of existing airports.)

Subsidies to the airport and air traffic control infrastructure of the civil aviation system are only part of the picture. Equally important are the direct role of the state in creating the heavy aircraft industry, whose heavy cargo and passenger jets revolutionized civil aviation after WWII. As we shall see below, after the World War II demobilization the aircraft industry was headed for bankruptcy. Without the Cold War heavy bomber program to revive it from the late '40s on, it is questionable in what form the aircraft industry would have survived at all; the growth of a civilian jumbo jet industry would have been unthinkable. The civil aviation system is, many times over, a creature of the state.

The result of the government-sponsored highway and civil aviation systems, taken together, was massive concentration in retail, agriculture, and food processing. The centralized corporate economy depends for its existence on a shipping price system which is artificially distorted by government intervention. To fully grasp how dependent the corporate economy is on socializing transportation costs, imagine what would happen if truck and aircraft fuel were taxed enough to pay the full cost of maintenance and new building costs on highways and airports; and if fossil fuels depletion allowances were removed. The result would be a massive increase in shipping costs. Does anyone seriously believe that Wal-Mart's national "warehouses on wheels" distribution system would be feasible, or corporate agribusiness could outcompete the family farm?

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55 James Coston, Amtrak Reform Council, 2001, in "America's long history of subsidizing transportation" <http://www.trainweb.org/moksrail/advocacy/resources/subsidies/transport.htm>.

It is fallacious to say that state-subsidized infrastructure "creates efficiencies" by making possible large-scale production for a national market. The fact that a large, centralized infrastructure system can only come about when the state subsidizes or organizes it from above, or that such state action causes it to exist on a larger scale than it otherwise would, indicates that the transaction costs are so high that the benefits *are not worth it* to people spending their own money. There is no demand for it by consumers willingly spending their own money, at the actual costs of providing the services, risks and all, without state intervention.

If production on the scale promoted by infrastructure subsidies were actually efficient enough to compensate for *real* distribution costs, the manufacturers would have presented enough effective demand for such long-distance shipping at actual costs to pay for it without government intervention. On the other hand, an apparent "efficiency" that presents a positive ledger balance only by shifting and concealing real costs, is really no "efficiency" at all. Costs cannot be destroyed. Shifting them does not make them any less of a cost--it only means that, since they aren't being paid by the beneficiary of the service, he profits at someone else's expense. There Ain't No Such Thing As A Free Lunch.

Intellectually honest free market advocates freely admit as much. For example, Tibor Machan wrote in *The Freeman* that

> Some people will say that stringent protection of rights [against eminent domain] would lead to small airports, at best, and many constraints on construction. Of course--but what's so wrong with that?
>
> Perhaps the worst thing about modern industrial life has been the power of political authorities to grant special privileges to some enterprises to violate the rights of third parties whose permission would be too expensive to obtain. The need to obtain that permission would indeed seriously impede what most environmentalists see as rampant--indeed reckless--industrialization.
>
> The system of private property rights--in which... all... kinds of... human activity must be conducted within one's own realm except where cooperation from others has been gained voluntarily--is the greatest moderator of human aspirations.... In short, people may reach goals they aren't able to reach with their own resources only by convincing others, through arguments and fair exchanges, to cooperate.[56]

The state played a central role in creating the centralized communications infrastructure of the twentieth century. The modern telecommunications system goes back to the Bell Patent association, organized in 1875, which controlled a huge arsenal of

[56] Tibor S. Machan, "On Airports and Individual Rights," *The Freeman: Ideas on Liberty* (February 1999), p. 11.

government-enforced patents on virtually every aspect of telephony.[57] Meanwhile, as the Bell patents began to expire in the 1890s, AT&T turned to the "progressive" expedient of becoming a regulated utility to protect itself from competition. Here's Mary Ruwart's account:

> Before 1894, Bell Telephone's patents protected it from competition by other firms. Its growth averaged 16% per year; annual profits approached 40% of its capital. Bell catered primarily to the business sector and the wealthy. When the patents expired, other companies began providing affordable telephone service to the middle class and rural areas. The independents charged less since customers could call only those serviced by the same company. Consumers were evidently pleased to make such a tradeoff; by 1907, some 20,000 independents controlled half of all the new telephone installations. The number of phones zoomed from 266,000 in 1893 to 6.1 million in 1907. The independents matched Bell's monopoly market share in 14 short years.
>
> Competition from the independents had caused annual Bell profits to plummet from 40% to 8% as many consumers chose the independents who served them best. The marketplace ecosystem was again protecting consumers from monopoly profits.
>
> As telephones went from a curiosity to a standard household utility, the independents began developing a plan for sharing each other's lines to avoid duplication and to increase the number of phones each customer could call. The marketplace ecosystem was again working to promote cooperation for the benefit of the consumer, without aggression. Service providers voluntarily sought to give the customer better service because they would, in turn, be rewarded by more business and the positive feedback of profit....
>
> Theodore Vail, Bell's new chairman, was determined to regain a monopoly market. He asked Americans to use the aggression of exclusive licensing against the independents that had served them so well. He claimed that competition caused duplication and penalized the customer (i.e., telephone service was a "natural" monopoly). Had this been true, the independents would never have been able to lure customers from the established Bell monopoly in the first place!
>
> ...Nevertheless, by 1910, Americans were persuaded to accept Bell's proposal. The government of each local community would allow only one telephone company to operate in that region. Other companies would be stopped-at gunpoint, if necessary-from providing service to willing customers. Since Bell was the largest single company, it was in the best position to lobby the state utility commissions effectively and was almost always chosen over the independents....[58]

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[57] David F. Noble, *America by Design* 91-2.

[58] Mary Ruwart, *Healing Our World: The Other Piece of the Puzzle* (Kalamazoo, Michigan: SunStar Press, 1992, 1993). "Chapter 7. Creating Monopolies that Control Us"

It's hard to say what form a national telephone network would have taken absent the AT&T monopoly for most of the twentieth century, but it seems unlikely in the extreme that the pattern of local cooperation and bottom-up federation Ruwart describes before 1910 could have led to a centralized system of trunk lines. Mumford's contrast of a loose network of locally oriented light rail systems, as against the centralized national network created by the federal land grant program, is probably a useful basis for comparison.

On a global scale, the physical backbone of the telecom network until the 1960s was the transoceanic cable system, largely the creature of the British state. And as Edward Herman describes, its successor--the communications satellite network--was an even larger state capitalist project by the U.S. government:

> ...the research and development funds that led to the conception and production of [the communications satellite network] were provided by an American military-commercial alliance with very clear objectives in mind.... Satellite development, *from the beginning*, represented the successful drive of private communications corporations in the United States to dislodge the British from their domination of international communications, exercised through their... control of intercontinental submarine cables. In this effort monopolistic business acted closely with the U.S. Armed Forces, whose interest in instantaneous global communications was extraordinarily high.... In fact, the first communications satellite system in operation was a military-controlled operation.
>
> A decade later, in the early 1970s, an international consortium (called INTELSAT) of (currently [as of 1976]) 91 nations uses the United States-developed satellite system. The system has, from the start, been controlled by American Big Business... working with the U.S. State Department at the intergovernmental level.[59]

[See also Nicholas Garnham," "Trojan Horses: Some Socio-Political Implications of Communications Technology," paper presented at International Broadcast Institute General Meeting, Mexico City, Sept. 1-5, 1974.]

The most recent such project was the infrastructure of the Internet, originally built by the Pentagon. [Chandler material?]

> The internet owes its very *existence* to the state and to state funding. The story begins with ARPA, created in 1957 in response to the Soviets' launch of Sputnik and established to research the efficient use of computers for civilian and military

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http://www.ruwart.com/Healing/chap7.html.

[59] Herbert Schiller, *Communications and Cultural Domination* (White Plains, N.Y.: M.E. Sharpe, Inc., 1976), p. 59. Schiller discusses the history this project at length in *Mass Communications and American* Empire (N.Y.: Augustus M. Kelley, 1969), pp. 127-146.

applications.

During the 1960s, the RAND Corporation had begun to think about how to design a military communications network that would be invulnerable to a nuclear attack. Paul Baran, a RAND researcher whose work was financed by the Air Force, produced a classified report in 1964 proposing a radical solution to this communication problem. Baran envisioned a decentralized network of different types of "host" computers, without any central switchboard, designed to operate even if parts of it were destroyed. The network would consist of several "nodes," each equal in authority, each capable of sending and receiving pieces of data.

Each data fragment could thus travel one of several routes to its destination, such that no one part of the network would be completely dependent on the existence of another part. An experimental network of this type, funded by ARPA and thus known as ARPANET, was established at four universities in 1969.

Researchers at any one of the four nodes could share information, and could operate any one of the other machines remotely, over the new network. (Actually, former ARPA head Charles Herzfeld says that distributing computing power over a network, rather than creating a secure military command-and-control system, was the ARPANET's original goal, though this is a minority view.)

By 1972, the number of host computers connected to the ARPANET had increased to 37. Because it was so easy to send and retrieve data, within a few years the ARPANET became less a network for shared computing than a high-speed, federally subsidized, electronic post office. The main traffic on the ARPANET was not long-distance computing, but news and personal messages.

As parts of the ARPANET were declassified, commercial networks began to be connected to it. Any type of computer using a particular communications standard, or "protocol," was capable of sending and receiving information across the network. The design of these protocols was contracted out to private universities such as Stanford and the University of London, and was financed by a variety of federal agencies. The major thoroughfares or "trunk lines" continued to be financed by the Department of Defense.

By the early 1980s, private use of the ARPA communications protocol — what is now called "TCP/IP" — far exceeded military use. In 1984 the National Science Foundation assumed the responsibility of building and maintaining the trunk lines or "backbones." (ARPANET formally expired in 1989; by that time hardly anybody noticed). The NSF's Office of Advanced Computing financed the internet's infrastructure from 1984 until 1994, when the backbones were privatized.

In short, both the design and implementation of the internet have relied almost exclusively on government dollars....

We must be very careful not to describe the internet as a "private" technology, a spontaneous order, or a shining example of capitalistic ingenuity. It is none of these. Of course, almost all of the internet's current applications — unforeseen by its original designers — have been developed in the private sector.

(Unfortunately, the original web and the web browser are not among them, having been designed by the state-funded European Laboratory for Particle Physics (CERN) and the University of Illinois's NCSA.)

And today's internet would be impossible without the heroic efforts at Xerox PARC and Apple to develop a useable graphical user interface (GUI), a lightweight and durable mouse, and the Ethernet protocol. Still, none of these would have been viable without the huge investment of public dollars that brought the network into existence in the first place.

Now, it is easy to admire the *technology* of the internet. I marvel at it every day. But technological value is not the same as economic value. That can only be determined by the free choice of consumers to buy or not to buy. The ARPANET may well have been technologically superior to any commercial networks that existed at the time, just as Betamax may have been technologically superior to VHS, the MacOS to MS-DOS, and Dvorak to QWERTY. (Actually Dvorak wasn't.) But the products and features valued by engineers are not always the same as those valued by consumers. Markets select for economic superiority, not technological superiority (even in the presence of nefarious "network effects," as shown convincingly by Liebowitz and Margolis)....

What kind of global computer network would the market have selected? We can only guess. Maybe it would be more like the commercial online networks such as Comcast or MSN, or the private bulletin boards of the 1980s. Most likely, it would use some kind of pricing schedule, where different charges would be assessed for different types of transmissions.[60]

Johan Soderberg provides some more detail for one of the items Klein mentions, the Bulletin Board System (BBS):

The Internet was predated by a grassroots network, the Bulletin Board System (BBS). The software and the hardware devices necessary to hike on to the telephone lines and to send electronic text and code through it were largely developed by phone phreaks.[61]

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[60]Peter G. Klein, "Government Did Invent the Internet, But the Market Made It Glorious," Mises.Org, June 12, 2006 <http://www.mises.org/story/2211>.

[61] Johan Soderberg, *Hacking Capitalism: The Free and Open Source Software Movement* (New York and London: Routledge, 2008), p. 96.

The transition from NSF to private control in the early 1990s was described, fascinatingly, by a contemporary participant who reminisced in a Mises Blog comment on Klein's article:

> I started working at NASA Ames Research Center in July, 1992. Prior to this I had worked as a computer operator then network engineer for a large multinational, and I'd been using network services starting with Compu$erve in 1983, Fido-net, I-link, BBS's, etc.
>
> Being about as close to the heart of things as one could get, and working the graveyard and evening shifts, gave me a wonderful ring-side seat to watch as a Liberty occurred.
>
> Ames was the location of the Metropolitan Area Exchange, West. MAE-East was located at Goddard Space Flight Center, also my responsibility to monitor and help fix. This was where, if you were an "Internet" participant, your circuits were connected so that your IP packets could be routed to other "Internet" participants. Ames and Goddard also had two of the Root Name Servers, which I believe are still being run from there.
>
> The machines that held the look-up tables of participant addresses were owned and operated by the National Science Foundation. I had to watch over all this and make sure that the right people were notified if anything went wrong, so I was pretty much on top of who-owned-what.
>
> If you're old enough to remember, recall that AlGore had been promising the "Information Superhighway" long before he became Vice President. HillaryCare was in vogue, centralization not yet the boogyman in the press that it was to become. The Information Superhighway would have been 6 peering points, connected to each other, and everybody would have had to connect to one of these points by law in order to talk to anyone else by computer.
>
> Since I was working graveyard, then evening shift, I don't recall the exact date (graveyard and I don't get along) the Liberty occurred, but here's what it was: The NSF released control of the routing tables.
>
> Until then, the NSF was who said exactly who could connect to the "Internet" and how to get to them. That had also been the model of the Information Superhighway. Now it was up to the company or organization who connected to the MAE "ring" to maintain their own routing tables, their own equipment, to decide who they would reach and who they would not reach.
>
> The MAE-West, and -East, expanded to include other facilities because all the people who wanted to connect couldn't fit. It wasn't explosive, it was evolutionary. Only as experience and available capital increased could people be "good neighbors"

on the "rings". This and the MAE service contract also kept the growth problems as much as possible to just technical ones.

Content could now be commercial, since that had been one of the restrictions of the NSF. CNN.com came online, as did the AltaVista search engine nearby at Digital Equipment. The HTTP protocol and "browser" were established, and the smart BBS operators became dial-up real-time service providers, some of which morphed into Netcom, AOL, JPS, a list too long and too variable for anyone to know.

The need for every content consumer to reach every content provider, or even just for this email to be able to reach everyone on the list, created a market for those who maintained routs to "everyone" to sell the service of being able to get from here to there. People who didn't play nicely, like Alternet, didn't last long. Their own customers demanded the ability to reach everyone, and the sovereign consumer always wins in the end.

