

# Organized Crime

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The Unvarnished Truth About Government

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THOMAS J. DILORENZO

**MISES**  
INSTITUTE

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*To Laura  
and all of those like her  
who have enriched their lives  
by discovering the literature of liberty.*



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## INTRODUCTION

# Austrian Political Economy

**T**he late Milton Friedman once said that if the average tariff rate in America was a few percentage points lower than it would otherwise be thanks to influence of academic economists, that would more than justify all of their salaries and then some because of the wealth-enhancing effects of freer trade. Friedman was correct as far as the story goes, but at the time that he made the comment the “mainstream” of the economics profession was mostly involved in supporting the wealth-destroying efforts of the parasitic welfare/regulatory state by spinning myriad tales of “market failure” and recommending endless government intervention.

Market failure theorists, whose epicenter was for many years the Harvard and M.I.T. economics departments, had three main characteristics: First, they concocted mathematical models that were usually far removed if not totally detached from economic reality. Indeed, a realistic theory that could explain real-world phenomena was (and is) often viewed as pedestrian and unscholarly. Only impossible-to-understand and seemingly trivial mathematical manipulations were said to be worthy of “economic science.” The mainstream of the economics profession has long suffered from physics envy and has sought to model the unmodelable—human action—to make their “science” appear to be physics-like and scientific.

The second characteristic of the market failure theorists is a consistent application of what UCLA economist Harold Demsetz labeled “the nirvana fallacy.” The game is played as follows: First, construct a totally unrealistic theory of “perfect” competition that assumes away all real-world competition with assumptions of perfect information, homogenous products and prices, free or costless entry and exit from industry, and “many” firms. Second, compare real-world markets to this utopian Nirvana state and condemn the markets as “imperfect” or “failed.”

The third characteristic of market failure theories is to recommend intervention by presumably perfect government that is assumed to suffer from no failures and which will correct the failures of the market.

There are two schools of thought in the field of economics that never accepted this statist charade as being legitimate: the Austrian School and the Public Choice School. The Public Choice School—at least the “Virginia School” variant of it—uses the economist’s understanding of incentives to study the behavior of government and all of its appendages (voters, bureaucrats, politicians, interest groups, etc.). Understanding how government actually works in this way will cure anyone of the stupidity of simply assuming that government is capable of correcting perceived shortcomings of the market.

The Austrian School never accepted the foolish Nirvana fallacy approach to “economic modeling” for obvious reasons, namely, it is intellectually dishonest. Rather than condemning markets as being “imperfect” because market participants possess less than “perfect” information (as though anyone does), for example, Austrian economists will explore the ways in which market participants make use of the information that is available to them and acquire new information. The object is always to understand how the economic world works, not to provide what appears to be a “scholarly” defense of government interventionism, as is the case with the market failure theorists.

Austrian economists also study how government works and do not simply assume that it is some kind of benevolent and omniscient mechanism that serves as a corrector of market failure. Examples would be Ludwig von Mises’ book, *Bureaucracy*, or the numerous writings of Murray N. Rothbard on the machinations of governments throughout history. There are many more examples in the Austrian literature.

Your author considers this book to be a collection of essays in the tradition of *Austrian political economy*—a combination of applied economics and the study of governmental reality. Unlike “mainstream” economists

who are content to spin mathematical model after mathematical model which explain little or nothing about the real world, your author's focus has always been just the opposite—to use economic understanding to gain a better understanding of how the political-economic world works. Austrian economics is indispensable to succeed at this task.

The book is divided into six sections: “Coercion and Regulation” analyzes various aspects of government regulation of business; “Politics and Thieves” is of course about the inherent nature of government; “Centralization versus Liberty” discusses the never-ending quest by statist to monopolize and centralize political power so as to isolate themselves as much as possible from public influence; “Money and the State” describes the myriad evils of central banking, which was always thought of by its original proponents in America as an engine of corruption; “Workers and Unions” discusses various labor union myths and superstitions that too often cloud the public's thinking about the reality of labor markets; and “Truth and Lies about Markets” is a taxonomy of some of the main market-failure myths that have long been used to illegitimately advance the cause of economic interventionism, as well as some newer ones.

*Thomas J. DiLorenzo*  
*May 2012*



SECTION 1

# Coercion and Regulation



## CHAPTER 1

# Four Thousand Years of Price Control

Supply and demand have generally been allowed to work in energy markets, resulting in ups and downs in gasoline prices. Whenever gasoline prices go up to any significant degree, the industry is inevitably threatened by Congress with price controls, euphemistically referred to as “anti-price gouging legislation” or some other synonym.

The case against price controls—no matter how they are labeled by politicians—has been well known for hundreds of years. By artificially stimulating demand while taking some or all of the profitability out of supply, price controls inevitably create shortages. They also induce suppliers to skimp on quality, to the extent that they can, and often lead to bizarre government-imposed rationing schemes that only make things worse.

The case against price controls is not merely an academic exercise, however, restricted to economics textbooks. There is a four-thousand year historical record of economic catastrophe after catastrophe caused by price controls. The record is nicely documented in the book, *Forty Centuries of Wage and Price Controls* by Robert Schuettinger and Eamon Butler, first published in 1979.

The authors begin by quoting Jean-Philippe Levy, author of *The Economic Life of the Ancient World*, as noting that in Egypt during the third century B.C. “there was a real omnipresence of the state” in regulating grain

production and distribution. “[A]ll prices were fixed by fiat at all levels.” This “control took on frightening proportions as there was a whole army of inspectors.” Egyptian farmers became so infuriated with the price control police that many of them simply left their farms. By the end of the century “the Egyptian economy collapsed as did her political stability.”

In Babylon some four thousand years ago the Code of Hammurabi was in reality a maze of price control regulations. “If a man hire a field-labourer, he shall give him eight gur of corn per annum,” the state dictated. “If a man hire a herdsman, he shall give him six gur of corn per annum”; and “If a man hire a sixty-ton boat, he shall give a sixth part of a shekel of silver per diem for her hire.” And on and on. Such laws “smothered economic progress in the empire for many centuries,” as the historical record describes. Once these laws were abolished, “there was a remarkable change in the fortunes of the people” for the better.

Ancient Greece also imposed price controls on grain and established “an army of grain inspectors appointed for the purpose of setting the price of grain at a level the Athenian government thought to be just.” Greek price controls inevitably led to grain shortages, but ancient entrepreneurs saved thousands from starvation by evading these unjust laws with black markets. Despite the *imposition of the death penalty for evading the Greek price control laws*, the laws “were almost impossible to enforce.” The shortages created by the Greek price control laws created black market opportunities to the great benefit of the public.

In 284 A.D. the Roman emperor Diocletian created inflation by placing too much money in circulation, and then “fixed the maximum prices at which beef, grain, eggs, clothing and other articles could be sold, and prescribed the penalty of death for anyone who disposed of his wares at a higher figure.” The results, as Schuettinger and Butler explain, quoting an ancient historian, were that “the people brought provisions no more to markets, since they could not get a reasonable price for them and this increased the dearth so much, that at last after many had died by it, the law itself was set aside.”

Moving closer to modern times, George Washington’s revolutionary army nearly starved to death thanks to price controls on food that were imposed by Pennsylvania and other colonial governments. Pennsylvania specifically imposed price controls on “those commodities needed for the use by the army,” creating disastrous shortages of almost everything needed by the army. The Continental Congress wisely adopted an anti-price control resolution on June 4, 1778 that read:

Whereas it hath been found by experience that limitations upon the prices of commodities are not only ineffectual for the purpose proposed, but likewise productive of very evil consequences—resolved, that it be recommended to the several states to repeal or suspend all laws limiting, regulating or restraining the price of any Article.

And, write Scheuttinger and Butler, “By the fall of 1778 the army was fairly well provided for as a direct result of this change in policy.”

French politicians repeated the same mistakes after their revolution, putting into place the “Law of the Maximum” in 1793, which first imposed price controls on grain, and then on a long list of other items. Predictably, “in some [French] towns, the people were so badly fed that they were collapsing in the streets from lack of nourishment.” A delegation from various provinces wrote to the government in Paris that before the new price control law “our markets were supplied, but as soon as we fixed the price of wheat and rye we saw no more of those grains. The other kinds not subject to the maximum were the only ones brought in.” The French government was forced to abolish its disastrous price control law after it had literally killed thousands. When Robespierre was being carried through the streets of Paris on the way to his execution the crowd shouted, “There goes the dirty Maximum!”

At the end of World War II American central planners were apparently just as totalitarian-minded as the Nazis were when it came to economic policy. During the post-war occupation of Germany American planners rather liked the Nazi economic controls, including price controls, and so they were kept in place after the war ended. The notorious Nazi Hermann Goering even lectured the American war correspondent Henry Taylor about the stupidity of such a policy! As recounted by Schuettinger and Butler, Goering said:

Your America is doing many things in the economic field which we found out caused us so much trouble. You are trying to control peoples' wages and prices—peoples' work. If you do that you must control peoples' lives. And no country can do that part way. I tried and it failed. Nor can any country do it all the way either. I tried that too and it failed. You are no better planners than we. I should think your economists would read what happened here.

Price controls were finally ended in Germany by Economic Minister Ludwig Erhard in 1948, on a Sunday, when the American occupation authorities would be out of their offices and unable to stop him. This spawned

the “German economic miracle” which of course was no miracle but only a return to common sense by allowing markets and not politicians to set prices.

Price controls were the cause of the energy crisis in the U.S. in the 1970s and of the California energy crisis of the 1990s. For more than four thousand years, dictators, kings, despots, and politicians of every variety have viewed price controls as the ultimate “something for nothing” promise to the public. And for more than four thousand years the results have been the same: shortages, deterioration of product quality, the proliferation of black markets operated by criminals, bribery, destruction of a nation’s productive capacity, economic chaos, the creation of massive price control bureaucracies and police states, and a dangerous concentration of power in the hands of the price controllers.

## CHAPTER 2

# The Other War

**A** former MBA student of the author's who was the director of emergency medicine at a large urban hospital once said that he and his colleagues spent about 90 percent of their time treating the knife and gunshot wounds of drug gang members. His medical preparation for such a job included serving as a surgeon during wartime, which he said came in very handy. Such injuries dominate all such hospitals at tremendous expense. The incredible violence in America's cities is a direct result of the government's war on drugs and would end if the "war" was to end.

None of this should be surprising to anyone. In a free and legal market, any dispute between businesses, or buyers and sellers, can be settled through negotiation or, if need be, the courts. If a businessman believes he has been cheated or defrauded, then he can seek to have his property protected by the courts. He of course can also quit doing business with the suspect businessman, and urge everyone else he knows to do the same.

No such relatively civilized solution is available when government makes products or services illegal. A drug dealer cannot go to a judge and say, "Your Honor, I delivered one ton of cocaine to Mr. Smith here, and he refuses to pay me in full. I would like you to force him to live up to his end of our contract." Instead, drug dealers—like booze peddlers during Prohibition—resort to the only effective means available to enforce their business agreements: violence.

There is an even more ominous dynamic at work here, however. Once violence becomes the means by which one succeeds in illegal markets, the enormous profits earned in those markets will attract competition from those elements of society who have a comparative advantage in violence and brutality. The most violent will rise to the top.

Drug gangs are simply business partnerships, but unlike normal business partnerships in legal markets, they have great latitude in destroying their competitors by violent means. In legal markets, competitors can only be “destroyed” by producing better and/or cheaper products than theirs. In illegal markets competitors are often simply murdered. Murder is used to create “barriers to entry” into the business, to borrow a phrase from economics.

The police are often “silent partners” in this murder and mayhem since existing drug gangsters can easily pay off the police and become “informants” and alert the police of any new entrants into their business. That way the police do their dirty work for them by arresting their competitors.

In legal markets a brand name that is established by years of good performance and/or low prices is a valuable asset that fuels profits. In illegal markets, a brand name is established by especially brutal acts of violence. The ability of drug gangs to intimidate their rivals is the only “brand name” that counts in such a business.