Everybody who had a clue knew that the MAE's couldn't handle the traffic, and quickly there were other "public" peering locations. Some, like the beautiful PAIX in Palo Alto, California, were computing facilities who created the same kind of environment that the early MAE's had been. Others, such as Pacific Bell and AADS-NAP Chicago, created virtual peering "points" which were actually just meshed networks within their own telephone switches. People built facilities and others came to use them, each free to offer desired services no matter what those may be. Freedom of infrastructure had occurred.[62]

As Klein's reference to private bulletin boards suggests, it is quite plausible that some sort of Internet would have come about through voluntary interaction and free contributions. Universities and private firms might have built a less ambitious system of trunk lines, and community bulletin boards might have linked together from the bottom up. It would almost certainly have been more decentralized and lower in capacity than the Internet we know today. One useful analogy might be Lewis Mumford's speculations on the local light rail networks that might have developed in a decentralized eotechnic economy, with the "national" system consisting largely of a loosely networked, low capacity amalgamation of local systems, as opposed to the centralized system of trunk lines actually created by the state. The Internet might, in that case, be a loose network of community Internets, with the process of patching through to a distant community bulletin board being comparable to that of making a long-distance call in the days before direct dialing.

It permits, for the first time, direction of global operations in real time from a single corporate headquarters, and is accelerating the concentration of capital on a global scale.

[62] Curt Howland, comment to Peter G. Klein, "Government Did Invent the Internet, But the Market Made It Glorious," Mises Economics Blog, June 12, 2006. http://blog.mises.org/archives/005174.asp.

To quote Chomsky again, "The telecommunications revolution... is... another state component of the international economy that didn't develop through private capital, but through the public paying to destroy themselves...."[63]

C. Patents and Copyrights

Although free market libertarians of all stripes are commonly stereotyped as apologists for big business, it is hard to imagine a position more at odds with the interests of big busines than the dominant libertarian view on patents. Certainly that is true of Murray Rothbard, who was not shy about denouncing patents as a fundamental violation of free market principles:

> The man who has not bought a machine and who arrives at the same invention independently, will, on the free market, be perfectly able to use and sell his invention. Patents prevent a man from using his invention even though all the property is his and he has not stolen the invention, either explicitly or implicitly, from the first inventor. Patents, therefore, are grants of exclusive monopoly privilege by the State and are invasions of property rights on the market.[64]

It is sometimes argued, in response to attacks on patents as monopolies, that "all property is a monopoly." True, as far as it goes; but tangible property is a monopoly by the nature of the case. A parcel of land can only be occupied and used by one owner at a time, because it is finite. By nature, two people cannot occupy the same physical space at the same time. "Intellectual property," in contrast, is an artificial monopoly on the right to perform a certain action--to arrange material elements or symbols in a particular configuration--which is not otherwise restricted of necessity to one person at a time. And unlike property in tangible goods and land, the defense of which is a necessary outgrowth of the attempt to maintain possession, enforcement of "property rights" in ideas requires the invasion of someone else's space.

> [E]veryone's property right is defended in libertarian law without a patent. If someone has an idea or plan and constructs an invention, and it is stolen from his house, the stealing is an act of theft illegal under general law. On the other hand, patents actually invade the property rights of those *independent* discoverers of an idea or an invention who made the discovery after the patentee…. Patents, therefore, invade rather than defend property rights.[65]

Patents make an astronomical price difference. Until the early 1970s, for example, Italy did not recognize drug patents. As a result, Roche Products charged the British

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[63] Noam Chomsky, *Class Warfare: Interviews with David Barsamian* (Monroe, Maine: Common Courage Press, 1996), p. 40.
[64] Rothbard, *Man, Economy, and State*. p. 5.
[65] Rothbard, *Power and Market*, p. 71.

national health a price over 40 times greater for patented components of Librium and Valium than charged by competitors in Italy.[66]

Patents suppress innovation as much as they encourage it. Chakravarthi Raghavan pointed out that research scientists who actually do the work of inventing are required to sign over patent rights as a condition of employment, while patents and industrial security programs prevent sharing of information, and suppress competition in further improvement of patented inventions.[67] Rothbard likewise argued that patents eliminate "the competitive spur for further research" because incremental innovation based on others' patents is hindered, and because the holder can "rest on his laurels for the entire period of the patent," with no fear of a competitor improving his invention. And they hamper technical progress because "mechanical inventions are discoveries of natural law rather than individual creations, and hence similar independent inventions occur all the time. The simultaneity of inventions is a familiar historical fact.[68]

Patents are also a hindrance to progress because of the "shoulders of giants" effect. Any new invention presupposes a wide variety of existing technologies that are combined and reworked into a new configuration. Patents on existing technologies may or may not marginally increase the incentives to new invention, but they also increase the cost of doing so by levying a tariff on the aggregation of existing knowledge to serve as building blocks of a new invention.[69] James Watt's refusal to license his patent on the steam engine, for example, prevented others from improving the design until the patent expired in 1800. This delayed the introduction of locomotives and steamboats.[70]

And patents are not necessary as an incentive to innovate, which means that their main practical effect is to cause economic inefficiency by levying a monopoly charge on the use of existing technology without significantly promoting innovation. According to Rothbard, invention is motivated not only by the quasi-rents accruing to the first firm to introduce an innovation, but by the threat of being surpassed in product features or productivity by its competitors. "In active competition... no business can afford to lag behind its competitors. The reputation of a firm depends upon its ability to keep ahead, to be the first in the market with new improvements in its products and new reductions in their prices."[71]

This is borne out by F. M. Scherer's testimony before the Federal Trade Commission in 1995.[72] Scherer spoke of a survey of 91 companies in which only seven "*accorded*

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[66] Chakravarthi Raghavan, *Recolonization: GATT, the Uruguay Round & the Third World* (Penang, Malaysia: Third World Network, 1990), p. 124.
[67] Chakravarthi Raghavan, *Recolonization: GATT, the Uruguay Round & the Third World* (Penang, Malaysia: Third World Network, 1990), p. 118.
[68] Rothbard, *Man, Economy, and State*, pp. 655, 658-9.
[69] Yochai Benkler, *The Wealth of Networks*, pp. 36-37.
[70] Soderberg, *Hacking Capitalism*, p. 116.
[71] Rothbard, *Power and Market*, p. 74.
[72] *Hearings on Global and Innovation-Based Competition*. FTC, 29 November 1995.

high significance to patent protection as a factor in their R & D investments." Most of them described patents as "*the least important of considerations*." Most companies considered their chief motivation in R & D decisions to be "*the necessity of remaining competitive, the desire for efficient production, and the desire to expand and diversify their sales*." In another study, Scherer found no negative effect on R & D spending as a result of compulsory licensing of patents. A survey of U.S. firms found that 86% of inventions would have been developed without patents. In the case of automobiles, office equipment, rubber products, and textiles, the figure was 100%.

The one exception was drugs, of which 60% supposedly would not have been invented. Even this is doubtful, though. For one thing, drug companies get an unusually high portion of their R & D funding from the government, and many of their most lucrative products were developed entirely at government expense. And Scherer himself cited evidence to the contrary. The reputation advantage for being the first into a market is considerable. For example in the late 1970s, the structure of the industry and pricing behavior was found to be very similar between drugs with and those without patents. Being the first mover with a non-patented drug allowed a company to maintain a 30% market share and to charge premium prices. We have already seen, in the previous chapter, the extent to which the direction of innovation of skewed by considerations of gaming the patent system and patent trolling the competition. The majority of R & D expenditure is geared toward developing "me, too" drugs: in essence slightly different versions of existing drugs, tweaked just enough to justify repatenting. And of the enormous R & D expenditures which patents are allegedly necessary to allow the drug companies to recoup, a majority goes not to developing the actual drug that goes to market, but to securing patent lockdown on all the possible major variations of that drug.

The injustice of patent monopolies is exacerbated by government funding of research and innovation, with private industry reaping monopoly profits from technology it spent little or nothing to develop. In 1999, extending the research and experimentation tax credit was, along with extensions of a number of other corporate tax preferences, considered the most urgent business of the Congressional leadership. Hastert, when asked if any elements of the tax bill were essential, said: "I think the [tax preference] extenders are something we're going to have to work on." Ways and Means Chair Bill Archer added, "before the year is out... we will do the extenders in a very stripped down bill that doesn't include anything else." A five-year extension of the research and experimentation credit (retroactive to 1 July 1999) was expected to cost $13.1 billion. (That credit makes the effective tax rate on R & D spending less than zero).[73]

The Government Patent Policy Act of 1980, with 1984 and 1986 amendments,

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<http://www.ftc.gov/opp/gc112195.pdf>.

[73] Citizens for Tax Justice. "GOP Leaders Distill Essence of Tax Plan: Surprise! It's Corporate Welfare" 14 September 1999 <http://www.ctj.org/pdf/corp0999.pdf>.

allowed private industry to keep patents on products developed with government R & D money--and then to charge ten, twenty, or forty times the cost of production. For example, AZT was developed with government money and in the public domain since 1964. The patent was given away to Burroughs Wellcome Corp.[74]

As if the deck were not sufficiently stacked already, Congress has more than once extended drug companies' patents beyond the expiration of their normal term under patent law; as just one example, the pharmaceutical companies in 1999 lobbied Congress to extend certain patents by two years by a special act of private law.[75]

So far we have considered patents mainly insofar as they resulted in unequal exchange and higher prices at the individual level--essentially from Tucker's standpoint of the nineteenth century. We have not yet examined their structural effects on the economy--the ways in which they promoted the corporate transformation of capitalism.

The patent privilege has been used on a massive scale to promote concentration of capital, erect entry barriers, and maintain a monopoly of advanced technology in the hands of western corporations. It is hard even to imagine how much more decentralized the economy would be without it.

Patents played a large role in the creation of the corporate economy from the late nineteenth century on. According to David Noble, they were "bought up in large numbers to suppress competition," which also resulted in "the suppression of invention itself."[76] Edwin Prindle, a corporate patent lawyer, wrote in 1906:

> Patents are the best and most effective means of controlling competition. They occasionally give absolute command of the market, enabling their owner to name the price without regard to the cost of production.... Patents are the only legal form of absolute monopoly.[77]

The exchange or pooling of patents between competitors, historically, has been a key method for cartelizing industries. This was true especially of the electrical appliance, communications, and chemical industries. G. E. and Westinghouse expanded to dominate the electrical manufacturing market at the turn of the century largely through patent control. In 1906 they curtailed the patent litigation between them by pooling their patents. G.E., in turn (later to become the patriarchal see of Gerard Swope), had been formed in 1892 by consolidating the patents of the Edison and Thomson-Houston interests.[78]

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[74] Chris Lewis, "Public Assets, Private Profits," *Multinational Monitor*, in *Project Censored Yearbook 1994* (New York: Seven Stories Press, 1994).
[75] Benjamin Grove, "Gibbons Backs Drug Monopoly Bill," *Las Vegas Sun* 18 February 2000 <http://www.ahc.umn.edu/NewsAlert/Feb00/022100NewsAlert/44500.htm>.
[76] David Noble, *America by Design: Science, Technology, and the Rise of Corporate Capitalism* (New York: Alfred A. Knopf, 1977), pp. 84-109.
[77] Ibid., p. 90.
[78] Ibid., p. 92.

AT&T also expanded "primarily through strategies of patent monopoly." The American chemical industry was marginal until 1917, when Attorney-General Mitchell Palmer seized German patents and distributed them among the major American chemical companies. Du Pont got licenses on 300 of the 735 patents.[79]

As Benjamin Darrington points out, "intellectual property" promotes large scale organization in another way. It

> promotes time and investment intensive forms of development and research with high potential payoffs at the expense of the incremental, tinkering sort of innovation that would prevail in the absence of these "rights," which tilts the market for the development of new technology and techniques in favor of centralized institutions and high-tech solutions.[80]

The rise of the global economy in recent decades has been associated with a severe upward ratcheting of copyright protections.

In the contemporary global economy, "intellectual property" plays the same protectionist role for TNCs that tariffs performed in the old national economies.

Bill Gates "Halloween Memo"

Darl McBride, of the software company SCO, warned Congress that "the unchecked spread of Open Source software, under the GPL, is a much more serious threat to the spread of our capitalist system than U.S. corporations realize."[81]

The new digital copyright regime has done away with many traditional limitations on copyright from the days when it affected mainly the print medium, like the fair use exception. We can thank the traditional exceptions to copyright, for example, for the public library and for free access to photocopiers.

Charles Johnson gives, as an example of the fair use exception, the common university practice of making course reserves available for photocopying, rather than expecting every student to buy a scholarly book at the academic publishing houses' steep rates. (I myself have numerous photocopies of books ordered through Interlibrary Loan, which would otherwise have cost me $70 or more, often for slim volumes of under two hundred pages.) But, he says,

> as soon as the University eliminates the paper medium, and facilitates *exactly the same thing* through an non-commercial, internal University course pack website — which does nothing at all more than what the xerox packets did, except that it delivers the information to pixels

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[79] Ibid., pp. 10, 16.
[80] Darington, op. cit., p. 18.
[81] <http://www.osaia.org/letters/sco_hill.pdf>, in Johan Soderberg, *Hacking Capitalism: The Free and Open Source Software Movement* (New York and London: Routledge, 2008), p. 31.

> on a monitor instead of toner on a page — the publishers' racket can run to court, throw up its arms, and start hollering Computers! Internet!, send their lawyers to try to shake down have a discussion with the University administration for new tribute to their monopoly business model, and then, failing that, *utterly uncontroversial* decades-old practices of sharing knowledge among colleagues and students suddenly become a legal case raising core issues like the future of the business model for academic publishers, while even the most absurd protectionist arguments are dutifully repeated by legal flacks on behalf of sustaining the racket. (Thus: It's difficult to argue that this is a truly noncommercial use [even though Georgia State receives no money from students for the course packs]. Georgia State may be a nonprofit institution, but its students pay a lot of money for course materials, and would presumably pay money for the materials being provided to them by the university.)[82]

Indeed, if copyright law for print media were governed by the same principles as the WIPO Copyright Treaty and the DMCA, photocopiers would either be considered an illegal technical means of circumventing copyright (with even the dissemination of technical information on how to build a photocopier being treated as criminal speech), or could be legally built only with mandated "DRM" safeguards to prevent the photocopying of copyrighted material.

D. Tariffs

As with patents, we are interested here in the aspects of tariffs that Tucker neglected: their effect in promoting the cartelization of industry. In the next chapter, on the rise of monopoly capitalism, we will see the full-blown effects of what Schumpeter called "export-dependent monopoly capitalism." That term refers to an economic system in which industry cartelizes behind the protection of tarriff barriers; sells its output domestically for a monopoly price significantly higher than market-clearing level, in order to obtain super-profits at the consumer's expense; and disposes of its unsellable product abroad, by dumping it below cost if necessary.

Brandeis referred to the tariff as "the mother of trusts" because of the way it facilitated collusion between large domestic producers and the creation of oligopolies. Mises, in *Human Action*, described the dependence of cartels on tariff barriers (especially interacting with other state-enforced monopolies like patents). Of course, in keeping with his usual "pro-business" emphasis, Mises treated the large industrial firms, at worst, as passive beneficiaries of a state protectionist policy aimed primarily at raising the wages of labor. This parallels his view of the early industrial capitalists, and their non-implication in the primitive accumulation process, in the previous chapter.

II. 20TH CENTURY STATE CAPITALISM

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[82] Charles Johnson, "How Intellectual Protectionism promotes the progress of science and the useful arts," *Rad Geek People's Daily*, May 28, 2008 <http://radgeek.com/gt/2008/05/28/how_intellectual/>.

The state capitalism of the twentieth century differed fundamentally from the misnamed "laissez-faire" capitalism of the nineteenth century in two regards: 1) the growth of direct organizational ties between corporations and the state, and the circulation of managerial personnel between them; and 2) the eclipse of surplus value extraction from the worker through the production process (as described by classical Marxism), by the extraction of "super-profits" a) from the consumer through the exchange process and b) from the taxpayer through the fiscal process.

Although microeconomics texts generally describe the functioning of supply and demand curves as though the nature of the market actors were unchanged since Adam Smith's day, in fact the rise of the large corporation as the dominant type of economic actor has been a revolution as profound as any in history. It occurred parallel to the rise of the "positive" state (i.e., the omnicompetent, centralized regulatory state) in the nineteenth and early twentieth century. And, vitally important to remember, the two phenomena were mutually reinforcing. The state's subsidies, privileges and other interventions in the market were the major force behind the centralization of the economy and the concentration of productive power. In turn, the corporate economy's need for stability and rationality, and for state-guaranteed profits, has been the central force behind the continuing growth of the leviathan state.

The rise of the centralized state and the centralized corporation has created a system in which the two are organizationally connected, and run by essentially the same recirculating elites (a study of the careers of David Rockefeller, Averell Harriman, and Robert McNamara should be instructive on the last point). This phenomenon has been most ably described by the "power elite" school of sociologists, particularly C. Wright Mills and G. William Domhoff.

It is interesting, in this regard, to compare the effect of antitrust legislation in the U.S. to that of nationalization in European "social democracies." In most cases, the firms affected by both policies involve centrally important infrastructures or resources, on which the corporate economy as a whole depends. Nationalization in the Old World is used primarily in the case of energy, transportation and communication. In the U.S., the most famous antitrust cases have been against Standard Oil, AT&T, and Microsoft: all cases in which excessive prices in one firm were perceived as a threat to the interests of monopoly capital as a whole. And recent "deregulation," as it has been applied to the trucking and airline industries, has likewise been in the service of those general corporate interests harmed by monopoly transportation prices. In all these cases, the state has on occasion acted as an executive committee on behalf of the entire corporate economy, by thwarting the mendacity of a few powerful corporations.

Rothbard treated the "war collectivism" of World War I as a prototype for twentieth century state capitalism. He described it as

> a new order marked by strong government, and extensive and pervasive government intervention and planning, for the purpose of providing a network of subsidies and

> monopolistic privileges to business, and especially to large business, interests. In particular, the economy could be cartelized under the aegis of government, with prices raised and production fixed and restricted, in the classic pattern of monopoly; and military and other government contracts could be channeled into the hands of favored corporate producers. Labor, which had been becoming increasingly rambunctious, could be tamed and bridled into the service of this new, state monopoly-capitalist order, through the device of promoting a suitably cooperative trade unionism, and by bringing the willing union leaders into the planning system as junior partners.[83]

The *International Socialist Review* in 1912, for example, warned workers not to be fooled into identifying social insurance or the nationalization of industry with "socialism." Such state programs as workers' compensation, old age and health insurance, were only measures to strengthen and stabilize capitalism. And nationalization simply reflected the capitalist's realization "that he can carry on certain portions of the production process more efficiently through his government than through private corporations..... Some muddleheads find that will be Socialism, but the capitalist knows better."[84] Friedrich Engels had taken the same view of public ownership:

> At a further stage of evolution this form [the joint-stock company] also becomes insufficient: the official representative of capitalist society--the state--will ultimately have to undertake the direction of production. This necessity for conversion into state property is felt first in the great institutions for intercourse and communication--the post office, the telegraphs, the railways.[85]

Kolko used the term "political capitalism" to describe the general objectives big business pursued through the "Progressive" state:

> *Political capitalism* is the utilization of political outlets to attain conditions of stability, predictability, and security--to attain rationalization--in the economy. *Stability* is the elimination of internecine competition and erratic fluctuations in the economy. *Predictability* is the ability, on the basis of politically stabilized and secured means, to plan future economic action on the basis of fairly calculable expectations. By *security* I mean protection from the political attacks latent in any formally democratic political structure. I do not give to *rationalization* its frequent definition as the improvement of efficiency, output, or internal organization of a company; I mean by the term, rather, the organization of the economy and the larger political and social

[83] Murray Rothbard, "War Collectivism in World War I," in Murray Rothbard and Ronald Radosh, eds., *A New History of Leviathan: Essays on the Rise of the American Corporate State* (New York: E. P. Dutton & Co., Inc., 1972), pp. 66-7.
[84] Robert Rives La Monte, "You and Your Vote," *International Socialist Review* XIII, No. 2 (August 1912); "Editorial," *International Socialist Review* XIII, No. 6 (December 1912).
[85] Friedrich Engels, *Anti-Dühring*, vol. 25 of Marx and Engels *Collected Works* (New York: International Publishers, 1987) 265.

> spheres in a manner that will allow corporations to function in a predictable and secure environment permitting reasonable profits over the long run.[86]

A. Cartelizing Regulations

From the turn of the twentieth century on, there was a series of attempts by corporate leaders to create some institutional structure by which price competition could be regulated and their respective market shares stabilized. "It was then," Paul Sweezy wrote,

> that U.S. businessmen learned the self-defeating nature of price-cutting as a competitive weapon and started the process of banning it through a complex network of laws (corporate and regulatory), institutions (e.g., trade associations), and conventions (e.g., price leadership) from normal business practice.[87]

But merely private attempts at cartelization (i.e., collusive price stabilization) before the Progressive Era--namely the so-called "trusts"--were miserable failures, according to Kolko. The dominant trend at the turn of the century--despite the effects of tariffs, patents, railroad subsidies, and other existing forms of statism--was competition. The trust movement was an attempt to cartelize the economy through such voluntary and private means as mergers, acquisitions, and price collusion. But the over-leveraged and over-capitalized trusts were even less efficient than before, and steadily lost market share at the hands of their smaller, more efficient competitors. Standard Oil and U.S. Steel, immediately after their formation, began a process of eroding market share. In the face of this resounding failure, big business acted through the state to cartelize itself--hence, the Progressive regulatory agenda. "Ironically, contrary to the consensus of historians, it was not the existence of monopoly that caused the federal government to intervene in the economy, but the lack of it."[88]

The FTC and Clayton Acts reversed this long trend toward competition and loss of market share and made stability possible.

> The provisions of the new laws attacking unfair competitors and price discrimination meant that the government would now make it possible for many trade associations to stabilize, for the first time, prices within their industries, and to make effective oligopoly a new phase of the economy.[89]

The Federal Trade Commission created a hospitable atmosphere for trade associations

[86] Gabriel Kolko, *The Triumph of Conservatism: A Reinterpretation of American History 1900-1916* (New York: The Free Press of Glencoe, 1963) 3.
[87] Paul M. Sweezy, "Competition and Monopoly," *Monthly Review* (May 1981), pp. 1-16.
[88] Kolko, *Triumph of Conservatism*, p. 5.
[89] Ibid., p. 268.

and their efforts to prevent price cutting.[90] The two pieces of legislation accomplished what the trusts had been unable to: it enabled a handful of firms in each industry to stabilize their market share and to maintain an oligopoly structure between them. This oligopoly pattern has remained stable ever since.

> It was during the war [i.e. WWI] that effective, working oligopoly and price and market agreements became operational in the dominant sectors of the American economy. The rapid diffusion of power in the economy and relatively easy entry [i.e., the conditions the trust movement failed to suppress] virtually ceased. Despite the cessation of important new legislative enactments, the unity of business and the federal government continued throughout the 1920s and thereafter, using the foundations laid in the Progressive Era to stabilize and consolidate conditions within various industries. And, on the same progressive foundations and exploiting the experience with the war agencies, Herbert Hoover and Franklin Roosevelt later formulated programs for saving American capitalism. The principle of utilizing the federal government to stabilize the economy, established in the context of modern industrialism during the Progressive Era, became the basis of political capitalism in its many later ramifications.[91]

Frank Dobbin, *The New Economic Sociology: A Reader* (Princeton, N.J.: Princeton University Press, 2004).

In addition, the various safety and quality regulations introduced during this period likewise had the effect of cartelizing the market. They served essentially the same purpose as the later attempts in the Wilson war economy to reduce the variety of styles and features available in product lines, in the name of "efficiency." Any action by the state to impose a uniform standard of quality (e.g. safety), across the board, necessarily eliminates that feature as a competitive issue between firms. As Butler Shaffer put it, the purpose of "wage, working condition, or product standards" is to "universalize cost factors and thus restrict price competition."[92] Thus, the industry is partially cartelized, to the very same extent that would have happened had all the firms in it adopted a uniform level of quality standards, and agreed to stop competing in that area. A regulation, in essence, is a state-enforced cartel in which the members agree to cease competing in a particular area of quality or safety, and instead agree on a uniform standard which they establish through the state. And unlike non-state-enforced cartels, which are unstable, no member can seek an advantage by defecting.

Although theoretically the regulations might simply put a floor on quality competition and leave firms free to compete by exceeding the standard, corporations often take a harsh view of competitors who exceed regulatory safety or quality requirements:

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[90] Ibid., p. 275.
[91] Ibid., p. 287.
[92] Butler Shaffer, *Calculated Chaos: Institutional Threats to Peace and Human Survival* (San Francisco: Alchemy Books, 1985), p. 143.

> The Bush administration said Tuesday it will fight to keep meatpackers from testing all their animals for mad cow disease.
>
> The Agriculture Department tests fewer than 1 percent of slaughtered cows for the disease, which can be fatal to humans who eat tainted beef. A beef producer in the western state of Kansas, Creekstone Farms Premium Beef, wants to test all of its cows.
>
> Larger meat companies feared that move because, if Creekstone should test its meat and advertised it as safe, they might have to perform the expensive tests on their larger herds as well.
>
> The Agriculture Department regulates the test and argued that widespread testing could lead to a false positive that would harm the meat industry.[93]

In other words, exceeding government safety standards unfairly implies that products which merely meet the ordinary USDA standard are less than adequate. Likewise, government minimum labeling requirements sometimes become a de facto maximum, with restraints the voluntary provision of additional information not required by law: e.g. Monsanto's legal thuggery against competitors which label their products as free from recombinant bovine growth hormone (rBGH), and similar use of "food libel" laws to constrain commercial free speech:

> FEDERAL AGENCIES ADVISED OF MISLEADING MILK LABELS AND ADVERTISING....
>
> ST LOUIS (April 3, 2007) - Monsanto Company announced today that letters from more than 500 concerned individuals and Monsanto have been submitted to the U.S. Food and Drug Administration (FDA) and Federal Trade Commission (FTC) requesting action to stop deceptive milk labeling and advertising. The two letters outline how certain milk labels and promotions that differentiate milk based on farmer use of POSILAC bovine somatotropin (bST) are misleading to consumers and do not meet the standards set by laws and regulations for either the Federal Trade Commission or the Food and Drug Administration.
>
> "The people who signed these letters are dairy producers, industry professionals and consumers from across the country who have expressed concerns about specific labels they find to be false or misleading," said Kevin Holloway, president of Monsanto Dairy Business. "In many cases, they came to Monsanto to find out what could be done about milk marketing tactics that disparage milk and deny farmers a

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[93] Associated Press, "U.S. government fights to keep meatpackers from testing all slaughtered cattle for mad cow," *International Herald-Tribune*, May 29, 2007 <http://www.iht.com/articles/ap/2007/05/29/america/NA-GEN-US-Mad-Cow.php>.

choice in using approved technologies. We believe FDA and FTC are the correct agencies to address the matter with the companies who employ misleading labels or promotions."

> The letter to the FDA highlights deceptive milk labels and calls for clear guidance and enforcement by FDA to address labeling that disparages milk from cows supplemented with POSILAC....
>
> "This is of great concern to dairy producers" said Dennis Areias, a Los Banos, Calif., dairy producer who signed the letters. "Deceptive labels suggest to consumers that there is something wrong with the milk they have been drinking for the past 13 years. Even though the companies that print these labels know this is not true, they choose to mislead consumers in an effort to charge more money for the same milk...."
>
> "Deceptive labels and ads are not only damaging to dairy producers who are forced to give up technology that helps them make a living, they hurt consumers" said John Vrieze, an Emerald, Wisc., dairy producer who also signed the letters to the FDA and FTC.
>
> "The misleading language clearly aims to scare people into paying more for the same milk. These ill-gotten gains are not shared with farmers and shame on us if we would seek to profit by disparaging the image of milk that we have invested heavily in promoting as a safe, healthy product."
>
> POSILAC is an FDA-approved supplement used by U.S. dairy farmers to increase productivity. Since it was first sold in 1994, POSILAC has become one of the leading dairy animal supplements in the United States.[94]

So once the FDA approves POSILAC, it is forbidden to advertise any product differentiation based on a more stringent safety standard than that of the FDA. Merely telling the consumer whether or not you choose to use FDA-approved additives constitutes disparagement of those who follow the government-established industry standard.

In one jurisdiction, the issue is no longer in doubt. Pennsylvania, in November 2007, officially prohibited dairies from labeling their milk growth hormone-free.

> State Agriculture Secretary Dennis C. Wolff said advertising one brand of milk as free from artificial hormones implies that competitors' milk is not safe, and it often comes with what he said is an unjustified higher price.
>
> "It's kind of like a nuclear arms race," Wolff said. "One dairy does it and the next tries to

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[94] "Monsanto Declares War on 'rBGH-free' Dairies," April 3, 2007 (reprint of Monsanto press release by Organic Consumers Association) <http://www.organicconsumers.org/articles/article_4698.cfm>.

> outdo them. It's absolutely crazy."...
>
> Monsanto spokesman Michael Doane said the hormone-free label "implies to consumers, who may or may not be informed on these issues, that there's a health-and-safety difference between these two milks, that there's 'good' milk and 'bad' milk, and we know that's not the case."
>
> Rick North of the Oregon Physicians for Social Responsibility, a leading critic of the artificial growth hormone, said the Pennsylvania rules amounted to censorship.
>
> "This is a clear example of Monsanto's influence," he said. "They're getting clobbered in the marketplace by consumers everywhere wanting rBGH-free products."
>
> Acting on a recommendation of an advisory panel, the Pennsylvania Agriculture Department has notified 16 dairies in Pennsylvania, New York, New Jersey, Connecticut and Massachusetts that their labels were false or misleading and had to be changed by the end of December.[95]

Every time I think the morally repellant filth at Monsanto have gone as far as humanly possible in trampling normal standards of decency underfoot, they manage to outdo themselves.

Nobody who's read the material above should be surprised to learn that Monsanto actually lobbied to preserve the regulatory state. When Congressman James Walsh, a New York Republican, tried in 1995 to repeal of GMO regulations, Monsanto and other leaders in the industry lobbied against the repeal.[96]

Similarly, the provision of services by the state (R&D funding, for example) removes them as components of price in cost competition between firms, and places them in the realm of guaranteed income to all firms in a market alike. Whether through regulations or direct state subsidies to various forms of accumulation, the corporations act through the state to carry out some activities jointly, and to restrict competition to selected areas.