Worse yet, there are economies of scale, so to speak, to such violent behavior. If a drug gang is especially notorious in say, Los Angeles, that fact will make it easier for it to enter and dominate the illicit drug markets in Chicago, New York, Miami, and other cities.

The use of violence to create extraordinary monopoly profits in the illicit drug markets has also lured thousands of children into the business. They work as “spotters” of police or “runners” who deliver the drugs to the drug gang’s customers. In most states children under the age of 18 are usually placed on probation for drug-related crimes, and in some states a jail term cannot extend past age 17. Facing little or no negative consequences for their participation in the illegal drug trade, these children grow up to be some of the most hardened and violent criminals in American society.

Ending the war on drugs would cause a dramatic, unprecedented drop in violence in American cities. The healthcare costs associated with the war on drugs would plummet as well, and hospitals would be able to devote more resources to other kinds of medical care, an especially valuable benefit now that the baby boom generation is approaching retirement age and will be making more and more intensive use of healthcare. The only losers would be the myriad government bureaucracies that are funded by the war on drugs, and of course the drug gangsters themselves.

## CHAPTER 3

# Who Will Regulate the Regulators?

**I**n government, failure is success. That's what I call DiLorenzo's First Law of Government. When the welfare state bureaucracy fails to reduce poverty, it is rewarded with more tax dollars and more responsibilities. When the government schools fail to educate children, they are rewarded with more tax dollars and more power to meddle in education. When NASA blows up a space shuttle, it is rewarded with a large budget increase (unlike a private airline which would probably go bankrupt). And when the Fed caused the worst depression since the Great Depression in 2007, it was rewarded with a vast expansion of its powers.

DiLorenzo's Second Law of Government is that politicians will rarely, if ever, assume responsibility for any of the problems that they cause with bad policies. No one group in society is more irresponsible than politicians. There are a few exceptions, but in general they will always blame capitalism for our economic problems even when capitalism is not even the economic system that we live under (economic fascism or crony capitalism would be more accurate). Nothing is more irresponsible than knowingly destroying what's left of our engine of economic growth with more and more governmental central planning, even if it is given the laughable name of "public interest regulation."

DiLorenzo's Third Law of Government is that, with few exceptions, politicians are habitual liars. The so-called "watchdog media" is

more appropriately labeled the “lapdog media,” for pointing out the lies of politicians is the best way to end one’s career as a journalist. Do this, and your sources of information will cut you off.

One of the biggest governmental lies is that financial markets are unregulated and in dire need of more central planning by government. *Laissez-faire* is said to have caused the “Great Recession.” Fed bureaucrats have lobbied for some kind of Super Regulatory Authority to supposedly remedy this problem. This is all a lie because according to one of the Fed’s own publications (“The Federal Reserve System: Purposes and Functions”), the Fed already has “supervisory and regulatory authority” over the following *partial* list of activities: bank holding companies, state-chartered banks, foreign branches of member banks, edge and agreement corporations, U.S. state-licensed bank branches, agencies and representative offices of foreign banks, nonbanking activities of foreign banks, national banks, savings banks, nonbank subsidiaries of bank holding companies, thrift holding companies, financial reporting procedures of banks, accounting policies of banks, business “continuity” in case of economic emergencies, consumer protection laws, securities dealings of banks, information technology used by banks, foreign investment by banks, foreign lending by banks, branch banking, bank mergers and acquisitions, who may own a bank, capital “adequacy standards,” extensions of credit for the purchase of securities, equal opportunity lending, mortgage disclosure information, reserve requirements, electronic funds transfers, interbank liabilities, Community Reinvestment Act sub-prime lending “demands,” all international banking operations, consumer leasing, privacy of consumer financial information, payments on demand deposits, “fair credit” reporting, transactions between member banks and their affiliates, truth in lending, and truth in savings.

In addition, the Fed also engages in legalized price fixing of interest rates and creates price inflation and boom-and-bust cycles with its “open market operations.” In addition, financial markets are just as heavily regulated by the Securities and Exchange Commission, Comptroller of the Currency, Office of Thrift Supervision, and dozens of state government regulatory agencies. All of this is the Washington, D.C. definition of “*laissez-faire*” in financial markets.

DiLorenzo’s Fourth Law of Government is that politicians will only take the advice of their legions of academic advisors if the advice promises to increase the state’s power, wealth, and influence even if the politicians know that the advice is bad for the rest of society. The academics happily

play along with this corrupt game because it also increases their notoriety and wealth. A glaring example of this phenomenon is the fact that, in the aftermath of the onset of the “Great Recession” there was almost no discussion at all by government officials, the media, or op-ed writers about the vast literature of economics that documents the gross failures of government regulation over the past century to promote “the public interest.”

There has always been some kind of government regulation of economic activity in America, but the federal regulatory state got its first big boost with an 1877 Supreme Court case known as *Munn v. Illinois*. The two Munn brothers owned a grain storage business and the powerful farm lobby in their state wanted to essentially steal their property by having the state legislature impose price ceilings on grain storage. Such laws had previously been ruled unconstitutional as a violation of the Contract Clause of the U.S. Constitution. But the plunder-seeking farmers prevailed, and it was hailed by statist everywhere as a victory for “the public interest.” Thus, the very first major example of “public interest regulation” was unequivocally an act of legal plunder that benefited a very narrow special interest at the expense of the public, which would have benefited more from a free market.

Either because of ignorance or corruption (or both), the statist academics of the time sang the “public interest” tune with regards to regulation, creating the myth that markets always “fail” and that the remedy is benevolent and wise government regulation in the public interest. The academics did this despite the fact that there was glaring evidence all around them that regulation was always and everywhere a special-interest phenomenon, as indeed almost all governmental activity is.

As historian Gabriel Kolko wrote in his 1963 book, *The Triumph of Conservatism*, big business in the early twentieth century sought government regulation because the regulation “was invariably controlled by leaders of the regulated industry, and directed toward ends they deemed acceptable or desirable.” Government regulation has generally served to further the very economic interests that are being regulated. Chicago School economists labeled this phenomenon the “capture theory of regulation.”

Most academic economists, seduced by the prestige, employment, and money that came from being governmental advisors, ignored all of this reality and instead spent roughly fifty years—from the pre-World War I years to the 1960s—inventing myriad factually empty *theories* of “market failure.” A popular book at the time was entitled *Anatomy of Market Failure*, by Francis Bator. This literature was (and is) based on the fraudulent

technique of comparing real-world markets to an unobtainable, theoretical, utopian ideal (“perfect competition”) and then condemning the real world for being “imperfect,” all the while *assuming* that the politics of government regulation would perfectly “correct” these imperfections. Economist Harold Demsetz labeled this charade “the Nirvana Fallacy.” Comparing real-world markets to “Nirvana” will always cause one to conclude that markets are “imperfect” by comparison. The market failure theorists never once compared government to Nirvana to subject interventionism to the same criteria. The Austrian School of economics is the only school of thought within the economics profession that never participated in this farce.

To its credit, the Chicago School of economics joined with the Austrians in exposing many of the market failure/regulation-is-always-good fallacies. Hundreds of journal articles and books were published that rediscovered the old truth that “as a rule, regulation is acquired by the industry and is designed and operated primarily for its benefit,” as Nobel laureate George Stigler wrote in 1971.

This kind of research was expanded over the years to show that large corporations often support and lobby for onerous government “safety” and environmental regulations because they understand that the regulations will be so costly to enforce that they will likely bankrupt their smaller competitors while deterring others from entering the market in the first place. Businesses long ago discovered that the only way to have a long-lasting cartel is to have the cartel agreement enforced by the government. Privately-enforced cartels always break down because of cheating by the cartel members. The railroad and trucking industries were cartelized by the federal Interstate Commerce Commission (ICC) for many decades, for example. The ICC set monopolistic prices in these industries and prohibited genuine competition. The Civil Aeronautics Board (CAB) cartelized the airline industry by prohibiting price competition until it was deregulated in the late 1970s. There was vigorous competition in the electric power industry in the U.S. until it was ended by government regulation in the early twentieth century by the creation of monopoly franchises by state and local governments. AT&T enjoyed a government-sanctioned monopoly for many decades as well.

During the period of history when government-sanctioned monopoly was increasingly the norm, the Fed was created to facilitate the creation of a banking industry cartel. As Murray Rothbard wrote in *A History of Money and Banking in the United States*,

the financial elites of this country . . . were responsible for putting through the Federal Reserve System, as a governmentally created and sanctioned cartel device to enable the nation's banks to inflate the money supply . . . without suffering quick retribution from depositors or note holders demanding cash.

In other words, giving the Fed more regulatory authority is not unlike giving an alcoholic another bottle of whisky, a murderer another gun, or a bank robber a ski mask. It is bound to make things worse, not better.

## CHAPTER 4

# Regulation and the Stock Market

**T**he Dow Jones Industrial Average would be several thousand points higher than it is were it not for government regulation that causes businesses to divert immeasurable time and resources to pandering to government regulators rather than pursuing profits by creating new products, improving existing products and services, and cutting costs and prices. Since expected future profitability is the major ingredient in stock pricing, regulation destroys stock values.

Government regulation has transformed American corporations from entrepreneurial enterprises to sluggish bureaucratic behemoths. As Ludwig von Mises wrote in *Liberalism*:

The bureaucratization of privately owned enterprises that we see going on about us everywhere today is purely the result of interventionism, which forces them to take into account factors that, if they were free to determine their policies for themselves, would be far from playing any role whatsoever in the conduct of their business. When a concern must pay heed to the political prejudices and sensibilities of all kinds in order to avoid being continually harassed by various organs of the state, it soon finds that it is no longer in a position to base its calculations on the solid ground of profit and loss.

Mises wrote that passage in 1962 when government was miniscule compared to today's omnipotent, Leviathan state. With their blizzard of regulations the courts and regulatory agencies have eviscerated three of the most important ingredients of capitalism: private property, freedom of contract, and freedom of association. Genuinely private property rights barely exist in the business world any more thanks to regulatory controls that affect every business in America.

The volume of government regulation of business is mind numbing. Each year the Competitive Enterprise Institute in Washington, D.C. publishes *Ten Thousand Commandments* (edited by Clyde Wayne Crews, Jr.), an accounting of the scope of federal regulation. The 2011 edition of the publication showed that the monetary cost to businesses of complying with federal regulations was estimated at \$1.752 trillion, an amount equivalent to 50 percent of the entire federal budget for that year. This amount exceeds all corporate pre-tax profits and is nearly double the amount of income tax revenue collected in that year. There are more than 80,000 pages of small-print regulations listed in *The Federal Register*, with no fewer than 58 federal regulatory agencies working diligently to add thousands more each year. Thousands of additional pages of regulations are enforced by state and local governments.

Obviously, American corporations must spend inordinate amounts of time, in addition to billions or trillions of dollars, complying with government paperwork, rules, and regulations instead of concentrating on making better and cheaper products. Profits are reduced, jobs are destroyed or never materialize in the first place, and stock prices are stifled. The instability of property rights caused by pervasive regulatory edicts leads investors to be much less certain about the value of the contracts they enter into, since rules and regulations are constantly changing, and sometimes seem to come out of nowhere.

As a rule, most government regulation produces very little, if any benefit to the consumers in whose names they are promulgated. That was the conclusion of Nobel laureate Ronald Coase, who as a University of Chicago law professor edited the prestigious *Journal of Law and Economics* for many years at a time when that journal published hundreds of scholarly studies of the effects of regulation. After editing and publishing hundreds of such studies Professor Coase (in J.F. Weston's, *Large Corporations in a Changing Society*) concluded that:

There have been more serious studies made of government regulation of industry in the last fifteen years or so, particularly in

the United States, than in the whole preceding period. These studies have been both quantitative and nonquantitative . . . the main lesson to be drawn from these studies is clear: they all tend to suggest that the regulation is either ineffective or that when it has a noticeable impact, on balance the effect is bad, so that consumers obtain a worse product or a higher-priced product or both as a result of regulation. Indeed, this result is found so uniformly as to create a puzzle: one would expect to find, in all these studies, at least some government programs that do more good than harm.

Universities with schools of business rarely teach anything about entrepreneurship in particular or the virtues of free-market capitalism in general, but offer numerous courses in “business law,” “administrative law,” “business ethics,” and “corporate social responsibility.” All of these courses focus on teaching students how to become good corporate bureaucrats who ignore profit making by pandering to the myriad agents of the state instead. Even accounting is taught according to the dictates of the Securities and Exchange Commission. Because of the stranglehold that government regulators have over every business more and more top business executives have backgrounds as lawyers, lobbyists, or publicists, the tools of governmental manipulation, as opposed to manufacturing and engineering.

Regulation has also all but destroyed free speech in the business world. Very few business people will speak out against government regulation out of fear of regulatory retribution, a tax audit, and other forms of harassment by the government. Many American corporations are so intimidated by the regulatory state that they give away billions of dollars to political activist groups that lobby for even more regulation and interventionism. The Capitol Research Center in Washington, D.C., estimated that for every philanthropic dollar that large American corporations give to pro free enterprise organizations like the Mises Institute they donate three dollars to anti free enterprise organizations. Some of them apparently believe that they are “buying” the good graces of regulators, but they are in reality giving away the “rope” with which the state will “hang” them economically. Others are simply victims of extortion by left-wing activist groups.

The federal bureaucracy is utterly incapable of managing its own budget let alone the budgetary decisions of thousands of private businesses. Government enterprises are notorious for being lazy, slothful, inefficient,

and corrupt. The very notion that they should be in charge of business decision making on the part of thousands of private businesses is a farce that is destroying capitalism in America.

## CHAPTER 5

# Our Totalitarian Regulatory Bureaucracy

In chapter 5 of F.A. Hayek's 1944 classic, *The Road to Serfdom*, the Nobel laureate warned that the state need not directly control all or even most of the means of production to exert totalitarian control over the economic life of a nation. He cited the example of Germany where, as of 1928, "the central and local authorities directly control 53 percent" of the German economy. In addition to this, wrote Hayek, private industry in Germany was so heavily regulated that the state *indirectly* controlled "almost the whole economic life of the nation." It was through such totalitarian controls that Germany traveled down "the road to serfdom." As Hayek further stated, "there is, then scarcely an individual end which is not dependent for its achievement on the action of the state, and the 'social scale of values' which guides the state's action must embrace practically all individual ends." In other words, government regulation was so pervasive that the pursuit of profit, driven by consumer preferences, was mostly replaced by the whims of regulatory bureaucrats.

It may sound shocking to some, but modern-day America compares favorably to the fascist Germany of the 1930s with regard to the degree to which the state interferes with and controls economic activity. First of all, government expenditures at all levels of government account for about 40 percent of national income. It differs by a few percentage points year by

year, but it has been in the 40 percent range in recent years. This doesn't count all of the off-budget government agencies that exist at the federal, state, and local levels of government, as James Bennett and I discussed in our book, *Underground Government: The Off-Budget Public Sector*. If this is included, government expenditures as a percentage of national income would be at least 45–50 percent, which is not so far from the 53 percent in Nazi Germany that Hayek alluded to.

As for regulation, there are nine cabinet-level departments at the federal level that regulate, control, and regiment housing, transportation, healthcare, education, energy, mining, agriculture, labor, and commerce in general. On top of dozens of federal regulatory agencies the state governments also supply a mountain of regulation. The state of Alabama's Web site, for instance, lists regulatory agencies and commissions that regulate: retirement, geology, public health, education, conservation, natural resources, industrial relations, agriculture, senior citizens, tourism, travel, veterans, environmental management, forensic science, business development, rehabilitation, banking, insurance, labor, transportation, youth services, children's affairs, film making, ports, disabilities, arts, real estate, oil and gas, forests, ethics, surface mining, alcoholic beverages, auctioneers, and "faith-based initiatives." And Alabama is a relatively conservative state; most other states probably have much longer lists of regulatory functions.

Because of the inevitable failures of all governmental planning in a democracy, Hayek wrote that "the conviction [will grow] that if efficient planning is to be done, the direction must be 'taken out of politics' and placed in the hands of experts—permanent officials or independent autonomous bodies." Moreover, the "cry for an economic dictator is a characteristic stage in the movement toward [central] planning of an entire economy. This indeed describes many of the above-mentioned regulatory functions but is especially descriptive of the central planning "czars" who now populate the executive branch of the federal government. As of 2010 these included political appointees who are given "czar" status for the following categories: Afghanistan, AIDS, auto recovery, borders, California water, cars, Middle East, Persian Gulf, Pakistan, South Asia, climate, domestic violence, drugs, economics, energy, environment, faith-based initiatives, government performance, Great Lakes, green jobs, Guantanamo base closure, health, information, intelligence, science, stimulus legislation, pay, regulation, Sudan, TARP, technology, terrorism, urban affairs, weapons, weapons of mass destruction, war, oil, manufacturing, cybersecurity, safe schools, and Iran.

It would be very difficult indeed to argue against the proposition that the U.S. economy today is even more heavily controlled, regulated and regimented by the state than Nazi Germany was at the time Hayek was writing *The Road to Serfdom*. Americans have traveled many miles down the road to serfdom by deluding themselves that the god of democracy will somehow save them from statist slavery. As Hayek warned, “there is no justification for the belief that, so long as power is conferred by democratic procedure, it cannot be arbitrary . . .”

## CHAPTER 6

# Antitrust, Anti-Truth

**W**hen the U.S. government prosecuted the Microsoft Corporation during the 1990s (after a decade of “investigations” that turned up nothing illegal) the head of the U.S. Justice Department’s Antitrust Division, Joel Klein, rationalized the lawsuit by saying that it was in keeping with the long history of consumer protection regulation in America, beginning with the Sherman Antitrust Act of 1890. In reality, the history of antitrust regulation has been a history of politically-inspired witch hunts launched against America’s most innovative and entrepreneurial businesses, usually instigated by their sour-grapes competitors.

In the June 1985 issue of the peer-reviewed *International Review of Law and Economics* I showed that the industries accused of “monopolization” by Senator John Sherman and his colleagues were expanding production four times faster than the economy as a whole, on average (some as much as ten times faster) for the decade prior to the 1890 Sherman Act. They were also dropping their prices faster than the price level was dropping during this ten-year period of price deflation. The “trusts” were subjected to political attack precisely because they had been making products cheaper and cheaper, much to the dismay of their less efficient but politically-connected rivals. Antitrust was a protectionist racket from the very beginning.

The judge in the Microsoft antitrust case, one Thomas Penfield Jackson, was so biased that he was thrown off the case (i.e., fired) by the panel of three federal judges who had appointed him. One example of his bias was a magazine interview in which he compared Microsoft founder Bill Gates to John D. Rockefeller (and to Al Capone). Judge Jackson was way off base when he compared Gates to Capone, but not so much when he compared him to Rockefeller. As Dominick Armentano demonstrated in his book, *Antitrust and Monopoly: Anatomy of a Policy Failure*, Rockefeller's Standard Oil Company caused the price of refined petroleum to fall from over 30 cents/gallon in 1869 to 5.9 cents in 1897 while creating myriad new products and stimulating innovation in the entire industry. For this, Rockefeller was prosecuted and forced to break up his company despite the fact that he had more than 300 competitors when he supposedly "monopolized" the oil industry.

In his classic, *Antitrust and Monopoly*, Dominick Armentano carefully examined fifty-five of the most famous antitrust cases in U.S. history and concluded that in every single case the accused firms were *dropping* prices, *expanding* production, innovating, creating new products, and generally *benefiting consumers*. It was not consumers who were being harmed, but the less-efficient, sour-grape competitors of these companies. For example, the American Tobacco Company was found guilty of "monopolization" in 1911 even though the price of cigarettes (per thousand) had declined from \$2.77 in 1895 to \$2.20 in 1907, all despite a 40 percent increase in raw material costs to the company.

In what is perhaps the best example of nonsensical double-talk in antitrust history, in 1944 Judge Learned Hand found Alcoa guilty of "monopolizing" the virgin ingot aluminum market by employing "superior skill and foresight" which the judge said "forestalled" competition by those businesses with less skill and foresight. He condemned Alcoa for being extremely adept at correctly anticipating market demand for its product and then supplying that demand, to the "exclusion" of higher-priced competitors.

Alcoa "embraced every new opportunity" with a "great" organization, intoned Judge Hand, and it staffed the organization with "elite business personnel." This "sin" must be published, he said.

In 1962 the government prohibited the Brown Shoe Company, which had 1 percent of the shoe market, from acquiring Kinney Shoes, which also had a whopping 1 percent market share at the time. A company with 2

percent of the market supposedly threatened competition in the industry, the government ludicrously claimed.

In 1969 IBM had a 65 percent market share in the computer market and was sued by the federal government for allegedly monopolizing the computer industry. IBM was mired in a court battle for thirteen years before the government finally gave up on the case. In the meantime, the company was eclipsed in the marketplace by Intel, Microsoft, and other companies. This governmental assault on IBM undeniably weakened the company.

In 1962 the government forced the Schwinn Bicycle Company to divorce itself from its network of dealers. Foreign competition then drove Schwinn into bankruptcy.

General Motors was never prosecuted for violating the anti-monopoly laws, but the company's fear of antitrust drove it to adopt a policy from 1937 to 1956 of never allowing its market share among the "Big Three" automakers to exceed 45 percent. This contributed to the company's competitive downfall at the hands of foreign automakers, especially ones from Japan.

RCA was prohibited by antitrust regulators from charging royalties to American licensees, so the company licensed its products to Japanese companies instead. This led directly to the overwhelming dominance of the Japanese electronics industry in the American marketplace.

Antitrust regulation killed Pan American World Airways by forbidding it from acquiring domestic routes. Without these "feeder" routes for its international flights, the company went bankrupt.

Monopoly is impossible in a free market. Government is the real source of monopoly with its monopoly franchises, protectionist tariffs, licensing laws, "certificates of need," and other monopolistic regulatory gimmicks like antitrust regulation.

## CHAPTER 7

# Antitrust Luddites

**T**he “Luddites” were early nineteenth century British textile workers who protested the introduction of mechanized looms by destroying them and issuing proclamations denouncing the new technology in the name of the mythical King Ludd of Sherwood Forest. What the Luddites failed to understand—and what today’s neo-Luddites fail to understand—is that “labor-saving technology” that reduces production costs and prices increase consumer demand for the product being produced, which in turn generates *more* jobs in the industry, not less.

In 2011 neo-Luddism was on display when the Obama administration blocked a proposed merger between AT&T and T-Mobile USA. According to the *New York Times* on August 31, 2011, stopping the merger would supposedly “help save jobs of American workers.” “The view that [the Obama] administration has is that through innovation and through competition, we create jobs,” Deputy Attorney General for Antitrust James M. Cole was quoted as saying. Mergers usually reduce job creation “through the elimination of redundancies,” said Cole. “So we see this as a move that will help protect jobs in the economy,” he added. The formula for job creation in the American economy, according to the Obama administration, was the protection and expansion, if need be, of cost-increasing “redundancies.” American industries’ foreign competitors must have been cheering on the Obama administration.

In reality, as opposed to the Obama administration's "economic analysis," the reduction of "redundancies" in business is another way of saying "cutting costs to become more competitive in international markets." When a company succeeds in becoming more competitive in this way its market share expands and *more jobs are created in that company*.

It is true that "innovation" can create jobs. What the Obama administration didn't understand is that a merger like the AT&T/T-Mobile alliance is an innovation. It was a proposed innovative way to reduce the cost of providing cell phone services. Constant innovation is a necessity in an industry as hyper-competitive as the cell phone industry.