Kolko provided abundant evidence that the main force behind this entire legislative agenda was big business. The Meat Inspection Act, for instance, was passed primarily at the behest of the big meat packers. In the 1880s, repeated scandals involving tainted meat had resulted in U.S. firms being shut out of several European markets. The big packers had turned to the U.S. government to conduct inspections on exported meat. By carrying out this function jointly, through the state, they removed quality inspection as a competitive issue between them, and the U.S. government provided a seal of approval in much the same way a trade association would--but at public expense. The problem with

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[95] "Pa. bars hormone-free milk labels," *USA Today*, November 13, 2007 <http://www.usatoday.com/news/nation/2007-11-13-milk-labels_N.htm>.

[96] Charlers Derber, *Corporation Nation: How Corporations are Taking Over Our Lives and What We Can Do About It* (New York: St. Martin's Griffin, 1998), p. 150.

this early inspection regime was that only the largest packers were involved in the export trade; mandatory inspections therefore gave a competitive advantage to the small firms that supplied only the domestic market. The main effect of Roosevelt's Meat Inspection Act was to bring the small packers into the inspection regime, and thereby end the competitive disability it imposed on large firms. Upton Sinclair simply served as an unwitting shill for the meat-packing industry.[97] This pattern was repeated, in its essential form, in virtually every component of the "Progressive" regulatory agenda.

Within the cartelizing framework of the regulatory state, it's a stretch to call the relationship between industries in an oligopoly market "competitive."

> The corporate web of today is a byzantine mix of interlocking board directorships, strategic alliances, and contracting networks that link virtually every Fortune 500 corporation with every other. John Malone, CEO of TCI, one of the great cable and media giants, describes his relationship to Rupert Murdoch as that of variously "competitors or partners or co-schemers."[98]

B. Central Banking Policy

Austrian theory of malinvestment. Monetary inflation lengthens the structure of production by making more roundabout forms of production seem artificially profitable, and thereby causing malinvestment--namely, the misdirection of resources into excessive amounts of higher order goods.

C. Tax Policy

Coase argued that the differential treatment, for sales tax purposes, of transactions organized through the market and transactions organized internally, gave a competitive advantage to the firm over the market: "...it is clear that [the sales tax] is a tax on market transactions and not on the same transactions organized within the firm." The sales tax, therefore, would not only "furnish a reason for the emergence of a firm in a specialized exchange economy," but "tend to make [firms] larger than they would otherwise be."[99]

Schumpeter on double taxation of dividends as a force for concentration. Hellwig on centralizing effects of funding primarily from retained earnings. Firms in the monopoly capital sector with retained earnings that exceed opportunities for rational investment will tend toward overaccumulation, while firms in the competitive sector will be starved for investment funds.

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[97] Kolko, *Triumph of Conservatism*, pp. 98-108.
[98] Derber, *Corporation Nation*, p. 18.
[99] Coase, "The Nature of the Firm," 1937.

Other tax policies also encourage the concentration of capital. Stock transactions involved in mergers and acquisitions are exempted from the capital gains tax, for example (Henry Manne referred to stock swaps as "one of the most important 'get-rich-quick' opportunities in our economy today").[100] And the interest on corporate debt is a significant deduction from the corporate income tax. A study of hostile takeovers in the '80s found that the tax savings from increased indebtedness was one of the chief benefits.[101]

Tax credits and deductions for research and development and for capital depreciation, along with state-subsidized technical education, tend to increase the capital- and technology-intensiveness of the predominant firm--thereby increasing the firm size and capitalization necessary to enter the market, and promoting cartelization.

D. The Corporate Liberal Pact With Labor

The old Progressive leitmotif of Big Business-Big Government collusion reappeared in the New Deal, along with another Crolyite theme: coopting labor into the corporatist system. The core of business support for the New Deal was, as Ronald Radosh described it, "leading moderate big businessmen and liberal-minded lawyers from large corporate enterprises."[102] Thomas Ferguson and Joel Rogers described them more specifically as "a new power bloc of capital-intensive industries, investment banks, and internationally oriented commercial banks."[103] (This is also the bloc of industries which, as Joseph Stromberg points out, is most heavily dependent on government promotion of exports and other action to absorb its surplus output; likewise, according to the Austrian class theory of Walter Grinder and John Hagel, it is the bloc of industry that profits directly from credit inflation by the central banking system, which promotes artificially roundabout forms of production.)

Labor was a relatively minor part of the total cost package of such businesses; at the same time, capital-intensive industry, as Galbraith pointed out in his analysis of the "technostructure," depended on long-term stability and predictability for planning. Therefore, this segment of big business was willing to trade higher wages for social peace

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[100] Henry Manne, "Mergers and the Market for Corporate Control," p. 113. [110-119]

[101] Sanjai Bhagat, Andrei Shleifer and Robert W. Vishny, "Hostile Takeovers in the 1980s: The Return to Corporate Specialization," *Brookings Papers on Economic Activity: Microeconomics* (1990), pp. 1-85. Quoted in Doug Henwood, *Wall Street: How it Works and for Whom* (London and New York: Verso, 1997), p. 280.

[102] Ronald Radosh, "The Myth of the New Deal," in Rothbard and Radosh, eds., *A New History of Leviathan*, pp. 154-5.

[103] Thomas Ferguson and Joel Rogers. *Right Turn* (New York: Hill and Wang, 1986), p. 46; this line of analysis is pursued more intensively in Thomas Ferguson, *Golden Rule*: *The Investment Theory of Party Competition and the Logic of Money-Driven Political Systems* (Chicago: University of Chicago Press, 1995).

in the workplace.[104] The roots of this faction can be traced to the relatively "progressive" employers described by James Weinstein in his account of the National Civic Federation at the turn of the century, who were willing to engage in collective bargaining over wages and working conditions in return for uncontested management control of the workplace.[105]

This attitude was at the root of the Taylorist/Fordist social contract, in which the labor bureaucrats agreed to let management manage, so long as labor got an adequate share of the pie.[106] Such an understanding was most emphatically in the interests of large corporations. The sitdown movement in the auto industry and the organizing strikes among West coast longshoremen were virtual revolutions among rank and file workers on the shop floor. In many cases, they were turning into regional general strikes. The Wagner Act domesticated this revolution and brought it under the control of professional labor bureaucrats.

Industrial unionism, from the employer's viewpoint, had the advantage over craft unionism of providing a single bargaining agent with which management could deal. One of the reasons for the popularity of "company unions" among large corporations, besides the obvious advantages in pliability, was the fact that they were an alternative to the host of separate craft unions of the AFL. Even in terms of pliability, the industrial unions of the Thirties had some of the advantages of company unions. By bringing collective bargaining under the aegis of federal labor law, corporate management was able to use union leadership to discipline their own rank and file, and to use the federal courts as a mechanism of enforcement.

> The New Dealers devised... a means to integrate big labor into the corporate state. But only unions that were industrially organized, and which paralleled in their structure the organization of industry itself, could play the appropriate role. A successful corporate state required a safe industrial-union movement to work. It also required a union leadership that shared the desire to operate the economy from the top in formal conferences with the leaders of the other functional economic groups, particularly the corporate leaders. The CIO unions... provided such a union leadership.[107]

Moderate members of the corporate elite also gained reassurance from the earlier British experience in accepting collective bargaining. Collective bargaining did not affect the distribution of wealth, for one thing: "Labor gains were made due to the general growth in wealth and at the expense of the consumer, which would mean small businessmen, pensioners, farmers, and nonunionized white collar employees." (Not to mention a large contingent of unskilled laborers and lumpenproles without bargaining

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[104] Ferguson, *Golden Rule* pp. 117 et seq.; John Kenneth Galbraith, *The New Industrial State* (New York: Signet Books, 1967), pp. 25-37, 258-9, 274, 287-9.
[105] Weinstein, *Corporate Ideal in the Liberal State*, esp. the first two chapters.
[106] Montgomery, *Workers' Control in America*, pp. 49-57.
[107] Radosh, "The Myth of the New Deal," pp. 178-9, 181.

leverage against the employing classes). And the British found that firms in a position of oligopoly, with a relatively inelastic demand, were able to pass increased labor costs on to the consumer at virtually no cost to themselves.[108]

The Wagner Act served the central purposes of the corporate elite. To some extent it was a response to mass pressure from below. But the decision on whether and how to respond, the form of the response, and the implementation of the response, were all firmly in the hands of the corporate elite. According to Domhoff (writing in *The Higher Circles*), "The benefits to capital were several: greater efficiency and productivity from labor, less labor turnover, the disciplining of the labor force by labor unions, the possibility of planning labor costs over the long run, and the dampening of radical doctrines."[109] James O'Connor described it this way: "From the standpoint of monopoly capital the main function of unions was... to inhibit disruptive, spontaneous rank-and-file activity (e.g., wildcat strikes and slowdowns) and to maintain labor discipline in general. In other words, unions were... the guarantors of 'managerial prerogatives.'"[110] The objectives of stability and productivity were more likely to be met by such a limited Taylorist social compact than by a return to the labor violence and state repression of the late nineteenth century.

In *The Power Elite and the State*, Domhoff put forth a slightly more nuanced thesis than in *The Higher Circles*.[111] It was true, he admitted, that a majority of large corporations opposed the Wagner Act in its final form. But the basic principles of collective bargaining embodied in it had been the outcome of decades of corporate liberal theory and practice, worked out through policy networks in which "progressive" large corporations had played a leading role; the National Civic Federation, as Weinstein described its career, was a typical example of such networks. The motives of those in the Roosevelt administration who framed the Wagner Act were very much in the mainstream of corporate liberalism. Although they may have been ambivalent about the specific form of FDR's labor legislation, Swope and his corporate fellow travelers had played the major role in formulating the principles behind it. Whatever individual business leaders thought of Wagner, it was drafted by mainstream corporate lawyers who were products of the intellectual climate created by those same business leaders; and it was drafted with a view to their interests. Although it was not accepted by big business as a whole, it was largely the creation of representatives of big business interests whose understanding of the Act's purpose was largely the same as those outlined in Domhoff's quote above from *The Higher Circles*. At the same time, although it was designed to contain the threat of working class power, it enjoyed broad working class support as the best deal they were likely to get. The class nature of the legislation was further complicated by the fact that the southern segment of the Democratic Party establishment, largely made up of large

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[108] Domhoff, *Higher Circles*, p. 223.
[109] Domhoff, *Higher Circles*, p. 225.
[110] James O'Connor, *The Fiscal Crisis of the State* (New York: St. Martin's Press, 1973).
[111] G. William Domhoff, *The Power Elite and the State: How Policy is Made in America* (New York: Aldine de Gruyter, 1990), pp. 65-105.

agricultural capitalists, used its veto power to limit the corporate liberal agenda of the big industrialists: the southern wing was willing to go along with Wagner because it specifically exempted agricultural laborers.

Another major aspect of American labor policy, which perhaps began with Cleveland's response to the Pullman strike, was continued in the Railway Labor Relations Act and Taft-Hartley (which, in James O'Connor's words, "included a ban on secondary boycotts and hence tried to 'illegalize' class solidarity...",[112] and Truman's and Bush's threats to use soldiers as scabs in, respectively, the steelworkers' and longshoremen's strikes. Taft-Hartley's "cooling off" and arbitration provisions enable the government to intervene in any case where transport workers threaten to turn a local dispute into a general strike.

Of course, the facts of the case are an almost complete reversal of the vulgar libertarian critique of organized labor, which commonly asserts that unions depend entirely on force (or the implicit threat of force), backed by the state, against non-union laborers. They assume, in so arguing, that the strike as it is known today has always been the primary method of labor struggle. Any of Thomas DiLorenzo's articles on the subject at Mises.Org can be taken as a proxy for this ideological tendency. I quote the following as an example:

> Historically, the main "weapon" that unions have employed to try to push wages above the levels that employees could get by bargaining for themselves on the free market without a union has been the strike. But in order for the strike to work, and for unions to have any significance at all, some form of coercion or violence must be used to keep competing workers out of the labor market.[113]

This betrays a profound ignorance of the history of the labor movement outside the sterile bubble of the Wagner Act.

First of all, when the strike *was* chosen as a weapon, it relied more on the threat of imposing costs on the employer than on the forcible exclusion of scabs. You wouldn't think it so hard for the Misoids to understand that the replacement of a major portion of the workforce, especially when the supply of replacement workers is limited by moral sympathy with the strike, might entail considerable transaction costs and disruption of production. The idiosyncratic knowledge of the existing workforce, the time and cost of bringing replacement workers to an equivalent level of productivity, and the damage short-term disruption of production may do to customer relations, together constitute a rent that invests the threat of walking out with a considerable deterrent value. And the cost and disruption is greatly intensified when the strike is backed by sympathy strikes at other stages of production.

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[112] James O'Connor, *Accumulation Crisis* (Oxford: Basil Blackwell Ltd, 1984) p. 75.
[113] Thomas DiLorenzo, "The Myth of Voluntary Unions," Mises.Org, September 14, 2004 <http://www.mises.org/story/1604>.

Wagner and Taft-Hartley greatly reduced the effectiveness of strikes at individual plants by transforming them into declared wars fought by Queensbury rules, and likewise reduced their effectiveness by prohibiting the coordination of actions across multiple plants or industries. Taft-Hartley's cooling off periods, in addition, gave employers time to prepare ahead of time for such disruptions and greatly reduced the informational rents embodied in the training of the existing workforce. Were not such restrictions in place, today's "just-in-time" economy would likely be far more vulnerable to such disruption than that of the 1930s.

More importantly, though, unionism was historically less about strikes or excluding non-union workers from the workplace than about what workers did *inside* the workplace to strengthen their bargaining power against the boss.

The Wagner Act, along with the rest of the corporate liberal legal regime, had as its central goal the redirection of labor resistance away from the successful asymmetric warfare model, toward a formalized, bureaucratic system centered on labor contracts enforced by the state and the union hierarchies. As Karl Hess suggested in a 1976 *Playboy* interview,

> one crucial similarity between those two fascists [Hitler and FDR] is that both successfully destroyed the trade unions. Roosevelt did it by passing exactly the reforms that would ensure the creation of a trade-union bureaucracy. Since F.D.R., the unions have become the protectors of contracts rather than the spearhead of worker demands. And the Roosevelt era brought the "no strike" clause, the notion that your rights are limited by the needs of the state.[114]

The federal labor law regime criminalizes many forms of resistance, like sympathy and boycott strikes up and down the production chain from raw materials to retail, that made the mass and general strikes of the early 1930s so formidable. The Railway Labor Relations Act, which has since been applied to airlines, was specifically designed to prevent transport workers from turning local strikes into general strikes. Taft-Hartley's cooling off period can be used for similar purposes in other strategic sectors, as demonstrated by Bush's invocation of it against the longshoremen's union.

E. The Socialization of Cost

The common thread in all these lines of analysis is that an ever-growing portion of the functions of the capitalist economy have been carried out through the state. According to James O'Connor, state expenditures under monopoly capitalism can be divided into

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[114] I'm indebted to the blogger freeman, libertarian critter for scanning it in online: "More From Hess," *freeman, libertarian critter*, June 9, 2005 <http://freemanlc.blogspot.com/2005/06/more-from-hess.html>.