The Obama administration's position on the proposed merger was a combination of Luddism and mercantilism. The mercantilists of the eighteenth century believed in the superstition that wealth was created not by production but by the hoarding of gold. The Obama mercantilists apparently believed that existing jobs, not gold, must be hoarded. They failed to recognize that the economy is dynamic, with jobs constantly being created and destroyed as new-and-improved industries and business practices replace the older and less efficient ones (efficient in serving consumers, that is).

As usual in antitrust cases, the Obama administration defended its blocking of the merger by arguing that the merger would somehow reduce competition. But how, exactly, could that happen? At the time there were more than 180 cell-phone companies in the U.S, with hundreds more around the world posing as potential competitors in the U.S. market. AT&T and T-Mobile would never have been able to raise prices at all, let alone raise them to monopolistic levels, with hundreds of competitors waiting in the wings to take advantage of their foolish pricing decision.

The obvious objective of the proposed merger was to reduce prices in order to make more profit. This is not to say that they would have succeeded in doing so, for there is no such thing as a sure thing in business. What is certain, however, is that the blocking of the proposed merger by the Obama administration prohibited these two companies from trying to become more competitive and even bigger job generators than they already were.

## CHAPTER 8

# Socialized Healthcare vs. the Laws of Economics

**A**t the heart of the U.S. government's continued takeover of the healthcare sector of the economy was a law passed during the Obama administration that would eventually drive the private health insurance industry out of business or transform it into a *de facto* nationalized industry. The law imposed additional taxes and other costs on health insurance companies while creating a government health "insurance" bureaucracy to ostensibly "compete" with private companies. This is all part of a long-term plan to finally achieve the socialist pipe dream of socialized medicine in America, socialism having performed so wonderfully in so many other countries. Like all government monopolies, this one would operate with all the compassion of the IRS and the efficiency of the post office.

Some years ago the Nobel laureate economist Milton Friedman studied the economic history of healthcare supply in America. In a 1992 study published by the Hoover Institution entitled "Input and Output in Health Care," Friedman noted that 56 percent of all hospitals in America were privately owned and operated as for-profit enterprises in 1910. Then after decades of subsidies for government-run hospitals, the number had fallen to 10 percent. It took decades, but by the early 1990s government had taken over almost the entire hospital industry. The tiny portion of the industry that remains private and for-profit is regulated so heavily that it might as

well be considered as an appendage of the state as well. The overwhelming majority of decisions made by “private” hospital administrators have to do with complying with government’s bureaucratic edicts, not patient care *per se*.

Friedman’s key conclusion was that, as will all bureaucratic systems, government-owned or government-controlled healthcare created a situation whereby increased “inputs” such as expenditures on equipment, infrastructure, and the salaries of medical professionals, actually led to *decreased* “output” in terms of the quantity and quality of medical care. For example, while medical expenditures rose by 224 percent from 1965 to 1989, the number of hospital beds per 1,000 population *fell* by 44 percent and the number of beds occupied declined by 15 percent. During the 1945–1989 period that Friedman studied, costs per patient-day also rose almost twenty-four-fold even after price inflation was taken into account. Increased government domination of hospital care resulted in less service while fueling astronomical cost increases.

This kind of result is present in all government-run bureaucracies because of the absence there of any kind of market feedback mechanism. Since there are no profits in an accounting sense in government, there is no reliable mechanism for rewarding good performance and penalizing poor performance. In fact, in all government enterprises exactly the opposite is true: poor performance is typically *rewarded* with larger budgets after promises are made to “do better” with more money.

Costs always explode in any industry whenever government gets involved. In 1970 the government forecast that the hospital insurance (HI) portion of Medicare would be “only” \$2.9 billion annually. Since the actual expenditures were \$5.3 billion, this was a 79 percent underestimate of cost. In 1980 the government forecast \$5.5 billion in HI expenditures; actual expenditures were more than four times that amount—\$25.6 billion. Yet government always promises cost *reductions* whenever it begins to take over any industry.

In response to the cost explosion that its own policies caused, government then granted itself even more extraordinary powers over the healthcare industry by enacting twenty-three new taxes in the first thirty years of Medicare (see Ronald Hamoway, “The Genesis and Development of Medicare,” in Roger D. Feldman, ed. *American Health Care*).

All government healthcare monopolies, whether they are in Canada, Great Britain, or Cuba, experience an explosion of both cost and demand, the latter since healthcare is “free” under such a system. (Of course it is not

“free”; the costs are simply buried in general tax bills). Whenever anything has a zero explicit price associated with it consumer demand will increase dramatically and healthcare is no exception. At the same time, routine bureaucratic bungling will guarantee gross inefficiencies that will fester and get worse and worse every year. As costs get out of control and begin to embarrass those who falsely promised cost *reductions*, the politicians can be expected to do what politicians always do in such situations and impose price ceilings on the industry, usually disguised by some kind of slick euphemism like “global budget controls.”

Price ceilings always stimulate demand while reducing supply, thereby creating shortages. Non-price rationing becomes necessary. This means that government bureaucrats, not individuals and their doctors, inevitably determine who will get medical treatment and who will not, what kind of medical technology will be available, how many doctors and nurses there will be coming out of medical and nursing schools, and so forth. They assume totalitarian control over the industry, in other words.

All countries that have adopted socialized healthcare have suffered from the disease of price control-induced shortages of care. If a Canadian, for instance, suffers third-degree burns in an automobile crash and is in need of reconstructive plastic surgery, the average waiting time for treatment is nearly five months. The waiting time for orthopedic surgery is also almost five months; for neurosurgery it is three months; and it is even more than a month for heart surgery (see The Fraser Institute publication by Baccus Barua, Mark Rovere, and Brett J. Skinner, *Waiting Your Turn: Hospital Waiting Lists in Canada, 2011 Report*). This of course is why so many of the more affluent Canadians in need of emergency care have flooded American hospitals for so many years.

A January 16, 2000 *New York Times* article entitled “Full Hospitals Make Canadians Wait and Look South,” by James Brooke, provided many examples of how Canada’s nationalized healthcare system has created serious, life-threatening shortages. For example, a fifty-eight-year-old grandmother awaited open-heart surgery in a Montreal hospital hallway with sixty-six other patients as electric doors opened and closed all night long, bringing in freezing drafts from sub-zero weather. She was on a *five-year waiting list* for her heart surgery at the time.

In Toronto, twenty-three of the city’s twenty-five hospitals turned away ambulances in a single day because of a shortage of doctors. In Vancouver, ambulances were at one time “stacked up” for hours in the parking lot while heart attack victims waited in them before being treated. At least

one-thousand Canadian doctors and many thousands of Canadian nurses have left for the U.S. to avoid price controls on their salaries. “Few Canadians would recommend their system as a model for export,” wrote James Brooke in the *New York Times*.

Canadian price control-induced shortages also manifest themselves in scarce access to medical technology. Per capita, the United States has eight times more MRI machines, seven times more radiation therapy units for cancer treatment, six times more lithotripsy units, and three times more open-heart surgery units. There are more MRI scanners in Washington state, with a population of around five million, than in all of Canada with a population of more than thirty million (see John Goodman and Gerald Musgrave, *Patient Power: Solving America’s Health Care Crisis*). This will be America’s future if it continues down the road of socialized medicine.



SECTION 2

# Politics and Thieves



## CHAPTER 9

# Pay to Play: Why the Fuss?

**I**n 2009 the Washington establishment and the national media feigned outrage over the fact that Governor Rod Blagojevich of Illinois had been selling political favors. The governor had apparently been taking “bids” for Barack Obama’s vacated U.S. Senate seat since he, as governor, was entitled to appoint Obama’s replacement. Federal prosecutor Patrick Fitzgerald provided perhaps the biggest laugh line when he claimed that Abraham Lincoln would roll over in his grave if he learned that a Chicago politician had been engaged in such shady behavior.

In reality, Lincoln would be rolling his eyes over the stupidity of such a statement. As Pulitzer prize-winning Lincoln biographer David Donald once noted, Lincoln had become the master political string puller in Illinois by the time he ran for president. As a young man Lincoln said that his main aspiration was to become “the DeWitt Clinton of Illinois,” referring to the former New York governor who is credited with inventing and perfecting the “spoils system” of institutionalized political corruption.

As president one of Lincoln’s very first acts was to put Congress into a special session in June of 1861 to begin work on the Pacific Railway bill, which would eventually result in the greatest spectacle of political graft and corruption in American history up to that point (the Credit Mobilier scandal). Lincoln benefited personally from this legislation which gave him, as president, the right to choose the eastern starting point of the government-subsidized transcontinental railroad. He chose Council Bluffs, Iowa, where

he had purchased a large parcel of land in 1857. Many of Lincoln's fellow Republican luminaries, from Thaddeus Stevens to Justin Morrill and Oakes Ames, and even General Sherman, accumulated fortunes as a result of the Pacific Railroad legislation.

The selling of political favors—including appointments to government offices—is what defines Washington politics (and all other politics in America). With the lone exception of Congressman Ron Paul in recent decades, virtually every Washington politician spends most of his time selling political favors of one kind or another. Legislation and regulation is “sold” for campaign “contributions, kickbacks, high-paying jobs for relatives and friends, promises of private-sector jobs and monetary favors, etc. It’s what politicians do and what politics is about. Governor Blagojevich was just doing a politician’s typical dishonest day’s work.

Government has become so adept at selling political favors that scholarly treatises have been written about a veritable science of political extortion. A case in point would be the book, *Money for Nothing: Politicians, Rent Extraction, and Political Extortion*, by Fred S. McChesney. Much has been written about governmental grants of favors to businesses and other groups in return for “campaign contributions,” but McChesney focuses on an even more insidious phenomenon: politicians threatening to impose menacing costs on businesses or entire industries with regulation and taxation unless the businesses and industries pay up and “contribute” to their campaigns. He calls it “a form of political extortion or blackmail.”

Political extortion or blackmail may take the form of threats to impose price controls, for example, or threats to withdraw occupational licenses, corporate charters, or building permits. Or, it can come in the form of threats to raise the cost of doing business through a special excise tax or an especially onerous and costly regulation. The purpose of the threats is to solicit campaign “contributions” from the threatened businesses. Politicians even have their own language of political extortion and blackmail. They call such legislation “milker bills,” since they “milk” campaign contributions from businesses that the politicians call “cash cows.”

There are also “juicer bills” that are designed to “squeeze” cash out of threatened businesses. And there are “fetcher bills” that are designed for the same purpose—to “fetch” cash from corporate lobbyists with threatening legislation. Among the examples cited by Professor McChesney are:

- Product liability legislation that is proposed periodically to fetch campaign cash from both sides of the debate.

- Proposed legislation to restrict futures trading that fetches loads of cash from futures traders.
- Proposed price controls on pharmaceuticals, which squeezed millions from the pharmaceutical industry.
- Proposed price controls on cable television which had the same effect.
- Proposals to ban smoking altogether, or to impose even more extreme taxes on tobacco products, always fetches millions from the tobacco companies.
- Proposals to increase excise taxes on alcoholic beverages are tried and true juicer bills.
- Proposals to “tax the wealthy” more heavily and “make them pay their fair share” are classic examples of fetcher legislation.

In each instance, once a “sufficient” amount of cash has been extracted from the threatened individuals, corporations, or groups, the menacing legislation is dropped. It is no different, in other words, from the practice of underworld thugs who demand bribes in return for allowing a business to exist in “their” neighborhood. Governor Blagojevich, who was eventually sentenced to fourteen years in prison, was a sacrificial political lamb who was used by the Chicago political machine that, in 2009, had migrated into the White House. Their apparent purpose in going after Blagojevich for doing what they themselves had done all of their political careers was to try to dupe the public into believing that Chicago politicians are not really the gang of thieves and crooks that so many people think they are.