"social capital" and "social expenses."

> *Social capital* is expenditures required for profitable private accumulation; it is indirectly productive (in Marxist terms, social capital indirectly expands surplus value). There are two kinds of social capital: social investment and social consumption (in Marxist terms, social constant capital and social variable capital).... *Social investment* consist of projects and services that increase the productivity of a given amount of laborpower and, other factors being equal, increase the rate of profit.... *Social consumption* consists of projects and services that lower the reproduction costs of labor and, other factors being equal, increase the rate of profit. An example of this is social insurance, which expands the productive powers of the work force while simultaneously lowering labor costs. The second category, *social expenses*, consists of projects and services which are required to maintain social harmony--to fulfill the state's "legitimization" function.... The best example is the welfare system, which is designed chiefly to keep social peace among unemployed workers.[115]

According to O'Connor, such state expenditures counteract the falling general rate of profit that Marx predicted. Monopoly capital is able to externalize many of its operating expenses on the state; and since the state's expenditures indirectly increase the productivity of labor and capital at taxpayer expense, the apparent rate of profit is increased.

> Unquestionably, monopoly sector growth depends on the continuous expansion of social investment and social consumption projects that in part or in whole indirectly increase productivity from the standpoint of monopoly capital. In short, monopoly capital socializes more and more costs of production.[116]

O'Connor listed several of the main ways in which monopoly capital externalizes its operating costs on the political system:

> Capitalist production has become more interdependent--more dependent on science and technology, labor functions more specialized, and the division of labor more extensive. Consequently, the monopoly sector (and to a much lesser degree the competitive sector) requires increasing numbers of technical and administrative workers. It also requires increasing amounts of infrastructure (physical overhead capital)--transportation, communication, R&D, education, and other facilities. In short, the monopoly sector requires more and more social investment in relation to private capital.... The costs of social investment (or social constant capital) are not borne by monopoly capital but rather are socialized and fall on the state.[117]

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[115] O'Connor, *Fiscal Crisis of the State*, pp. 6-7.
[116] Ibid., p. 24.
[117] Ibid., p. 24.

As suggested already by our reference above to O'Connor, these forms of state expenditure have the practical effect of promoting several of the "counteracting influences" to the declining rate of profit that Marx described in Volume 3 of *Capital*. The second such influence Marx listed, for example, was the "depression of wages below the value of labor power." Through welfare, taxpayer-funded education, and other means of subsidizing the reproduction cost of labor-power, the state reduces the minimum sustainable cost of labor-power that must be paid by employers. Regarding education, in particular, the Austrian economists Walter Grinder and John Hagel commented from a free market perspective:

> A distinct institutional framework, benefitting from extensive socialization of costs, supplies the economy with a highly skilled and literate labor force inculated with "technocratic" values. The evolution of the state-financed educational system has been profoundly influenced by the changing needs of the corporate economy and this itimate, if somewhat inefficient, relationship has been a prominent characteristic of state capitalist societies. Compulsory education also inculates a value system encouraging subservience and docility among unskilled labor and the lower strata of society.[118]

This is true, likewise, of Marx's third influence: the "cheapening of the elements of constant capital." The state, by subsidizing many of the operating costs of large corporations, artificially shifts their balance sheet further into the black. The fourth influence listed, "relative overpopulation," is promoted by state subsidies to the adoption of capital-intensive forms of production and to the education of technically skilled manpower at government expense--with the effect of artificially increasing the supply of labor relative to demand, and thus reducing its bargaining power in the labor market.[119] According to Samuel Bowles and Herbert Gintis, the formal right of the employer to hire and fire

> is effective... only when the cost to workers is high; that is, when there is a large pool of labor with the appropriate skills available in the larger society, into which workers are threatened to be pushed. Indeed, ...the maintenance of such a "reserve army" of skilled labor has been a major, and not unintended, effect of U.S. education through the years.[120]

We should briefly recall here our examination above of how such socialization of expenditures serves to cartelize industry. By externalizing such costs on the state, through the general tax system, monopoly capital removes these expenditures as an issue of cost competition between individual firms. It is as if all the firms in an industry formed a

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[118] Walter E. Grinder and John Hagel, "Toward a Theory of State Capitalism: Ultimate Decision-Making and Class Structure," *Journal of Libertarian Studies* 1:1 (Spring 1977), p. 73 <http://www.mises.org/journals/jls/1_1/1_1_7.pdf>.

[119] Karl Marx and Friedrich Engels, *Capital* vol. 3, vol. 37 of Marx and Engels *Collected Works* (New York: International Publishers, 1998), pp. 234-5.

[120] Samuel Bowles and Herbert Gintis, *Schooling in Capitalist America: Educational Reform and the Contradictions of Economic Life* (New York: Basic Books, Inc., Publishers, 1976), p. 55.

cartel to administer these costs in common, and agreed not to include them in their price competition. The costs and benefits are applied uniformly to the entire industry, removing it as a competitive disadvantage for some firms.

Although it flies in the face of "progressive" myth, big business is by no means uniformly opposed to national health insurance and other forms of social insurance. Currently, giant corporations in the monopoly capital sector are the most likely to provide private insurance to their employees; and such insurance is one of the fastest-rising components of labor costs. Consequently, firms that are already providing this service at their own expense are the logical beneficiaries of a nationalized system. The effect of such a national health system would be to remove the cost of this benefit as a competitive disadvantage for the companies that provided it. Even if the state requires only large corporations in the monopoly sector to provide health insurance, it is an improvement of the current situation, from the monopoly capital point of view: health insurance ceases to be a component of price competition among the largest firms. A national health system provides a competitive advantage to a nation's firms at the expense of their foreign competitors, who have to fund their own employee health benefits--hence, American capital's hostility to the Canadian national health, and its repeated attempts to combat it through the WTO. The cartelizing effects of socializing the costs of social insurance, likewise, was one reason a significant segment of monopoly capital supported FDR's Social Security agenda.

Daniel Gross, although erroneously viewing it as a departure from big business's supposed hostility to the welfare state, has made the same point about more recent big business support of government health insurance.[121] Large American corporations, by shouldering the burden of health insurance and other employee benefits borne by the state in Europe and Japan, is at a competitive disadvantage both against companies there and against smaller firms here.

Democratic presidential candidate Dick Gephart, or rather his spokesman Jim English, admitted to a corporate liberal motivation for state-funded health insurance in his 2003 Labor Day address. Gephart's proposed mandatory employer coverage, with a 60% tax credit for the cost, would (he said) eliminate competition from companies that don't currently provide health insurance as an employee benefit. It would also reduce competition from firms in countries with a single-payer system.[122]

The level of technical training necessary to keep the existing corporate system running, the current level of capital intensiveness of production, and the current level of R&D efforts on which it depends, would none of them pay for themselves on a free market. The state's education system provides a technical labor force at public expense, and whenever possible overproduces technical specialists on the level needed to ensure

[121] Daniel Gross, "Socialism, American Style: Why American CEOs covet a massive European-style social-welfare state" *Slate* Aug. 1, 2003 <http://slate.msn.com/id/2086511/>.
[122] C-SPAN, September 1, 2003.

that technical workers are willing to take work on the employers' terms. On this count, O'Connor quoted Veblen: the state answers capital's "need of a free supply of trained subordinates at reasonable wages...."[123] Starting with the Morrill Act of 1862, which subsidized agricultural and mechanical colleges, the federal government has underwritten a major part of the reproduction costs of technical labor.[124] In research and development, likewise, federal support goes back at least to the agricultural and experiment stations of the late nineteenth century, created pursuant to the Hatch Act of 1887.[125]

The state's cartelization and socialization of the cost of reproducing a technically sophisticated labor force, and its subsidies to R&D, make possible a far higher technical level of production than would support itself in a free market. The G.I. Bill was an integral part of the unprecedentedly high scale of state capitalism created during and after WWII.

> Technical-administrative knowledge and skills, unlike other forms of capital over which private capitalists claim ownership, cannot be monopolized by any one or a few industrial-finance interests. The discoveries of science and technology spill over the boundaries of particular corporations and industries, especially in the epoch of mass communications, electronic information processing, and international labor mobility. Capital in the form of knowledge resides in the specialized skills and abilities of the working class itself. In the context of a free market for laborpower... no one corporation or industry or industrial-finance interest group can afford to train its own labor force or channel profits into the requisite amount of R&D. Patents afford some protection, but there is no guarantee that a particular corporation's key employees will not seek positions with other corporations or industries. The cost of losing trained laborpower is especially high in companies that employ technical workers whose skills are specific to particular industrial process--skills paid for by the company in question. Thus, on-the-job training (OJT) is little used not because it is technically inefficient... but because it does not pay.

Nor can any one corporation or industrial-finance interest afford to develop its own R&D or train the administrative personnel increasingly needed to plan, coordinate, and control the production and distribution process. In the last analysis, the state is required to coordinate R&D because of the high costs and uncertainty of getting utilizable results.[126]

At best, from the point of view of the employer, the state creates a "reserve army" of scientific and technical labor--as William Appleman Williams described it, the elite has "seen to it that experts are a glut on the market."[127] At worst, when there is a shortage of

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[123] O'Connor, *Fiscal Crisis of the State*, p. 111.
[124] Noble, *America by Design*, pp. 24 et seq.
[125] Ibid., p. 132.
[126] O'Connor, *Fiscal Crisis of the State*, p. 112.
[127] William Appleman Williams, "A Profile of the Corporate Elite," in Rothbard and Radosh, eds., *New History of Leviathan*, p. 5.

such labor-power, the state at least absorbs the cost of reproducing it and removes it as a component of private industry's operating costs. In either case, "the greater the socialization of the costs of variable capital, the lower will be the level of money wages, and... the higher the rate of profit in the monopoly sector."[128] And since the monopoly capital sector is able to pass its taxes onto the consumer or to the competitive capital sector, the effect is that "the costs of training technical laborpower are met by taxes paid by competitive sector capital and labor."[129]

The "public" schools' curriculum can much more justly be described as servile than liberal education. Its objective is a human product which is capable of fulfilling the technical needs of corporate capital and the state, but at the same time docile and compliant, and incapable of any critical analysis of the system of power it serves. The public educationist movement and the creation of the first state school systems, remember, coincided with the rising factory system's need for a work force that was trained in obedience, punctuality, and regular habits. Technical competence and a "good attitude" toward authority, combined with twelve years of conditioning in not standing out or making waves, were the goal of the public educationists.

Even welfare expenses, although O'Connor classed them as a completely unproductive expenditure, are in fact another example of the state underwriting variable capital costs. Some socialists love to speculate that, if it were possible, capitalists would lower the prevailing rate of subsistence pay to that required to keep workers alive only when they were employed. But since that would entail starvation during periods of unemployment, the prevailing wage must cover contingencies of unemployment; otherwise, wages would be less than the minimum cost of reproducing labor. Under the welfare state, however, the state itself absorbs the cost of providing for such contingencies of unemployment, so that the uncertainty premium is removed as a component of wages in Adam Smith's "higgling of the market."

And leaving this aside, even as a pure "social expense," the welfare system acts primarily (in O'Connor's words) to "control the surplus population politically."[130] The state's subsidies to the accumulation of constant capital and to the reproduction of scientific-technical labor provide an incentive for much more capital-intensive forms of production than would have come about in a free market, and thus contribute to the growth of a permanent underclass of surplus labor;[131] the state steps in and undertakes the minimum cost necessary to prevent large-scale homelessness and starvation, which would destabilize the system, and to maintain close supervision of the underclass through the human services bureaucracy.[132]

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[128] O'Connor, *Fiscal Crisis of the State*, p. 124.
[129] Ibid., p.160.
[130] Ibid., p. 69.
[131] Ibid., p. 161.
[132] Piven and Cloward, *Regulating the Poor*.

The general effect of the state's intervention in the economy, then, is to remove ever increasing spheres of economic activity from the realm of competition in price or quality, and to organize them collectively through organized capital as a whole.

Through the military-industrial complex, the state has socialized a major share--probably the majority--of the cost of "private" business's research and development. If anything the role of the state as purchaser of surplus economic output is eclipsed by its role as subsidizer of research cost, as Charles Nathanson pointed out. The research and development process was heavily militarized by the Cold War "military-R&D complex." Military R&D often results in basic, general use technologies with broad civilian applications. Technologies originally developed for the Pentagon have often become the basis for entire categories of consumer goods.[133] The general effect has been to "substantially [eliminate] the major risk area of capitalism: the development of and experimentation with new processes of production and new products."[134]

This is the case in electronics especially, where many products originally developed by military R&D "have become the new commercial growth areas of the economy."[135] Transistors and other forms of miniaturized circuitry were developed primarily with Pentagon research money. The federal government was the primary market for large mainframe computers in the early days of the industry; without government contracts, the industry might never have had sufficient production runs to adopt mass production and reduce unit costs low enough to enter the private market. And the infrastructure for the worldwide web itself was created by the Pentagon's DARPA, originally as a redundant global communications system that could survive a nuclear war. Any implied commentary on the career of Bill Gates is, of course, unintended.

Overall, Nathanson estimated, industry depended on military funding for around 60% of its research and development spending; but this figure is considerably understated by the fact that a significant part of nominally civilian R&D spending is aimed at developing civilian applications for military technology.[136] It is also understated by the fact that military R&D is often used for developing production technologies (like automated control systems in the machine tool industry) that become the basis for production methods throughout the civilian sector.

F. State Action to Absorb Surplus Output

The roots of the corporate state in the U.S., more than anything else, lie in the crisis of overproduction as perceived by corporate and state elites--especially the traumatic Depression of the 1890s--and the requirement, also as perveived by them, for state

[133] Nathanson, p. 208.
[134] Ibid., p. 230.
[135] Ibid., p. 230.
[136] Ibid., pp. 222-25.

intervention to absorb surplus output or otherwise deal with the problems of overproduction, underconsumption, and overaccumulation.

William Appleman Williams summarized the lesson of the 1890s in this way: "Because of its dramatic and extensive nature, the Crisis of the 1890's raised in many sections of American society the specter of chaos and revolution."[137] American economic elites saw it as the result of overproduction and surplus capital, and believed it could be resolved only through access to a "new frontier." Without state-guaranteed access to foreign markets, output would be too far below capacity, unit costs would be driven up, and unemployment would reach dangerous levels.

The seriousness of the last threat was underscored by the radicalism of the Nineties. The Pullman Strike, Homestead, and the formation of the Western Federation of Miners (in many ways the precursor organization to the IWW) were signs of dangerous levels of labor unrest and class consciousness. Coxey's Army marched on Washington, a small foretaste of the kinds of radicalism that could be produced by unemployment. The labor, socialist, and anarchist movements had a growing foreign component, more radical than the older native faction, and the People's Party seemed to have a serious chance of winning national elections. At one point Jay Gould, the mouthpiece of the robber barons, was threatening a capital strike (much like those in Venezuela recently) if the populists came to power. In 1894 businessman F. L. Stetson warned, "We are on the edge of a very dark night, unless a return of commercial prosperity relieves popular discontent."[138] Both business and government resounded with claims that U.S. productive capacity had outstripped the domestic market's ability to consume, and that the government had to take active measures to obtain outlets.

This perception is often ridiculed by Austrians on the grounds that overproduction and underconsumption simply cannot happen: "J.B. Say said it, I believe it, that settles it." They ignore the fact that Say's law only applies to a free market. One might just as well airily dismiss Mises' theories of malinvestment and the crackup boom on the grounds that "such things cannot happen in the free market." Both assurances would doubtless be comforting--if only we had a free market. But as it is, we have a corporatist system in which the state subsidizes overaccumulation and the cartelization of industry, so that overbuilt industry cannot dispose of its entire product when operating at full capacity--especially not at cartel prices. Neo-Marxist theories of overproduction and imperialism, and New Left revisionist treatments of American foreign policy, both lend themselves quite well to thoughful Austrian analysis. Joseph Stromberg's essay, "The Role of State Monopoly Capitalism in the American Empire,"[139] is an excellent example of such an approach.

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[137] William Appleman Williams, *The Tragedy of American Diplomacy* (New York: Dell Publishing Company, 1959, 1962) 21-2.
[138] Ibid., p. 26.
[139] *Journal of Libertarian Studies* Volume 15, no. 3 (Summer 2001) http://www.mises.org/journals/jls/15_3/15_3_3.pdf.

The theoretical justification for state intervention was found in the work of John Maynard Keynes, and the corporate state of the New Deal was justified in large part as the practical implementation of Keynesian thought. The abortive NRA was an attempt to solve the problem of overproduction by government-sponsored industrial cartels: by that means, corporations would be able to set prices and apportion shares of output among themselves so as to maximize income through monopoly pricing, thus guaranteeing them a minimum rate of profit even while operating far below capacity. Besides this unsuccessful attempt, thwarted by the Supreme Court, FDR also attempted to mobilize idle manpower and spending power through deficit-funded spending programs, with mixed results at best.

The crowning achievement of FDR's state capitalism, of course, was the military-industrial complex which arose from World War II, and has continued ever since. It has since been described, variously, as "military Keynesianism," or a "perpetual war economy." A first step in realizing the monumental scale of the war economy's effect is to consider that the total value of plant and equipment in the United States increased by about two-thirds (from $40 to $66 billion) between 1939 and 1945, most of it a taxpayer "gift" of forced investment funds provided to the country's largest corporations.[140] Profit was virtually guaranteed on war production through "cost-plus" contracts.[141] In addition, some two-thirds of federal R&D spending was channeled through the 68 largest private laboratories (40% of it to the ten largest), and the resulting patents given away to the companies that carried out the research under government contract.[142]

Demobilization of the war economy after 1945 very nearly threw the overbuilt and government-dependent industrial sector into a renewed depression. For example, in *Harry Truman and the War Scare of 1948,* Frank Kofsky described the aircraft industry as spiraling into red ink after the end of the war, and on the verge of bankruptcy when it was rescued by Truman's new bout of Cold War spending on heavy bombers.[143]

The Cold War restored the corporate economy's heavy reliance on the state as a source of guaranteed sales. Charles Nathanson argued that "one conclusion is inescapable: major firms with huge aggregations of corporate capital owe their survival after World War II to the Cold War...."[144] For example, David Noble pointed out that civilian jumbo jets would never have existed without the government's heavy bomber contracts. The production runs for the civilian market alone were too small to pay for the complex and expensive machinery. The 747 is essentially a spinoff of military

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140 C. Wright Mills, *The Power Elite* (Oxford and New York: Oxford University Press, 1956, 2000), p. 101.
141 David W. Eakins, "Business Planners and America's Postwar Expansion," in David Horowitz, ed., *Corporations and the Cold War* (New York and London: Monthly Review Press, 1969), p. 148.
142 G. William Domhoff, *Who Rules America?* (Englewood Cliffs, N.J.: Prentice-Hall, 1967), p. 121.
143 Frank Kofsky, *Harry S. Truman and the War Scare of 1948* (New York: St. Martin's Press, 1993).
144 Charles E. Nathanson, "The Militarization of the American Economy," in Horowitz, ed., *Corporations and the Cold War*, p. 214.

production.[145]

The heavy industrial and high tech sectors were given a virtually guaranteed outlet, not only by U.S. military procurement, but by grants and loan guarantees for foreign military sales under the Military Assistance Program. Although apologists for the military-industrial complex have tried to stress the relatively small fraction of total production represented by military goods, it makes more sense to compare the volume of military procurement to the amount of idle capacity. Military production runs amounting to a minor percentage of total production might absorb a major part of total excess production capacity, and have a huge effect on reducing unit costs. Besides, the rate of profit on military contracts tends to be quite a bit higher, given the fact that military goods have no "standard" market price, and the fact that prices are set by political means (as periodic Pentagon budget scandals should tell us).[146] So military contracts, small though they might be as a portion of a firm's total output, might well make the difference between profit and loss.

Seymour Melman described the "permanent war economy" as a privately-owned, centrally-planned economy that included most heavy manufacturing and high tech industry. This "*state-controlled economy*" was based on the principles of "maximization of costs and of government subsidies."[147]

> It can draw on the federal budget for virtually unlimited capital. It operates in an insulated, monopoly market that makes the state-capitalist firms, singly and jointly, impervious to inflation, to poor productivity performance, to poor product design and poor production managing. The subsidy pattern has made the state-capitalist firms failure-proof. That is the state-capitalist replacement for the classic self-correcting mechanisms of the competitive, cost-minimizing, profit-maximizing firm.[148]

The chief virtue of the military economy is its utter unproductivity. That is, it does not compete with private industry to supply any good for which there is consumer demand. But military production is not the only such area of unproductive government spending. Neo-Marxist Paul Mattick elaborated on the theme in a 1956 article. The overbuilt corporate economy, he wrote, ran up against the problem that "[p]rivate capital formation... finds its limitation in diminishing market-demand." The State had to absorb part of the surplus output; but it had to do so without competing with corporations in the private market. Instead, "[g]overnment-induced production is channeled into non-market fields--the production of non-competitive public-works, armaments, superfluities and waste.[149] As a necessary result of this state of affairs,

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[145] Noble, *America by Design*, pp. 6-7.
[146] Nathanson, "The Militarization of the American Economy," p. 208.
[147] Seymour Melman, *The Permanent War Economy: American Capitalism in Decline* (New York: Simon and Schuster, 1974), p. 11.
[148] Ibid., p. 21.
[149] Paul Mattick, "The Economics of War and Peace," *Dissent* (Fall 1956), p. 377.

> so long as the principle of competitive capital production prevails, steadily growing production will in increasing measure be a "production for the sake of production," benefiting neither private capital nor the population at large.
>
> This process is somewhat obscured, it is true, by the apparent profitability of capital and the lack of large-scale unemployment. Like the state of prosperity, profitability, too, is now largely government manipulated. Government spending and taxation are managed so as to strengthen big business at the expense of the economy as a whole....
>
> In order to increase the scale of production and to accummulate [sic] capital, government creates "demand" by ordering the production of non-marketable goods, financed by government borrowings. This means that the government avails itself of productive resources belonging to private capital which would otherwise be idle.[150]

Such consumption of output, while not always directly profitable to private industry, serves a function analogous to foreign "dumping" below cost, in enabling industry to operate at full capacity despite the insufficiency of private demand to absorb the entire product at the cost of production.

It's interesting to consider how many segments of the economy have a guaranteed market for their output, or a "conscript clientele" in place of willing consumers. The "military-industrial complex" is well known. But how about the state's education and penal systems? How about the automobile-trucking-highway complex, or the civil aviation complex? Foreign surplus disposal ("export dependant monopoly capitalism") and domestic surplus disposal (government purchases) are different forms of the same phenomenon.

Finally, as Marx pointed out in Volume Three of *Capital*, the rise of major new forms of industry could serve as a countervailing influence against the falling direct rate of profit" resulting from overaccumulation. Baran and Sweezy, likewise, considered "epoch-making inventions" as partial counterbalances to the ever-increasing surplus. Their chief example of such a phenomenon was the rise of the automobile industry in the 1920s, which (along with the highway program) was to define the American economy for most of the mid-20th century.[151] The high tech boom of the 1990s was a similarly revolutionary event. It is revealing to consider the extent to which both the automobile and computer industries, far more than most industries, were direct products of state capitalism. And as we shall see in the next section of this chapter, the dominant and most profitable sectors of the new global economy are those most heavily reliant on state protection or subsidy.

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[150] Ibid., pp. 378-9.
[151] Paul Baran and Paul Sweezy, *Monopoly Capitalism: An Essay in the American Economic and Social Order* (New York: Monthly Review Press, 1966), p. 220.

G. Neoliberal Foreign Policy

Neoliberal foreign policy, in large measure, is a subset of the broader category of state action to absorb surplus output and surplus capital.

The central theme of American foreign policy, from the 1890s until today, was what William Appleman Williams called "Open Door imperialism";[152] it consisted of using U.S. political power to guarantee access to foreign markets and resources on terms favorable to American corporate interests, without relying on direct political rule. Its central goal was to obtain for U.S. merchandise, in each national market, treatment equal to that afforded any other industrial nation. Most importantly, this entailed active engagement by the U.S. government in breaking down the imperial powers' existing spheres of economic influence or preference. The result, in most cases, was to treat as hostile to U.S. security interests any large-scale attempt at autarky, or any other policy whose effect was to withdraw a major area of the world from the disposal of the U.S. corporate economy. When the power attempting such policies was an equal, like the British Empire, the U.S. reaction was merely one of measured coolness. When it was perceived as an inferior, like Japan, the U.S. resorted to more forceful measures, as events of the late 1930s indicate. And whatever the degree of equality between advanced nations in their access to Third World markets, it was clear that Third World nations were still to be subordinated to the industrialized West in a collective sense.

This Open Door system was the direct ancestor of today's neoliberal system, which is falsely called "free trade" in the apologetics of court intellectuals. It depended on active management of the world economy by dominant states, and continuing intervention to police the international economic order and enforce sanctions against states which did not cooperate.

The Breton Woods System, created on the initiative of FDR and Truman in the latter part of World War II, was the culmination of Open Door Empire. The second Roosevelt's administration saw the guarantee of American access to foreign markets as vital to ending the Depression and the threat of internal upheaval that went along with it. FDR's ongoing policy of Open Door Empire, faced with the withdrawal of major areas from the world market by the autarkic policies of the Greater East Asia Co-Prosperity Sphere and Fortress Europe, led to American entry into World War II, and culminated in the postwar establishment of what Samuel Huntington called a "system of world order" guaranteed both by global institutions of economic governance like the IMF, and by a hegemonic political and military superpower.

Beginning in the summer of 1940, the CFR and State Department undertook a joint

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[152] William Appleman Williams, *The Contours of American History* (Cleveland and New York: The World Publishing Company, 1961).

study to determine the minimum portion of the world the U.S. would have to integrate with its own economy, in order to provide sufficient resources and markets for economic stability; it also explored policy options for reconstructing the postwar world. They found that the U.S. economy could not survive in its existing form without access to the resources and markets not only of the Western Hemisphere, but of the British Empire and the Far East (together called the Grand Area). But the latter region was rapidly being incorporated into Japan's economic sphere of influence. And the fall of France and the Low Countries , and the ongoing Battle of Britain, raised the possibility that the fall of Britain might be followed by the Royal Navy (and with it some portion of the Empire) falling into German hands. FDR made the political decision to contest Japanese power in the Far East, and if necessary to initiate war.[153] In the end, however, he successfully maneuvered Japan into firing the first shot.

The American policy that emerged from these struggles was one of securing control over the markets and resources of the global "Grand Area" through institutions of global economic governance, reflected in the postwar Bretton Woods system.

The problem of access to foreign markets and resources was central to U.S. policy planning for a postwar world. Given the structural imperatives of what Schumpeter called "export dependent monopoly capitalism,"[154] the fear of a postwar depression was a real one. The original drive toward foreign expansion at the end of the nineteenth century reflected the fact that industry, with state capitalist encouragement, had expanded far beyond the ability of the domestic market to consume its output. Even before World War II, the state capitalist economy had serious trouble operating at the level of output needed for full utilization of capacity and cost control. Military-industrial policy during the war greatly exacerbated the problem of over-accumulation, increasing the value of plant and equipment by two-thirds at taxpayer expense. The end of the war, if followed by the traditional pattern of demobilization, would result in a drastic reduction in orders to that same overbuilt industry just as over ten million workers were being dumped back into the

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[153] Laurence H. Shoup and William Minter, "Shaping a New World Order: The Council on Foreign Relations' Blueprint for World Hegemony, 1939-1945," in Holly Sklar, ed., *Trilateralism: The Trilateral Commission and Elite Planning for World Management* (Boston: South End Press, 1980), pp. 135-56

[154] "Union in a cartel or trust confers various benefits on the entrepreneur--a saving in costs, a stronger position as against the workers--but none of these compares with this one advantage: a monopolistic price policy, possible to any considerable degree *only* behind an adequate protective tariff. Now the price that bings the maximum monopoly profit is generally far above the price that would be fixed by fluctuating competitive costs, and the volume that can be marketed at that maximum price is generally far below the output that would be technically and economically feasible. Under free competition that output *would* be produced and offered, but a trust cannot offer it, for it could be sold only at a competitive price. Yet the trust *must* produce it--or approximately as much--otherwise the advantages of large-scale enterprise remain unexploited and unit costs are likely to be uneconomically high.... [The trust] extricates itself from this dilemma by producing the full output that is economically feasible, thus securing low costs, and offering in the protected domestic market only the quantity corresponding to the monopoly price--insofar as the tariff permits; while the rest is sold, or "dumped," abroad at a lower price.... "
--Joseph Schumpeter, "Imperialism," in *Imperialism, Social Classes: Two Essays by Joseph Schumpeter.* Translated by Heinz Norden. Introduction by Hert Hoselitz (New York: Meridian Books, 1955) 79-80.

civilian labor force.

A central facet of postwar economic policy, as reflected in the Bretton Woods agencies, was state intervention to guarantee markets for the full output of U.S. industry and profitable outlets for surplus capital. The World Bank was designed to subsidize the export of capital to the Third World, by financing the infrastructure without which Western-owned production facilities could not be established there. According to Gabriel Kolko's 1988 estimate, almost two thirds of the World Bank's loans since its inception had gone to transportation and power infrastructure.[155] A laudatory Treasury Department report referred to such infrastructure projects (comprising some 48% of lending in FY 1980) as "externalities" to business, and spoke glowingly of the benefits of such projects in promoting the expansion of business into large market areas and the consolidation and commercialization of agriculture.[156]

A good example is the Volta River power project, built with American loans (at high interest). The primary beneficiary was Kaiser aluminum, which got electricity at very low rates.[157]

An anecdote from E. F. Schumacher, in *Good Work*, illustrates the dependence of large centralized enterprise on subsidized transportation. The Zambian government encouraged production of eggs as a way of augmenting protein consumption. Unfortunately, farmers lacked adequate means of packaging eggs for transport to market. Schumacher's Intermediate Technology Development Group approached the primary manufacturer of egg trays, a TNC, about the possibility of creating small egg tray factories in Zambia. The response, from the European division:

> Forget it. The smallest machine makes a million a month. So, unless you can somehow organize an All-African Common Market for Egg Trays, and build the roads for the lorries all coming out of Lusaka, to distribute the egg trays to the rural areas....