## CHAPTER 10

# Fed-ACORN Criminality

Several years ago the Association of Community Organizations for Reform Now (ACORN), the left-wing activist group that Barack Obama was employed by after leaving law school, was in the news after one of its “tax counselors” was videotaped giving advice on tax evasion to two people posing as a pimp and a prostitute. The imposters told the “counselor” that they wanted a government-subsidized loan to open a brothel where they would house dozens of teenage girls they would bring into the country illegally from Central America. On the videotape the “counselors” happily advised them on how to go about applying for the government loan without the legal authorities finding out about what they were really up to.

As sleazy as this story was, it pales by comparison to ACORN’s primary function over the past thirty years to so. ACORN has been a major player in what can be described as a legalized extortion racket administered by the Federal Reserve Board, the Comptroller of the Currency, and other government agencies. The racket started with President Jimmy Carter’s 1977 Community Reinvestment Act (CRA), which empowered “community groups” like ACORN to effectively extort billions of dollars from banks. Such groups are empowered by the CRA to “protest” proposed bank expansions or mergers. They file a protest with the Fed, while demanding that the bank that is proposing to merger or expand give it—ACORN—

millions of dollars, to supposedly be lent by ACORN to sub-prime borrowers. ACORN always keeps a hefty portion of the money for its own salaries and expenses, of course. WaMu Bank, which went bankrupt, once boasted of having made \$375 billion in CRA loans, and the Fed gave Countrywide Bank an award after it made \$600 billion in such loans before it, too, went bankrupt during the sub-prime mortgage meltdown of 2008–09.

Much of the money that ACORN and other similar, left-wing “community groups” receive from banks is used for political activities such as the mass registration of Democratic Party voters; supporting left-wing political candidates at all levels of government (the farther to the left, the better); organizing rallies, protests, and lobbying efforts for various planks of its “People’s Platform,” etc. The ACORN “People’s Platform” once promised, “We will continue our fight until the American way is just one way, until we have shared the wealth. . . .” Socialism, in other words.

The CRA itself is based on a falsehood—that banks will systematically walk away from billions of dollars in profits that are just waiting to be picked up by someone in low-income and minority neighborhoods. Bankers are supposedly so blinded by prejudice that they must be forced by government to make these billions in profits that are waiting for them in the sub-prime mortgage market.

The reality is that the Fed forces mortgage lenders under the CRA to make billions of dollars in bad loans to unqualified borrowers. When *Forbes* magazine columnists Peter Brimelow and Leslie Spence interrogated Boston Fed official Alicia Munnell about the Fed’s claims of systemic lending discrimination in the early 1990s, Munnell was forced to admit that she had no evidence of it. She and other Fed officials (and the Clinton administration) continued to increase CRA enforcement anyway. This suggests that the goal of the CRA has always been a forced redistribution of wealth, not fighting racial discrimination. Charges of discrimination are simply used as a ruse to intimidate any un-cooperating mortgage lenders.

## Price Gouging: The Real Problem

**T**he single most important tax reform of the 1980s was the indexation of the federal income tax to inflation and the reduction of the number of federal income tax brackets from fifteen to three. Prior to that, ordinary middle class workers were pushed up into higher and higher tax brackets by simply receiving cost-of-living pay raises. The result was that a couple of years of cost-of-living raises actually reduced one's standard of living by diminishing one's overall take-home pay after taxes, while enriching the state.

Under this corrupt scheme the Fed would print excessive amounts of money, creating price inflation. The inflation led to cost-of-living increases that in turn caused "bracket creep" and higher tax payments. The federal government's budget became bloated while the taxpayers suffered. Politicians never had to take the heat for voting for tax increases; inflation did it for them. It was truly a form of taxation without representation (not that taxation *with* representation is any better).

The federal government is no longer capable of plundering the middle class in this particular manner, thanks to income tax indexation. But state and local governments do through the vehicle of property taxation. Every time property values rise, as they did in a major way in the first seven years of the twenty-first century, property tax revenues automatically go

up without any politician ever having to vote to raise taxes. Property tax assessments do their dirty work for them.

So when the Fed's expansionary monetary policy caused the real estate bubble, the extraordinary increases in property values were accompanied by equally extraordinary property tax increases. (After the bubble had burst, local governments were eager to raise property tax *rates* so as not to lose property tax revenue, which is determined by property value  $x$  tax rate).

For example, in Maryland local governments reportedly collected 35 percent more in property tax revenues in 2005 than they did in 2000. It is unlikely that the quality or quantity of government "services" improved by a third or more during that time. Citizens were simply paying over a third more for the same—or worse—"services."

## CHAPTER 12

# Farmed Robbery

**I**n 1996 President Bill Clinton signed into law a “freedom to farm” bill that was supposed to end most farm subsidies. At the time, the primary form of farm subsidy was price supports—price floors that are forcefully imposed by the state that are above free-market prices.

Ending price supports would certainly allow agricultural markets to work more efficiently, but it is rare indeed—and a bit odd—to observe government voluntarily ending a subsidy program that benefits a powerful political constituency, namely, wealthy corporate farmers. The reality is that the subsidies did not end; they just took on a different form.

A principle of public choice economics is that politicians will always do all they can to disguise subsidies to less-than-meritorious groups, such as millionaire corporate farmers. If they can subsidize them through protectionism, or price supports, this is much preferred than simply writing the millionaire businessman a check. The latter policy would make it too easy for the taxpaying public to smell a rat. But price controls had created such gross distortions in agricultural markets that government apparently decided that it was finally time to get rid of them—sort of. In their place came “transition payments” that were supposedly designed to temporarily ease the pain and suffering of the poor millionaire farmers who had lost their guarantee of above-market prices for everything they sold.

This ploy was yet another example of the public being duped by a government bait-and-switch scheme. The transitional payments were never

truly transitional, and they were probably never intended to be. The power of the agricultural lobby was never diminished, and it immediately went to work lobbying for increases in the new subsidies and to make them permanent. And they have succeeded. Each year there is an avalanche of “supplemental spending bills” that increases the amounts of corporate farm welfare the American taxpayers must fork over amounting to tens of billions of dollars annually.

By calling the programs “transitional” congress guaranteed itself a perpetual stream of campaign contributions from farmers, who could be relied upon to lobby and cough up millions of dollars in cash, year after year, in return for legislated extensions of the programs.

How this system of farmed robbery works was explained in a February 1, 2005 article in *USA Today* about Texas cotton farmers. The article featured one Eugene Bednarz, who had harvested four-thousand bales of cotton. Altogether, that year’s cotton production was expected to exceed 7.5 million bales, the best yield in more than fifty years.

This also meant that there would be the largest theft of taxpayers’ income by the farm lobby in more than half a century. The way the new system works is that if the market price of cotton falls below a government-mandated price support level, then the government will use taxpayer dollars to pay the farmers the difference between the actual price they get for their cotton and the arbitrarily-determined price-support price.

At the time, the market price of cotton was 35 cents per pound, with the price-control price set at 52 cents per pound. A bale of cotton weighs about five hundred pounds. Thus, Mr. Bednarz was paid the difference—17 cents—for each pound of his cotton. Consequently, the government wrote him a check for \$340,000 for doing absolutely nothing. No consumer or taxpayer received any benefit whatsoever in return. Texas cotton farmers as a whole figured to benefit in this way to the tune of some \$637,500,000 in that year.

Cotton, wheat, corn, soybean, and rice famers make out like bandits through this scheme, while others, such as sugar farmers, plunder the taxpayers in a slightly different manner, through government-mandated supply reductions that push up prices three to four times the world price. Everything that is made with sugar becomes more expensive as well.

Virtually everything government does increases the cost of living by driving up prices. Yet, most Americans still believe in the fairy tale that it is the free market that causes higher prices and that it is government, through benevolent and omniscient regulation, that is needed to “save” us.

## CHAPTER 13

# The Founding Father of Crony Capitalism

**A**s soon as the federal government announced its multi-trillion dollar bailouts of Wall Street plutocrats during the first years of The Great Recession, defenders of the bailouts pulled out what they apparently considered was a secret weapon: the myth of Alexander Hamilton as the supposed inventor of American capitalism. Hamilton, it was said, would approve of the bailouts for it was he, after all, who first proposed protectionist tariffs for “infant” industries, and the introduction of European-style mercantilism in America, complete with myriad subsidies and “bounties” for various industries. (Hamilton did so in his famous *Report on Manufactures*).

One Wall Street institution—*Forbes* magazine—published an article entitled “Alexander Hamilton versus Ron Paul” to make the point that libertarian critiques of corporate welfare should be dismissed because Hamilton was supposedly such a great statesman and economic genius compared to Congressman Ron Paul and his like-minded supporters.

The *Wall Street Journal* joined in the Hamilton worship by publishing an article by business historian John Steele Gordon in which he argued that our real problem is that central banking is not centralized enough and we need more central planning by the Fed, not less. Gordon called for an economic strongman in the form of a financial markets dictator/regulator; he supported the bailouts; and blamed the crisis on—Thomas Jefferson!

Jefferson opposed the creation of America's first central bank, the Bank of the United States, which had been championed by Hamilton. He was a hard-money advocate who did not trust politicians with money. It is this kind of thinking, said Gordon, which was the cause of the Great Recession. In reality, it was the Fed's policy of pursuing zero interest rates for year after year, coupled with the federal government's policies of forcing or enticing mortgage lenders to make trillions of dollars of bad loans to unqualified borrowers (securitized by Fannie Mae and Freddie Mac) that created the housing bubble.

What all of this frantic Hamilton idolatry demonstrated is how the myth of Alexander Hamilton as some kind of ingenious central economic planner is the ideological cornerstone of the American system of crony capitalism financed by a huge public debt and legalized counterfeiting through central banking. It is this system that was the main cause of The Great Recession, not opposition to the system as Gordon and others argued.

## The Real Hamilton

Hamilton was the intellectual leader of the group of men at the time of the founding who wanted to import the system of British mercantilism and imperialistic government to America. As long as they were on the paying side of British mercantilism and imperialism, they opposed it and even fought a revolution against it. But being on the *collecting* side was a different matter. It's good to be the king, as actor/comedian Mel Brooks might say.

It was Hamilton who coined the phrase "The American System" to describe the policies of corporate welfare, protectionist tariffs, central banking, and a large public debt, which he said would be a "blessing" to America. Unlike his political nemesis Thomas Jefferson, who was deeply educated in the economics of his day, having studied Adam Smith, John Baptiste Say, Richard Cantillon, and others. Hamilton either ignored or dismissed, or was unaware of this knowledge. Instead, he spread mercantilist myths that had been invented by public relations apologists such as Sir James Steuart for British mercantilists.

Hamilton championed the cause of a large public debt not to establish the good credit of the U.S. government or to finance any particular government programs, but for the Machiavellian reason of tying the economic self-interest of the wealthy to the government. It would be the wealthy

who would purchase government bonds, he argued, so that they would naturally become a powerful lobbying force for higher taxes and bigger government. They would do so to assure that there was always enough tax revenue in the Treasury to guarantee that they would receive the interest payments on their bonds. He was right: government bondholders, and the investment bankers who market the government's bonds, have always been supportive of Big Government. This is why Wall Street investment bankers were first in line for government bailouts as soon as the Great Recession commenced. The state takes care of its own, first and foremost, as any Mafia-style gang would do.

Hamilton's main arguments in favor of an empire of crony capitalists were put forth in his *Report on Manufactures*. In his 1905 biography of Hamilton William Graham Sumner wrote that Hamilton's report advocated "the old system of mercantilism of the English school, turned around and adjusted to the situation of the United States." Jefferson himself once wrote that Hamilton's "schemes" for protectionism, corporate welfare, and central banking were "the means by which the corrupt British system of government could be introduced into the United States." Sumner and Jefferson were right.

Hamiltonian mercantilism is essentially the economic and political system that Americans have lived under for several generations: A king-like president who rules through executive orders and disregards constitutional constraints on his powers; state governments that are mere puppets of the central government; corporate welfare run amok; tens of trillions of dollars of accumulated government debt; and perpetual boom-and-bust cycles (and periodic price inflation) caused by the fumbling antics of the faux central planners at the Federal Reserve Board. This is Hamilton's curse on America—a curse that must be exorcized if American freedom and prosperity are ever to be reinvigorated.

## The Curse of Instigationism

**O**f all the Republican presidential candidates in 2011–2012, only Ron Paul espoused the American foreign policy philosophy of Washington and Jefferson. For this he, and all other like-minded statesmen over the past seven decades, have been misleadingly smeared as “isolationists.” In this context, “isolationist” is truly Orwellian. By advocating peace and free trade, and only supporting just and defensive war, Ron Paul is advocating the maximum possible interaction between the peoples of the world.

It is the international division of labor and freedom of commerce that is in fact the very source of human civilization. All of the goods and services that we enjoy and utilize in our daily lives are the result of the efforts of hundreds, or thousands of people from all over the world who all specialize in something and, motivated by self interest, see to it that we get our bread, our beef, our beer, and everything else. It is restrictions on trade that are truly “isolationist,” and nothing restricts mutually-advantageous trade among the people of the world more than war does. War leads to isolationism. People interact peacefully and beneficially in the free market; they kill each other when they are at war.

The core principle of economics is that as long as there is private property and reasonably free markets, individuals, in pursuing their own self interests, will specialize in whatever they are best at, selling those things to

others, and using the proceeds to purchase things which they are not very good at producing. This is how the poorest of the poor can still survive and improve their lives. There is no “survival of the fittest” mentality attached to the free market. The poorest of the poor do not need to produce their own food, build their own houses, and manufacture their own clothing (nor does anyone else): the international division of labor allows them to rely on others to provide such things so that their lives are sustainable.

War, on the other hand, “bursts asunder” the international division of labor, as Ludwig von Mises wrote in his masterpiece, *Human Action*. For example, during the late nineteenth and early twentieth centuries the industrial revolution enhanced the standard of living of the average person more than the previous generations could ever have imagined. Wherever capitalism was allowed to flourish the common man enjoyed the fruits of the international division of labor as his standard of living rose while his hours of work per week declined (also thanks to the increased productivity of labor caused by capital investment under capitalism). World War I destroyed all of this, throwing country after country into an *isolationist* abyss by all but destroying the international division of labor. The people of the world who had benefited in countless ways from the efforts of strangers were isolated from those benefits as their living standards declined. Countries became isolated from the benefits of international trade while forming political alliances to wage war with. War being the opposite of capitalism, the end result was the death of millions and the destruction of capital on a massive scale.

Of course, there are always those who benefit from war: the monarchs, dictators, and “statesmen” who enjoy wallowing in “imperial glory,” as Alexander Hamilton described it; the politically connected who enrich themselves through defense contracts; the academics and “journalists” who operate a pro-war propaganda machine for the state in return for notoriety, position, and money; and the state in general. War is the health of the state; nothing aggrandizes the state and all its functionaries more than war does. As a corollary, nothing destroys freedom and prosperity more than non-defensive war does, either. And as Murray Rothbard remarked in his essay entitled “Just War,” the only truly just and defensive wars in American history have been the American Revolution and the South’s defense against the invasion launched against it by the Republican Party in 1861–1865.

The real “isolationists” who seek to destroy the peaceful cooperation among the people of the world are a group of people who might be called “*instigationists*.” These are the egomaniacs and rent seekers mentioned

above who instigate wars with their lying, conniving, and manipulating behavior. They typically have never participated in a war, or even the peacetime military, themselves, and are deservedly labeled as “chickenhawks” by many commentators.

Abraham Lincoln made the strongest defense of Southern slavery that was ever made in his first inaugural address, even pledging to support its explicit enshrinement in the Constitution, while threatening war over tax collection in the same speech. Since he had no intention of freeing any slaves, and waging war over tax collection would have made him an international war criminal, he needed to invent an excuse for invading his own country (the very definition of treason under Article 3, Section 3 of the U.S. Constitution, by the way). So he fabricated the notion of a “perpetual union.” The founding fathers, Lincoln implied, would have agreed with him that if any group of people ever attempted to leave the “voluntary” union that the founders created, the central government would have the “right” to invade those states, murder their citizens by the hundreds of thousands, bomb their cities, burn some of them to the ground, and plunder their wealth. This of course is what Lincoln’s army did, all in the name of preserving a seventy-year old political bargain. As for Fort Sumter, it is revealing that Lincoln wrote his naval commander, Gustavus Fox, after the incident (in which no one was injured, let alone killed) thanking him for his assistance in goading the South Carolinians into firing the first shot and instigating a war.

The Spanish-American War was purely a war of imperialism and never had any prospect of providing any benefit whatsoever to the average American. That is why the great late nineteenth-century libertarian scholar William Graham Sumner penned his famous essay, “The Conquest of the United States by Spain.” The Spanish-American War turned America into an empire, just like the Spanish empire, instead of the constitutional republic of the founders. But egomaniacal blowhards like Teddy Roosevelt were able to build their political careers out of this deranged adventure.

Nor did Americans have any business intervening in World War I, the most colossal disaster of the twentieth century, if not of all centuries. All that was “accomplished,” as Jim Powell writes in *Wilson’s War*, was the strengthening of the power of the communists in the Soviet Union and the rise of the Nazis in Germany. But there was plenty of power, glory, and riches for the political class and all of its supporters. Defense contractors became rich beyond their wildest dreams; lowly government bureaucrats became powerful economic dictators; and the statist intellectual class

began to think of itself as a class of grand social engineers. The so-called progressives were almost unanimously pro-war, for instance, because of their twin beliefs that: (1) government can and should be used to create heaven on earth, in the U.S. and in Europe; and (2) wartime central planning, Soviet style, could be a demonstration project for Soviet-style central planning of the peacetime American economy after the war.

After eight years of complete failure in ending the Great Depression, with his massive interventionist policies only making things worse, FDR manipulated the Japanese into invading Pearl Harbor, as Robert Stinnett documents with great care in his book, *Day of Deceit: The Truth about FDR and Pearl Harbor*. Entering the European war, in FDR's mind, would be the Mother of all Government Spending Programs which would surely end the depression and at least divert the public's attention away from his abysmal failures. After all, the reputation and legacy of Franklin Roosevelt was at stake. (The war did not end the depression; it only ended unemployment because of the conscription of more than ten million men when only some five million Americans were unemployed in the late 1930s.)

The Instigationist cabal was responsible for lying America into the disastrous Vietnam War, which caused the senseless and needless death of 55,000 Americans and hundreds of thousands of Vietnamese. Then of course there is the latest "victory" of the instigationists, the war in Iraq, which even the CIA admits was based on a lie—that Saddam Hussein had "weapons of mass destruction" that threatened the U.S. Thousands of American soldiers died for nothing there, while hundreds of thousands more were maimed for life and hundreds of thousands of Iraqis were killed. It was all for nothing as far as the average American taxpayer is concerned.

Think about the sick history of instigationism the next time you see a smirking and smarmy political hack urging the invasion of Iran, Syria, North Korea, or any other faraway place where he believes American bombs should be dropping.

## The State's Media Lapdogs

**I**n the late 1970s University of Rochester economists William Meckling and Michael Jensen presented a theory of “liberal” bias in the media that was based on a rigorous exploration of how the media best pursue their own self interest, coupled with an analysis of the role of government in shaping that self interest. In short, their thesis was that government had become so big and pervasive that your average journalist relied primarily on government itself, with all of its politicians, bureaucrats, and special-interest appendages, for most of the information that is reported to the public. If one is an environmental reporter, for example, one must cultivate relationships with the Environmental Protection Agency bureaucrats who are the main source of the latest news about environmental policy. If one is a labor reporter, one must cultivate relationships with U.S. Department of Labor bureaucrats who are the main source of the latest news about labor policy, and so on.

Consequently, any news reporter who is too critical of the government agencies that he is reporting about risks being cut off from his information source, the lifeblood of his career. Thus, career self-preservation among journalists requires that they essentially become lapdogs and mouthpieces for the state. They will tolerate and occasionally report about relatively inconsequential criticisms of the state, but are more likely to demonize those who make such criticisms. They do this in order to fool the public into believing that there is actually a public policy debate in Washington.

Whenever someone like a Congressman Ron Paul appears on the scene, who challenges the very propriety and existence of any statist central planning institution (such as the Fed), the media will ignore and/or demonize him and everyone associated with his views.

The Jensen/Meckling theory is correct as far as it goes, but it omits some other important elements of the sources of statist bias in the media. Murray Rothbard filled in these gaps in our understanding in his two essays entitled “The Nature of the State” and “Anatomy of the State.” All governments, Rothbard wrote, rely crucially on a set of myths and superstitions about its alleged greatness and benevolence coupled with accompanying lies, myths and superstitions about the “evils” of freedom, voluntarism, private enterprise, and the civil society. These myths and superstitions are not spread by government bureaucrats as much as by various intellectual prostitutes in academe and the media. The “court historians” of academe spin tall tale after tall tale about the “failures” of voluntarism and free markets and argue for more government interference in our lives. Keynesian economics would be a perfect example of this phenomenon, and *New York Times*/Democratic Party pundit Paul Krugman would be a perfect example of such a court historian.

This is another reason why the media ignore people like Congressman Ron Paul. There are a few exceptions, but for the most part members of the media have invested many years as skilled propaganda mouthpieces for the welfare/warfare state. They are as much a part of the state apparatus as is any government bureaucrat or politician. They are the essential tool of the state in dumbing down the general population so that it will peacefully acquiesce in the never-ending expansion of the state and the financial enrichment of all of its functionaries, especially the media. The expansion of the state is always accompanied by a reduction in prosperity and freedom of the general population.

Most members of the “mainstream media” are therefore paid professional liars who repeat over and over such absurdities as: “Higher taxes and more government spending will make us all more prosperous”; “taking naked x-ray photographs of everyone passing through airports is constitutional”; “the Constitution gives the president of the United States the right to bomb any country on the planet without consulting first with anyone else, especially Congress”; “the founding fathers thought it would be a good idea to place everyone’s freedom in the hands of five government lawyers with lifetime tenure”; “healthcare socialism will cause healthcare costs to decline”; “recessions and depressions are caused by sudden outbursts of

greed and “animal spirits”; “capitalists get rich by selling people products that will harm or kill them”; the president has a constitutional right to order the murder of American citizens if he labels them as suspected “enemy combatants”; and so on.

Having spent their entire careers spreading such absurd lies, the appearance of an educated, articulate, and knowledgeable person like Congressman Ron Paul absolutely terrifies the “mainstream media,” for he threatens to expose them, once and for all, as the frauds and enemies of the free society that they really are. This also explains the hostility exhibited by the state and much of the media toward freedom-supporting Web sites in particular and the internet in general. Such sources of gate-keeperless communication threaten to burst asunder the empire of lies upon which all state power relies.



SECTION 3

# Centralization versus Liberty



## Freedom and Federalism

**A**mericans—and much of the rest of the world—have been deprived of one of the most important means of establishing and maintaining a free society, namely, federalism or states’ rights. It is not just an accident that states’ rights have either been relegated to the memory hole or denigrated as a tool of racists. The Jeffersonian states’-rights tradition was (and is) the key to understanding why Thomas Jefferson believed that the best government is that which governs least, and that a limited constitutional government was indeed possible. The enemies of freedom have always and everywhere been opposed to political decentralization and in favor of political monopoly.