The corporation's engineers were confident that production on a smaller scale would be "completely uneconomical." Schumacher, however, approached the Engineering Department of the University of Reading; its designers worked out a process for small-scale manufacture of egg trays. The prototype plant, which operated at roughly two percent the output of the TNC's mega-factories, with two percent of the capital outlay, found it entirely economical.[158]

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[155] Gabriel Kolko, *Confronting the Third World: United States Foreign Policy 1945-1980* (New York: Pantheon Books, 1988), p. 120.
[156] *United States Participation in the Multilateral Development Banks in the 1980s*. Department of the Treasury (Washingon, DC: 1982), p. 9.
[157] Stavrianos, *Promise of the Coming Dark Age*, p. 42.
[158] E.F. Schumacher, *Good Work*, pp. 58-60.

More recently, companies engaged in the supposedly "free market" activity of offshoring work notified host governments of their requirements for corporate welfare:

> SUNIL RAMAN, BBC - The Indian city of Bangalore must improve its infrastructure if it wants to hold on to vital IT business, company executives have warned. The heads of some of the biggest companies in India's IT industry have asked the government of the southern Indian state of Karnataka to improve infrastructure in Bangalore, or they will move their businesses to other states. The high-profile delegation included bosses of top Indian IT companies Wipro and Infosys, as well as representatives from Dell, IBM, Intel, and Texas Instruments among others.[159]

Besides the benefit of building "an internal infrastructure which is a vital prerequisite for the development of resources and direct United States private investments," such banks (because they must be repaid in U.S. dollars) require the borrowing nations "to export goods capable of earning them, which is to say, raw materials...."[160]

The International Monetary Fund was created to facilitate the purchase of American goods abroad, by preventing temporary lapses in purchasing power as a result of foreign exchange shortages. It was "a very large international currency exchange and credit-granting institution that could be drawn upon relatively easily by any country that was temporarily short of any given foreign currency due to trade imbalances."[161]

The Bretton Woods system by itself, however, was not nearly sufficient to ensure the levels of output needed to keep production facilities running at full capacity, or to absorb excess investment funds. First the Marshall Plan, and then the permanent war economy of the Cold War, came to the rescue.

The Marshall Plan was devised in reaction to the impending economic slump predicted by the Council of Economic advisers in early 1947 and the failure of Western Europe "to recover from the war and take its place in the American scheme of things." Undersecretary of State for Economic Affairs Clayton declared that the central problem confronting the United States was the disposal of its "great surplus."[162]

One New Deal partisan implicitly compared foreign economic expansion to domestic state capitalism as analogous forms of surplus disposal: "it is as if we were building a TVA every Tuesday."[163]

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[159] "Now Bangalore Faces Outsourcing" <http://news.bbc.co.uk/1/low/business/3553156.stm>.
[160] Gabriel Kolko, *The Roots of American Foreign Policy: An Analysis of Power and Purpose* (Boston: Beacon Press, 1969), p. 72.
[161] G. William Domhoff, *The Power Elite and the State: How Policy is Made in America* (New York: Aldine de Gruyter, 1990), p. 166.
[162] Williams, *Tragedy of American Diplomacy*, p. 271.
[163] Ibid., p. 272.

The permanent war economy, however, had another advantage over projects like the TVA that produced use-value for the civilian population: since it did not produce consumer goods, it did not add to the undisposable surplus or compete with the output of private capital in consumer markets. In the apt words of Immanuel Goldstein: "Even when weapons of war are not actually destroyed, their manufacture is still a convenient way of expending labor power without producing anything that can be consumed." War is a way of "shattering to pieces, or pouring into the stratosphere, or sinking in the depths of the sea," excess output and capital.[164]

Besides facilitating the export of goods and capital, the Bretton Woods agencies play a central role in the discipline of recalcitrant regimes. There is a considerable body of radical literature on the Left on the use of debt as a political weapon to impose pro-corporate policies (e.g., the infamous "structural adjustment program") on Third World governments, analogous to the historic function of debt in keeping miners and sharecroppers in their place.[165] As David Korten argued,

> The very process of the borrowing that created the indebtedness that gave the World Bank and the IMF the power to dictate the policies of borrowing countries represented an egregious assault on the principles of democratic accountability. Loan agreements, whether with the World Bank, the IMF, other official lending institutions, or commercial banks, are routinely negotiated in secret between banking officials and a handful of government officials--who in many instances are themselves unelected and unaccountable to the people on whose behalf they are obligating the national treasury to foreign lenders. Even in democracies, the borrowing procedures generally bypass the normal appropriation processes of democratically elected legislative bodies. Thus, government agencies are able to increase their own budgets without legislative approval, even though the legislative body will have to come up with the revenues to cover repayment. Foreign loans also enable governments to increase current expenditures without the need to raise current taxes--a feature that is especially popular with wealthy decision makers. The same officials who approve the loans often benefit directly through participation in contracts and "commissions" from grateful contractors. The system creates a powerful incentive to over-borrow.[166]

Another way the Bretton Woods agencies exercise political power over recalcitrant regimes is the punitive withholding of aid. This powerful political weapon has been used

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[164] George Orwell, *1984*. Signet Classics reprint (New York: Harcourt Brace Jovanovich, 1949, 1981), p. 157.

[165] Cheryl Payer, *The Debt Trap: The International Monetary Fund and the Third World* (New York: Monthly Review Press, 1974); Walden Bello, "Structural Adjustment Programs: 'Success' for Whom?" in Jerry Mander and Edward Goldsmith, eds., *The Case Against the Global Economy* (San Francisco: Sierra Club Books, 1996); Bruce Franklin. "Debt Peonage: The Highest Form of Imperialism?" *Monthly Review* 33:10 (March 1982) 15-31.

[166] David Korten, *When Corporations Rule the World* (West Hartford, Conn.: Kumarian Press, 1995; San Francisco, Calif.: Berrett-Koehler, Publishers, Inc., 1995) 166.

at times to undermine elective democracies whose policies fell afoul of corporate interests, and to reward compliant dictatorships. For example, the World Bank refused to lend to the Goulart government in Brazil; but following the installation of a military dictatorship by the 1964 coup, the Bank's lending averaged $73 million a year for the rest of the decade, and reached almost a half-billion by the mid-70s. Chile, before and after the Pinochet coup, followed a similar pattern.[167] Or as Ambassador Korry warned, in the latter-day equivalent of a papal interdict, "Not a nut or bolt shall reach Chile under Allende. Once Allende comes to power we shall do all within our power to condemn Chile and all Chileans to utmost deprivation and poverty."[168]

Cheryl Payer's *The Debt Trap* is an excellent historical survey of the use of debt crises to force countries into standby arrangements, precipitate coups, or provoke military crackdowns. In addition to their use against Goulart and Allende, as mentioned above, she provides case studies of the Suharto coup in Indonesia and Marcos' declaration of martial law in the Philippines.

Among the many features of the so-called structural adjustment program, mentioned above, the policy of "privatization" (by selling state assets to "latter-day Reconstructionists," as Sean Corrigan says below) stands out. Joseph Stromberg described the process, as it has been used by the Iraq Provisional Authority, as "funny auctions, that amounted to new expropriations by domestic and foreign investors...." Such auctions of state properties will "likely lead... to a massive alienation of resources into the hands of select foreign interests."[169]

The promotion of unaccountable, technocratic Third World governments, insulated from popular pressure and closely tied to international financial elites, has been a central goal of Bretton Woods agencies since World War II.

> From the 1950s onwards, a primary focus of [World] Bank policy was "institution-building", most often taking the form of promoting the creation of autonomous agencies within governments that would be continual World Bank borrowers. Such agencies were intentionally established to be independent financially from their host governments, as well as minimally accountable politically--except, of course, to the Bank.[170]

The World Bank created the Economic Development Institute in 1956 specifically to enculture Third World elites into the values of the Bretton Woods system. It offered a

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[167] Bruce Rich, "The Cuckoo in the Nest: Fifty Years of Political Meddling by the World Bank," *The Ecologist* (January/February 1994), p. 10.
[168] Holly Sklar, "Overview," in Holly Sklar, ed., *Trilateralism: The Trilateral Commission and Elite Planning for World Management* (Boston: South End Press, 1980), p. 28-9.
[169] Joseph R. Stromberg, "Experimental Economics, Indeed" Ludwig von Mises Institute, January 6, 2004 <http://www.mises.org/fullstory.asp?control=1409>.
[170] Rich, "Cuckoo in the Nest," p. 9.

six-month course in "the theory and practice of development," whose 1300 alumni by 1971 included prime ministers, ministers of planning, and ministers of finance.[171]

> The creation of such patronage networks has been one of the World Bank's most important strategies for inserting itself in the political economies of Third World countries. Operating according to their own charters and rules (frequently drafted in response to Bank suggestions), and staffed with rising technocrats sympathetic, even beholden, to the Bank, the agencies it has funded have served to create a steady, reliable source of what the Bank needs most--bankable loan proposals. They have also provided the Bank with critical power bases through which it has been able to transform national economies, indeed whole societies, without the bothersome procedures of democratic review and discussion of the alternatives.[172]

Despite the vast body of scholarly literature on the issues discussed in this passage, perhaps the most apt description of it was a pithy comment by a free market libertarian, Sean Corrigan:

> Does he [Treasury Secretary O'Neill] not know that the whole IMF-US Treasury carpet-bagging strategy of full-spectrum dominance is based on promoting unproductive government-led indebtedness abroad, at increasingly usurious rates of interest, and then--either before or, more often these days, after, the point of default--bailing out the Western banks who have been the agents provocateurs of this financial Operation Overlord, with newly-minted dollars, to the detriment of the citizenry at home?
>
> Is he not aware that, subsequent to the collapse, these latter-day Reconstructionists must be allowed to swoop and to buy controlling ownership stakes in resources and productive capital made ludicrously cheap by devaluation, or outright monetary collapse?
>
> Does he not understand that he must simultaneously coerce the target nation into sweating its people to churn out export goods in order to service the newly refinanced debt, in addition to piling up excess dollar reserves as a supposed bulwark against future speculative attacks (usually financed by the same Western banks' lending to their Special Forces colleagues at the macro hedge funds) - thus ensuring the reverse mercantilism of Rubinomics is maintained?[173]

What the American elite means by "free markets" and "free trade" has been ably stated by Thomas Friedman in one of his lapses into frankness:

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[171] Ibid., pp. 9-10.
[172] Ibid., p. 10.
[173] Sean Corrigan, "You Can't Say That!" August 6, 2002, *LewRockwell.Com* <http://www.lewrockwell.com/corrigan/corrigan13.html>.

> For globalism to work, America can't be afraid to act like the almighty superpower it is.... The hidden hand of the market will never work without a hidden fist--McDonald's cannot flourish without McDonnell Douglas, the designer of the F-15. And the hidden fist that keeps the world safe for Silicon Valley's technologies is called the United States Army, Air Force, Navy and Marine Corps.[174]

The "system of world order" enforced by the U.S. since World War II, and so celebrated by Friedman, is nearly the reverse of the classical liberal notion of free trade. This new version of "free trade" is aptly characterized in a passage by Christopher Layne and Benjamin Schwarz:

> The view that economic interdependence compels American global strategic engagement puts an ironic twist on liberal internationalist arguments about the virtues of free trade, which held that removing the state from international transactions would be an antidote to war and imperialism....
>
> ....Instead of subscribing to the classical liberal view that free trade leads to peace, the foreign policy community looks to American military power to impose harmony so that free trade can take place. Thus, U.S. security commitments are viewed as the indispensable precondition for economic interdependence.[175]

Oliver MacDonagh pointed out that the modern neoliberal conception, far from agreeing with Cobden's idea of free trade, resembled the "Palmerstonian system" that the Cobdenites so despised. Cobden objected, among other things, to the "dispatch of a fleet 'to protect British interests' in Portugal," to the "loan-mongering and debt-collecting operations in which our Government engaged either as principal or agent," and generally, all "intervention on behalf of British creditors overseas." Cobden favored the "natural" growth of free trade, as opposed to the forcible opening of markets. Genuine free traders opposed the confusion of "free trade" with "mere increases of commerce or with the forcible 'opening up' of markets."[176]

The neoliberal understanding of "How to Have Free Trade" was lampooned quite effectively by Joseph Stromberg:

> For many in the US political and foreign policy Establishment, the formula for having free trade would go something like this: 1) Find yourself a global superpower; 2) have this superpower knock together the heads of all opponents and skeptics until everyone is playing by the same rules; 3) refer to this new imperial order as "free trade;" 4) talk quite a bit about "democracy." This is the end of the story except for

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[174] Thomas Friedman, "What the World Needs Now," *New York Times*, March 28, 1999.
[175] Christopher Layne and Benjamin Shwartz, "American Hegemony Without an Enemy," *Foreign Policy* (Fall 1993), pp. 12-3.
[176] Oliver MacDonough, "The Anti-Imperialism of Free Trade," *The Economic History Review* (Second Series) 14:3 (1962).

> such possible corollaries as 1) never allow rival claimants to arise which might aspire to co-manage the system of "free trade"; 2) the global superpower rightfully in charge of world order must also control the world monetary system....
>
> The formula outlined above was decidedly not the 18th and 19th-century liberal view of free trade. Free traders like Richard Cobden, John Bright, Frederic Bastiat, and Condy Raguet believed that free trade is the absence of barriers to goods crossing borders, most particularly the absence of special taxes--tariffs--which made imported goods artificially dear, often for the benefit of special interests wrapped in the flag under slogans of economic nationalism....
>
> This sea-change in the accepted meaning of free trade neatly parallels other characteristically 20th-century re-definitions of concepts like "war," "peace," "freedom," and "democracy," to name just a few. In the case of free trade I think we can deduce that when, from 1932 on, the Democratic Party-- with its traditional rhetoric about free trade in the older sense--took over the Republicans project of neo-mercantilism and economic empire, it was natural for them to carry it forward under the "free trade" slogan. They were not wedded to tariffs, which, in their view, got in the way of implementing Open Door Empire. Like an 18th-century Spanish Bourbon government, they stood for freer trade within an existing or projected mercantilist system. They would have agreed, as well, with Lord Palmerston, who said in 1841, "It is the business of Government to open and secure the roads of the merchant." ....
>
> Here, John A. Hobson... was directly in the line of real free-trade thought. Hobson wrote that businessmen ought to take their own risks in investing overseas. They had no right to call on their home governments to "open and secure" their markets.[177]

And by the way, it's doubtful that superpower competition with the Soviets had much to do with the role of the U.S. in shaping the postwar "system of world order," or in acting as "hegemonic power" in maintaining that system of order. Layne and Schwarz cited NSC-68 to the effect that the policy of "attempting to develop a healthy international community" was "a policy which we would probably pursue even if there were no Soviet threat."

> Underpinning U.S. world order strategy is the belief that America must maintain what is in essence a military protectorate in economically critical regions to ensure that America's vital trade and financial relations will not be disrupted by political upheaval. This kind of economically determined strategy articulated by the foreign policy elite ironically (perhaps unwittingly) embraces a quasi-Marxist or, more correctly, a Leninist interpretation of American foreign relations.[178]

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[177] Joseph R. Stromberg, "Free Trade, Mercantilism and Empire," February 28, 2000 <http://www.antiwar.com/stromberg/s022800.html>.

[178] Layne and Shwartz, "American Hegemony Without an Enemy," pp. 5, 12.

The policy planners who designed the Bretton Woods system and the rest of the postwar framework of world order, apparently, paid little or no mind to the issue of Soviet Russia's prospective role in the world. The record that appears, rather, in Shoup and Minter's heavily documented account, is full of references to the U.S. as a successor to Great Britain as guarantor of a global political and economic order, and to U.S. global hegemony as a war aim (even before the U.S. entered the war). As early as 1942, when Soviet Russia's continued existence was very much in doubt, U.S. policy makers were referring to "domination after the war," "Pax Americana," and "world control." To quote G. William Domhoff, "the definition of the national interest that led to these interventions was conceived in the years 1940-42 by corporate planners in terms of what they saw as the needs of the American capitalist system, well before communism was their primary concern."[179]

The central feature of the post-Axis world, as envisioned by American planners, was the replacement of a world order under British by one under American hegemony. If anything, the Cold War with the Soviet Union appears almost as an afterthought to American planning for a postwar order. Far from being the cause of the U.S. role as guarantor of a system of world order, the Soviet Empire acted as a spoiler to preexisting U.S. plans for acting as sole global superpower.

Historically, any rival power which has refused to be incorporated into the Grand Area, or which has encouraged other countries (by "defection from within") to withdraw from the Grand Area, has been viewed as an "aggressor." Quoting Domhoff once again,

> ....I believe that anticommunism became a key aspect of foreign policy only after the Soviet Union, China, and their Communist party allies became the challengers to the Grand Area conception of the national interest. In a certain sense..., they merely replaced the fascists of Germany and Japan as the enemies of the international economic and political system regarded as essential by American leaders.[180]

Likewise, as Domhoff's last sentence in the above quote suggests, any country which has interfered with U.S. attempts to integrate the markets and resources of any region of the world into its international economic order has been viewed as a "threat." The Economic and Financial Group of the CFR/State Department postwar planning project, produced, on July 24, 1941, a document (E-B34), warning of the need for the United States to "defend the Grand Area," not only against external attack by Germany, but against "defection from within," particularly against countries like Japan (which, along with the rest of east Asia, was regarded as part of the Grand Area) bent on "destroying the area for its own political reasons."[181] The centrality of this consideration is illustrated by the report of a 1955 study group of the Woodrow Wilson Center, which pointed to the threat of "a serious reduction in the potential resource base and market opportunities of

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[179] Domhoff, *The Power Elite and the State*, p. 113.
[180] Ibid., p. 145.
[181] Ibid., pp. 160-1.

the West owing to the subtraction of the communist areas and their economic transformation in ways that reduce their willingness and ability to complement the industrial economies of the West."[182]

One way of defending against "defection from within" is to ensure that Third World countries have the right kind of government. That can be done either by supporting authoritarian regimes, or what neoconservatives call "democracy." The key quality for Third World elites, in either case, is an orientation toward what Thomas Barnett calls "connectivity." The chief danger presented by "outlaw regimes," according to Barnett, lies in their being disconnected "from the globalizing world, from its rule sets, its norms, and all the ties that bind countries together in mutually assured dependence."[183]

The neoconservative version of democracy is more or less what Noam Chomsky means by "spectator democracy": a system in which the public engages in periodic legitimation rituals called "elections," choosing from a narrow range of candidates all representing the same elite. Having thus done its democratic duty, the public returns to bowling leagues and church socials, and other praiseworthy manifestations of "civil society," and leaves the mechanics of policy to its technocratic betters--who immediately proceed to take orders from the World Bank and IMF. This form of democracy is nearly synonymous with what neocons call "the Rule of Law," which entails a healthy dose of Weberian bureaucratic rationality. The stability and predictability associated with such "democracies" is, from the business standpoint, greatly preferable to the messiness of dictatorship or death squads.

American "pro-democratic" policy in the Third World, traditionally, has identified "democracy" with electoralism, and little else. In Central America, for example, a country is viewed as a "democracy" if its government "came to power through free and fair elections." But this policy ignores the vital dimension of popular participation, "including the free expression of opinions, day-to-day interaction between the government and the citizenry, the mobilization of interest groups," etc. The "underlying objective" of pro-democracy policies is "to maintain the basic order of what... are quite undemocratic societies." Democracy is a means of "relieving pressure for more radical change," but only through "limited, top-down forms of democratic change that [do] not risk upsetting the traditional structures of power with which the United States has been allied."[184] Democracy policy in El Salvador, more specifically, promoted a form of "democracy" through the Duarte regime that did not touch the power of the military or the landed elite.[185]

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[182] William Yandell Elliot, ed., *The Political Economy of American Foreign Policy* (Holt, Rinehart & Winston, 1955), p. 42.
[183] Thomas Barnett, "The Pentagon's New Map," *Esquire* March 2003 <http://www.thomaspmbarnett.com/published/pentagonsnewmap.htm>.
[184] Thomas Carothers, "The Reagan Years: The 1980s," in Abraham F. Lowenthal, ed., *Exporting Democracy* (Baltimore: Johns Hopkins, 1991), pp. 117-8.
[185] Ibid., pp. 96-7.

American elites prefer "democracy" whenever possible, but will resort to dictatorship in a pinch. The many, many cases in which the U.S. Assistance Program, the School of the Americas, the CIA, the World Bank and IMF, and others from the list of usual suspects have collaborated in just this expedient are recounted, in brutal detail, by William Blum in *Killing Hope*.[186]

Had anti-Sovietism or anti-communism been the U.S. government's main preoccupation, its policy would have been much different.

> While there were many varieties of capitalism consistent with the anti-Communist politics the United States... sought to advance, what was axiomatic in the American credo was that the form of capitalism it advocated for the world was to be integrated in such a way that *its* businessmen played an essential part in it. Time and again it was ready to sacrifice the most effective way of opposing Communism in order to advance its own national interests. In this vital sense its world role was not simply one of resisting the left but primarily of imposing its own domination....
>
> ....[I]t was its clash with nationalist elements, as diverse as they were, that revealed most about the U.S. global crusade, for had fear of Communism alone been the motivation of its behavior, the number of obstacles to its goals would have been immeasurably smaller.[187]

This postwar global system suffered a series of perceived challenges in the 1970s. The fall of Saigon, the increasing ability of the Soviet Union to act as spoiler against American intervention, the nonaligned movement, the New International Economic Order, etc., were taken as signs that the corporate world order was losing control.

Reagan's escalating intervention in Central America, the military buildup, and the partial resumption of Cold War were all responses to this perception. In addition, the collapse of the rival Soviet superpower, the Uruguay Round of GATT, NAFTA, and similar "free trade" [sic] agreements (particularly their draconian "intellectual property" provisions, symbiotically related to domestic counterparts like the Digital Millennium Copyright Act), together achieved a total end run against the perceived challenges of the 1970s. The neoliberal revolution of the '80s and '90s, coming as it did directly on the heels of diminished American power in the '70s, snatched total victory from the jaws of defeat; it ended all barriers to TNCs buying up entire economies, locked the west into monopoly control of modern technology, and created a "de facto world government" on behalf of global corporations. The '90s were the era of the G8, Davos, and Tom Friedman.

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[186] William Blum. *Killing Hope: U.S. Military and CIA Interventions Since World War II* (Monroe, Maine: Common Courage Press, 1995).
[187] Kolko, *Confronting the Third World*, pp. 117, 123.

The draconian "intellectual property" lockdown we've experienced since the 1980s is mind-boggling in its extent. The first brick in the wall was the intellectual property regime under the Uruguay Round of GATT. It went far beyond traditional patent law in suppressing innovation. One benefit of traditional patent law, at least, was that it required an invention under patent to be published. Under U.S. pressure, however, "trade secrets" were included in GATT. As a result, governments will be required to help suppress information not formally protected by patents.[188]

Patents are also being used on a global scale to lock the transnational corporations into a permanent monopoly of productive technology. The single most totalitarian provision of the Uruguay Round is probably the Trade-Related aspects of Intellectual Property rights (TRIPS) agreement of 1995. It has extended both the scope and duration of patents far beyond anything ever envisioned in original patent law. In England, patents were originally for fourteen years--the time needed to train two journeymen in succession (and by analogy, the time necessary to go into production and reap the initial profit for originality). By that standard, given the shorter training times required today, and the shorter lifespan of technology, the period of monopoly should be shorter. Instead, the U.S. seeks to extend them to fifty years.[189] According to Martin Khor Kok Peng, the U.S. is by far the most absolutist of the participants in the Uruguay Round. Unlike the European Community, and for biological processes for animal and plant protection.[190]

Another key escalation of international "intellectual property" law was the World Intellectual Property Organization (WIPO) Copyright Treaty of 1996. The Digital Millennium Copyright Act (DMCA), was passed in 1998 pursuant to the U.S. government's obligations under that treaty. The DMCA is a fundamental departure from traditional copyright doctrines, like fair use and first sale. The legislation does not only punish strictly defined copyright violations after the fact. It prohibits the production of any hardware features which can circumvent digital locks, even when the purchaser is simply attempting what would have been considered fair use under the old regime. For example, it is illegal to circumvent DRM to copy content one has purchased from one medium to another, for one's own convenience. Jon Johanssen, for example, was proscecuted for distributing DeCSS, which circumvents the content scrambling system on DVDs.[191] The Sonny Bono Copyright Term Extension Act of 1998 extended copyright to seventy years after the death of the author. Similar legal mandates against DRM circumvention were introduced in the EU by the EU Copyright Directive in 2001 and the EU Directive on the Enforcement of Intellectual Property Rights in 2004.[192]

Another radical innovation is the extension of patent law into areas traditionally

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188 Raghavan, *Recolonization*, p. 122.
189 Ibid., pp. 119-20.
190 Martin Khor Kok Peng, *The Uruguay Round and Third World Sovereignty* (Penang, Malaysia: Third World Network, 1990), p. 28.
191 Soderberg, *Hacking Capitalism*, p. 87.
192 Soderberg, *Hacking Capitalism*, p. 83.

covered by copyright. This is especially true of software. Copyright law only protects an actual work, not the general idea behind it. Patents, on the other hand, cover the idea itself. In the case of software, this means that rather than simply copyrighting the code itself, a software proprietor can charge competitors with patent violations for even attempting to write code to deal with the same problem. Software patents are a powerful weapon against open-source software, since it is a roadblock to open-source developers attempting to develop software to perform the same functions as existing proprietary software.[193]

Another prospective treaty in its planning stages in the WIPO is a Broadcasting Treaty which will give "cable networks, broadcasters, and, possibly, Internet portals, a fifty year monopoly over the material which they are transmitting."[194]

In addition, the Western consumer corporations that tend to thrive in the global economy are those in the sectors most heavily dependent on the international "intellectual property" regime: entertainment, software, and biotech.

[Susan Sell. Private Power, Public Law--The Globalization of Intellectual Property Rights (Cambridge: Cambridge University Press, 2003).
Michael Perelman. "The Political Economy of Intellectual Property" *Monthly Review* (January 2003).
Julian Dibbell. "We Pledge Allegiance to the Penguin" *Wired* (November 2004).]

The provisions for biotech are really a way of increasing trade barriers, and forcing consumers to subsidize the TNCs engaged in agribusiness. The U.S. seeks to apply patents to genetically-modified organisms, effectively pirating the work of generations of Third World breeders by isolating beneficial genes in traditional varieties and incorporating them in new GMOs--and maybe even enforcing patent rights against the traditional variety which was the source of the genetic material. For example Monsanto has attempted to use the presence of their DNA in a crop as prima facie evidence of pirating--when it is much more likely that their variety cross-pollinated and contaminated the farmer's crop against his will. The Pinkerton agency, by the way, plays a leading role in investigating such charges--that's right, the same folks who have been breaking strikes and kicking organizers down stairs for the past century. Even jack-booted thugs have to diversify to make it in the global economy.

The developed world has pushed particularly hard to protect industries relying on or producing "generic technologies," and to restrict diffusion of "dual use" technologies. The U. S.-Japanese trade agreement on semi-conductors, for example, is a "cartel-like, 'managed trade' agreement." So much for "free trade."[195]

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[193] Ibid., pp. 83-84.
[194] Ibid., p. 84.
[195] Dieter Ernst, *Technology, Economic Security and Latecomer Industrialization*, in Raghavan, *Recolonization*, pp. 39-40.

Patent law traditionally required a holder to work the invention in a country in order to receive patent protection. U.K. law allowed compulsory licensing after three years if an invention was not being worked, or being worked fully, and demand was being met "to a substantial extent" by importation; or where the export market was not being supplied because of the patentee's refusal to grant licenses on reasonable terms.[196]

The central motivation in the GATT intellectual property regime, however, is to permanently lock in the collective monopoly of advanced technology by TNCs, and prevent independent competition from ever arising in the Third World. It would, as Martin Khor Kok Peng writes, "effectively prevent the diffusion of technology to the Third World, and would tremendously increase monopoly royalties of the TNCs whilst curbing the potential development of Third World technology." Only one percent of patents worldwide are owned in the Third World. Of patents granted in the 1970s by Third World countries, 84% were foreign-owned. But fewer than 5% of foreign-owned patents were actually used in production. As we have already seen, the purpose of owning a patent is not necessarily to use it, but to prevent anyone else from using it.[197]

Raghavan summed up nicely the effect on the Third World:

> Given the vast outlays in R and D and investments, as well as the short life cycle of some of these products, the leading Industrial Nations are trying to prevent emergence of competition by controlling... the flows of technology to others. The Uruguay round is being sought to be used to create export monopolies for the products of Industrial Nations, and block or slow down the rise of competitive rivals, particularly in the newly industrializing Third World countries. At the same time the technologies of senescent industries of the north are sought to be exported to the South under conditions of assured rentier income.[198]

Corporate propagandists piously denounce anti-globalists as enemies of the Third World, seeking to use trade barriers to maintain an affluent Western lifestyle at the expense of the poor nations. The above measures--trade barriers--to permanently suppress Third World technology and keep the South as one big sweatshop, give the lie to this "humanitarian" concern. This is not a case of differing opinions, or of sincerely mistaken understanding of the facts. Setting aside false subtleties, what we see here is pure evil at work--Orwell's "boot stamping on a human face forever." If any architects of this policy believe it to be for general human well-being, it only shows the capacity of ideology to justify the oppressor to himself and enable him to sleep at night.

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[196] Raghavan, *Recolonizatinon*, pp. 120, 138
[197] Martin Khor Kok Peng, *The Uruguay Round and Third World Sovereignty*, pp. 29-30.
[198] Raghavan, *Recolonization*, p. 96.