### What Are States’ Rights?

The idea of states’ rights is most closely associated with the political philosophy of Thomas Jefferson and his political heirs. Jefferson himself never entertained the idea that “states have rights,” which has always been a straw-man argument. Of course “states” don’t have rights; only individuals do. The essence of Jefferson’s idea is that if the people are to be the masters rather than the servants of their own government, then they must have some vehicle with which to control the government. That vehicle, in the Jeffersonian tradition, is political communities organized at the state and

local levels. That is how the people were to monitor, control, discipline, and even abolish, if need be, their own government.

It was Jefferson, after all, who wrote in the *Declaration of Independence* that government's just powers arise only from the consent of the people, and that whenever the government becomes abusive of the peoples' rights to life, liberty, and the pursuit of happiness it is the peoples' *duty* to abolish that government and replace it with another one. The people would achieve this just as they did when they adopted the Constitution, through political conventions organized by the states. The states, after all, were considered by the founding generation to be independent nations in the same sense that Great Britain and France were independent nations. The *Declaration of Independence* referred to them specifically as "free and independent," independent enough to raise taxes and wage war, just like any other state.

That is why the political heirs of Thomas Jefferson, mid-nineteenth-century Southern Democrats, held statewide political conventions (and popular votes) to decide whether or not they would continue to remain in the voluntary union of the founding fathers. It is also why the New England Federalists held a political convention in Hartford, Connecticut in 1814 when they were considering seceding from the union, ultimately deciding against it. Article 7 of the U.S. Constitution explained that the states could join or not join the union according to votes taken at state political conventions by representatives of the various communities within each state (not by state legislatures) and, in keeping with the words of the *Declaration*, they also had a right to vote to secede from the government and create a new one if they wished to do so.

Jefferson was not only the author of America's declaration of secession from the British empire; he championed the idea of state nullification of laws deemed to be unconstitutional with his Kentucky Resolutions of 1798, and also believed that the Tenth Amendment to the Constitution ("The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people") was the cornerstone of the entire document. He was a "strict constructionist" who believed that every effort should be made to force the central government to possess only those powers delegated to it *by the states* in Article 1, Section 8.

States' rights or federalism never meant that state government politicians were somehow more moral, wise, or less corrupt than national politicians are. The idea was always that: (1) It is easier for the people to keep an eye on and control government the closer it is to them; and

(2) a decentralized system of government consisting of numerous competing states provided citizens with an escape route from tyranny by a more centralized or monopolistic state. If say, Massachusetts created a state theocracy, those who did not want to live under that theocracy (or any theocracy) could escape to Virginia, Pennsylvania, or some other state. The idea of states' rights was never meant by the Jeffersonians to create a "laboratory of experimentation" with government policies, as contemporary political scientists have asserted. That would be treating people like so many experimental rats in a cage, and that is not likely how Jefferson liked to think of himself.

Secession or the threat of secession was always intended as a possible means of maintaining both the American union and constitutional government. The idea was that the central government would likely only propose constitutional laws if it understood that unconstitutional laws could lead to secession or nullification. Nullification and the threat thereof was intended to have the same effect. That is why the great British historian of liberty, Lord Acton, wrote the following to General Robert E. Lee on November 4, 1866, seventeen months after Lee's surrender at Appomattox:

I saw in States' rights the only availing check upon the absolutism of the sovereign will, and secession filled me with hope, not as the destruction but as the redemption of Democracy. The institutions of your Republic [referring to the Confederate Constitution] have not exercised on the old world the salutary and liberating influence which ought to have belonged to them, by reason of those defects and abuses of principle which the Confederate Constitution was expressly and wisely calculated to remedy. I believed that the example of that great Reform would have blessed all the races of mankind by establishing true freedom purged of the native dangers and disorders of Republics. Therefore I deemed that you were fighting the battles of our liberty, our progress, and our civilization; and I mourn for the stake which was lost at Richmond more deeply than I rejoice over that which was saved at Waterloo.

In addition to viewing the right of secession as the "only" means by which the people could effectively stop a tyrannical government, Lord Acton was also referring to such things as the Confederate Constitution's elimination of the "General Welfare Clause" of the U.S. Constitution; a single six-year term for president; the prohibition of protective tariffs and corporate welfare (with the exception of money for the dredging of harbors); and a generally more decentralized system of government. Of course, that system was

never allowed to become a reality since the Confederate states were being invaded by the largest army in the history of the world up to that point and did what states always do in such situations, namely, confiscate resources and centralize power to wage defensive war.

General Lee understood what Lord Acton was saying, and agreed with him. In a return letter on December 15, 1866, General Lee wrote the following:

While I have considered the preservation of the constitutional power of the General Government to be the foundation of our peace and safety at home and abroad, I yet believe that the maintenance of the rights and authority reserved to the states and to the people, not only are essential to the adjustment and balance of the general system, but the safeguard to the continuance of free government. I consider it as the chief source of stability to our political system, *whereas the consolidation of the states into one vast republic, sure to be aggressive abroad and despotic at home, will be the certain precursor of that ruin which has overwhelmed all those that have preceded it.* (Emphasis added)

Acton and Lee were prescient in their exchange of letters: the centralization of government power that was the hallmark of the world's political systems in the late nineteenth and all throughout the twentieth century was a plague on humanity as it was the prerequisite for the adoption of fascism and all other forms of socialism, including communism.

## The Origins of Nullification

**T**he defenders of centralized governmental power despise the Jeffersonian idea of nullification, that is, the idea that citizens of a state or states should have a say on the issue of the constitutionality of federal laws, and should be able to nullify those laws within their state if they are deemed to be unconstitutional.

This idea was popular among the American colonists, but is most closely associated with Thomas Jefferson and James Madison, authors of the Virginia and Kentucky Resolutions of 1798. Jefferson authored the “Kentucky Resolves” at the request of friends from Kentucky as a tool for nullifying the hated Sedition Act that was being enforced by President John Adams. The Sedition Act effectively made it illegal to criticize the federal government.

As soon as the Federalist Party gained power and George Washington went into retirement, it effectively outlawed free political speech in America in clear violation of the First Amendment. The spark that ignited this totalitarian impulse was an editorial by the grandson of Benjamin Franklin, Benjamin Franklin Bache, editor of the *Philadelphia Aurora* newspaper. Bache was a follower of Jefferson and his Democratic-Republican party, and was outspokenly opposed to the Federalist program of economic statism, i.e., protectionist tariffs, a national bank, corporate welfare, high taxes,

and a large public debt. In an editorial he called John Adams “old, querulous, bald, blind, crippled, toothless Adams.”

Abigail Adams is said to have been greatly upset over Bache’s characterization of her husband, and she and the Federalist-friendly newspapers began calling for Bache’s punishment. The result was the Alien and Sedition acts. The Sedition Act was enacted on July 14, 1798, and made it a crime to publish “false, scandalous, and malicious writing against the government or its officials.” Of course, government itself would decide what constituted improper and illegal speech, as would be the case in all future totalitarian societies. The law was written so that it would expire on the day that John Adams left office so that it could only be used against members and supporters of Jefferson’s party.

Many of the Jeffersonians resented the ostentatious displays of king-like grandeur that the Adams family was known for and were quite outspoken about it. In November of 1798 a man named David Brown put up a liberty pole in Dedham, Massachusetts with the words, “No Stamp Act, No Sedition Act, No Alien Bills, No Land Tax, Downfall to the Tyrants of America; Peace and Retirement to the President; Long Live the Vice President [Jefferson].” For this he was fined and sentenced to eighteen months in prison.

Several dozen newspaper writers who were supporters of Jefferson were arrested under the Sedition Act for criticizing the government. In addition, Federalist Party mobs often attacked newspapers and newspaper editors who were sympathetic to the Democratic-Republican Party or who criticized John Adams. Federalist Roger Griswold, a congressman from Connecticut, attacked fellow Congressman Mathew Lyon of Vermont by beating him with a hickory cane on the floor of the House of Representatives after Lyon criticized the Federalists as being “in opposition to the interests and opinions of nine-tenths of their constituents.”

After Lyons wrote a newspaper article suggesting that Adams had “an unbounded thirst for ridiculous pomp, foolish adulation, and selfish avarice,” the Adams administration convened a grand jury and indicted Lyons. After forcing the Revolutionary War veteran to walk through the streets of his home town in shackles, he was imprisoned. He ran for reelection from prison and won handily.

This is the kind of despotic behavior that motivated Jefferson to author the Kentucky Resolution of 1798. Section One of his famous “Resolve” reads as follows:

Resolved, that the several States composing the United States of America, are not united on the principles of unlimited submission to their General Government; but that by compact under the style and title of a Constitution For the United States and of amendments thereto, they constituted a General Government for special purposes, delegated to that Government certain definite powers, reserving each State to itself, the residuary mass of right to their own self Government; and that whensoever the General Government assumes undelegated powers, its acts are unauthoritative, void, and of no force. . . . That the Government created by this compact was not made the exclusive or final judge of the extent of the powers delegated to itself; since that would have made its discretion, and not the Constitution, the measure of its powers; but that as in all other cases of compact among parties having no common Judge, each party has an equal right to judge for itself, as well as of infractions as of the mode and measure of redress.

Madison's Virginia Resolve was almost identical. When Jefferson was elected president the Sedition Act was ended. The new president immediately ended all ongoing federal prosecutions and pardoned those who had been convicted under the Sedition Act, including Congressman Lyon.

During Jefferson's presidency the New England Federalists used the Kentucky Resolve to nullify enforcement of the trade embargo that President Jefferson had imposed after the British Navy began stealing American ships and kidnapping American sailors for use in its war against France. On February 5, 1809, the Massachusetts legislature declared that the embargo was "not legally binding on the citizens of the state" and denounced the law as "unjust, oppressive, and unconstitutional," as described by James J. Kilpatrick in *The Sovereign States*. All of the New England states, and Delaware, nullified the Embargo Act.

When the War of 1812 broke out the New England Federalists effectively seceded from the union by not participating in the war. The political vehicle for their antiwar stance was nullification. As stated by the Connecticut state assembly, as described by Kilpatrick:

[I]t must not be forgotten that the state of Connecticut is a FREE SOVEREIGN and INDEPENDENT State; that the United States are a confederated and not a consolidated Republic. The Governor of this State is under a high and solemn obligation, "to maintain the lawful rights and privileges thereof, as a sovereign, free and independent State," as he is "to support the

Constitution of the United States,” and the obligation to support the latter imposes an additional obligation to support the former. The building cannot stand, if the pillars upon which it rests, are impaired or destroyed.

This statement echoed Jefferson’s states’ rights interpretation of the Constitution as a compact among the states. Similar reasoning was subsequently used by South Carolinians to nullify the 1828 “Tariff of Abominations”; by Ohioans in their battle against the Bank of the United States attempting to operate branches of the bank in that state; and by the governments of Wisconsin and several other states to nullify the 1850 Fugitive Slave Act. It was never a ruse concocted by slave owners to “justify” slavery, as dishonest or inept contemporary historians have falsely asserted.

## The Real Meaning of the Fourth of July

**M**ost Americans seem unaware of the fact that one of their favorite holidays, the Fourth of July, is properly construed as a celebration of an act of violent secession. “Independence Day” is a celebration of the colonists’ secession from the British Empire, America’s first war of secession.

America’s most prominent secessionist, Thomas Jefferson, was very clear about what he was saying when he authored the nation’s declaration of secession, known to most as the *Declaration of Independence*: Governments derive their just powers from the consent of the governed, he wrote, and whenever that consent is withdrawn, it is the right and duty of the people to “alter or abolish” that government and to “institute a new government.”

In his first inaugural address President Jefferson further defended the right of secession by declaring: “If there be any among us who would wish to dissolve this Union or to change its republican form, let them stand undisturbed as monuments of the safety with which error of opinion may be tolerated where reason is left to combat it.” Debating the issue of secession is acceptable; using violent, governmental force to stop it was not in the mind of Thomas Jefferson. (Contrast this with Abraham Lincoln’s threats of “invasion” and “bloodshed” in any state that attempted to secede in *his* first inaugural address).

As time wore on, Jefferson never changed his opinion of the importance of the right of secession as an instrument of freedom. He considered all Americans, regardless of geographical location, to be part of the same “family,” and would never have contemplated violent opposition to any state or region that wanted to secede from the union. In a January 29, 1804 letter to Dr. Joseph Priestly he wrote:

Whether we remain in one confederacy, or form into Atlantic and Mississippi confederacies, I believe not very important to the happiness of either part. Those of the western confederacy will be as much identified with that country, in future time, as with this; and did I now foresee a separation at some future day, yet I should feel the duty & the desire to promote the western interests as zealously as the eastern, doing all the good for both portions of our future family . . .

In an August 12, 1803 letter to John C. Breckenridge, Jefferson addressed the same issue in the context of the New England Federalists’ attempt to secede and create their own confederacy in response to the Louisiana Purchase, which they vehemently opposed. If there were to be a “separation,” Jefferson wrote, then “God bless them both, & keep them in the union if it be for their good, but separate them, if it be better.”

The original American union of the founding fathers was a voluntary union based on the consent of the people of the free, independent, and sovereign states. It was not a union held together by violence, intimidation, censorship, and military invasion. That is what the *Soviet* Union was, and what the American union *became* in the post-1865 era.

## CHAPTER 19

# Electing U.S. Senators was a Bad Idea

**T**he popular election of U.S. Senators allows a small cabal of wealthy plutocrats to exert grossly disproportionate influence over government policy. This is because getting elected to the U.S. Senate requires the raising of millions of dollars for television advertising, campaign consultants, publicists, and the other elements of modern campaigning. Consequently, U.S. Senators have long been “in the pockets” of their major “campaign contributors,” some of whom may not even be American citizens. And the interests of these donors is not always the same as the best interests of the voting constituents in the home states of the senators.

It was not always that way. The original constitutional system called for the appointment of U.S. Senators by state legislatures. It wasn't until the Seventeenth Amendment was ratified in 1913 that senators were popularly elected.

Professor Ralph Rossum of Claremont McKenna College explained the rationale for the system of appointing senators in his book, *Federalism, the Supreme Court, and the Seventeenth Amendment*. The founding fathers intended that state legislatures would appoint senators and then instruct them on how to vote in Congress. This was to safeguard against the corruption of senators by special interests. “The ability of state legislatures to instruct senators was mentioned frequently during the Constitutional

Convention and the state ratifying conventions and was always assumed to exist,” wrote Professor Rossum.

At the New York ratifying convention John Jay, one of the authors of *The Federalist Papers*, said that “The Senate is to be composed of men appointed by the state legislatures. . . . I presume they will also instruct them, that there will be a constant correspondence between the senators and the state executives.” At the Massachusetts ratifying convention Fisher Ames referred to U.S. senators as “ambassadors of the states.” James Madison wrote in *Federalist* #45 that because of this system of appointing senators the U.S. Senate “would be disinclined to invade the rights of the individual States, or the prerogatives of their governments.” In *Federalist* #62 Madison further wrote that the appointment system “gave to state governments such an agency in the formation of the federal government as must secure the authority of the former.” In other words, it was meant to enhance the ability of the citizens of the states to be the masters rather than the servants of their own central government.

When Kentucky and Virginia nullified the Alien and Sedition Acts, the Kentucky and Virginia Resolutions, issued by the state legislatures, instructed the states’ U.S. senators to vote to repeal these acts. The appointment of senators often led to the resignation of senators whenever they reneged on their promises to remain faithful to the wishes of their state’s legislature. John Quincy Adams resigned from the U.S. Senate for supporting the Madison administration’s enforcement of the trade embargo, which the state’s legislature opposed. Senator David Stone of North Carolina resigned in 1814 after his state legislature disapproved of his collaboration with the New England Federalists on several legislative issues. Senator Peleg Sprague of Maine resigned in 1835 after opposing his state legislature’s instructions to oppose the rechartering of the Second Bank of the United States.

When the U.S. Senate “censored” President Andrew Jackson for having vetoed the rechartering of the Bank, seven U.S. Senators resigned rather than carry out their state legislatures’ instructions to vote to have President Jackson’s censure expunged. One of them was Senator John Tyler of Virginia, who would become president of the United States in 1841.

The original system of state legislative appointment of U.S. senators did exactly what it was designed to do: limit the tyrannical proclivities of the central government. As Professor Todd Sywicky of George Mason University wrote in a 1997 issue of the *Cleveland State Law Review*, “the Senate played an active role in preserving the sovereignty and independent sphere

of action of state governments” in the pre-Seventeenth Amendment era prior to 1913. “Rather than delegating lawmaking authority to Washington, state legislators insisted on keeping authority close to home. . . . As a result, the long-term size of the federal government remained fairly stable and relatively small during the pre-Seventeenth Amendment era.” This of course is also why there was a decades-long crusade to end the system of legislative appointment of senators and replace it with direct elections. The “god” of democracy provided a clever subterfuge for the advocates of unlimited powers in the hands of the central government.

## False Virtue: The Politics of Lying About History

In 1961 *Life* magazine invited the Pulitzer Prize-winning poet and novelist Robert Penn Warren (author of *All the King's Men* and nineteen other novels) to record his thoughts on the meaning of the American “Civil War” on the centennial of that event. Warren responded with a long essay on “the symbolic value of the war” which was eventually published as a small paperback book entitled *The Legacy of the Civil War*.

Writing long before the plague of political correctness dominated American society, Warren wrote that in addition to the issue of the extension of slavery into the new territories, in 1861 there was “a tissue of causes” of the war, including the dispute over the constitutionality of secession, “the mounting Southern debt to the North, economic rivalry, Southern fear of encirclement, Northern ambitions, and cultural collisions . . .”

There were myriad economic causes of the war apart from the issue of slavery, Robert Penn Warren believed. “The Morrill tariff of 1861 actually preceded the firing on Fort Sumter, but it was the mark of Republican victory and an omen of what was to come; and no session of Congress in the next four years failed to raise the tariff.”

What Warren was saying was that as soon as the population of the North grew enough to assure congressional dominance over the South, it used that dominance (through a lopsided congressional majority) to plunder the South economically with a protectionist tariff that mostly benefited

Northern manufacturers). And this began before Fort Sumter; the ten tariff-rate increases that occurred during the Lincoln administration, which raised the average tariff rate from 15 percent to nearly 50 percent, were a bedrock of Republican Party policy, not war-financing measures. Such rates of taxation would indeed last for another half century of Republican Party political domination, until the income tax was adopted in 1913.

“Even more importantly,” wrote Warren, “came the establishment of a national banking system . . . and the issuing of national greenbacks . . . plus government subsidy [to politically-connected corporations].” “Hamilton’s dream” of a large national debt was also realized, and “this debt meant a new tax relation of the citizen to the Federal government, including the new income tax.” All of this greatly centralized political power in Washington, D.C., which was certainly the effect, if not the primary purpose, of the war.

“Out of the Civil War came the concept of total war,” he wrote, referring to the intentional mass murder of tens of thousands of Southern civilians and the destruction of entire towns and cities along with the plundering of tens of millions of dollars of private property (and he was not referring to “slave property”). Warren mocked Lincoln’s lame attempt to “justify” the mass murder of civilians by quoting his (Lincoln’s) 1862 speech in which he said, “The dogmas of the quiet past are inadequate to the stormy present. . . . As our case is new, we must think anew and act anew.” That is, “we” must abandon the moral code of civilized societies, and international law, which prohibits the intentional murder of civilians (mostly women and children) during war. In light of the fact that Lincoln illegally suspended the writ of *habeas corpus*, mass arrested and imprisoned tens of thousands of Northern political dissenters without due process, shut down hundreds of opposition newspapers, deported an opposition member of Congress (Clement Vallandigham of Ohio), rigged Northern elections, illegally orchestrated the secession of West Virginia from Virginia, and essentially declared himself dictator, Lincoln’s “think anew” statement also meant that the Constitution itself should be abandoned.

A major theme of *The Legacy of the Civil War* is that the war supposedly left the North (which monopolized the federal government for the succeeding half century and longer) with “a treasury of virtue.” This, said Warren, is the “psychological heritage” left to the North by the war. “The Northerner, with his Treasury of Virtue, feels redeemed by history,” he wrote. “He has in his pocket, not a Papal indulgence peddled by some

wandering pardoner of the Middle Ages, but an indulgence, a plenary indulgence, for all sins past, present, and future.”

Thus, this supposed “treasury of virtue” would fill the U.S. government with extraordinary hubris and would become the all-purpose rationale for its twenty-five year war of genocide against the Plains Indians that was commenced just three months after Appomattox; for the decade-long plundering of Southerners after the war under the laughable rubric of “reconstruction”; for the murder of some 200,000 Filipinos for their opposition to becoming pawns of the U.S. empire after having just gotten rid of the Spanish empire; for entering a European war that was none of our business to supposedly “make the world safe for democracy”; and on and on. All of this was supposedly done in the name of virtue, freedom, and democracy.

This farcical theory of “American exceptionalism” was more accurately described by Robert Penn Warren as “moral narcissism” which is “a poor basis for national policy.” Nevertheless, it was the “justification” for “our crusades of 1917–1918 and 1941–1945 and *our diplomacy of righteousness, with the slogan of unconditional surrender and universal spiritual rehabilitation for others*” (emphasis added).

Posturing as The Most Moral Humans on Earth requires Americans to forget many facts about their own history—or more precisely, for the government-dominated school system to either eliminate these facts from the curriculum or to distort them beyond recognition. In Warren’s own words:

[I]t is forgotten that the Republican platform of 1860 pledged protection to the institution of slavery where it existed, and that the Republicans were ready, in 1861, to guarantee slavery in the South, as bait for a return to the union. It is forgotten that in July 1861, both houses of Congress, by an almost unanimous vote, affirmed that the war was waged not to interfere with the institutions of any state but only to maintain the Union. It is forgotten that the Emancipation Proclamation . . . was limited and provisional: slavery was to be abolished only in the seceded states and only if they did not return to the Union before the first of next January.

Moreover, it must also be forgotten, Warren wrote, that most Northern states “refused to adopt Negro suffrage” and that Lincoln was as much a white supremacist as any man of his time. “It is forgotten that Lincoln, at Charlestown, Illinois, in 1858, formally affirmed: ‘I am not, nor ever have

been, in favor of bringing about in any way the social and political equality of the white and black races.”

Only if the true history of Lincoln and his war is whitewashed from the history books can the war be viewed, “according to this doctrine of *The Treasury of Virtue*, as a consciously undertaken crusade so full of righteousness that there is enough overplus stored in Heaven, like the deeds of the saints, to take care of all small failings and oversights of the descendants of the crusaders, certainly unto the present generation.”

Warren further quoted the historian Samuel Eliot Morison as commenting that one effect of this supposed *Treasury of Virtue* on his (Morison’s) native New England was that “In the generation to come [after the Civil War] that region would no longer furnish the nation with teachers and men of letters, but with a mongrel breed of politicians” obsessed with “profiteering” through their political connections.

With such overflowing virtue, Americans only need to announce their policy intentions, said Warren, without even contemplating an examination of whether or not the policies did what they were promised to do (make the world safe for democracy, for example). For “the man of righteousness tends to be so sure of his own motives that he does not need to inspect consequences.” Moreover, “the effect of the conviction of virtue is to make us lie automatically and awkwardly . . . and then in trying to justify the lie, lie to ourselves and transmute the lie into a kind of superior truth.”

Robert Penn Warren believed that most Americans were content to believe in all of these lies about their own history that were the work of “the manipulations of propaganda specialists, and their sometimes unhistorical history.” Most Americans “are prepared to see the Civil War as a fountainhead of our power and prestige among the nations.”

The lies have accumulated like snowflakes during a Colorado blizzard, year after year, since Robert Penn Warren wrote those words in 1961. Prestige based on an avalanche of lies is a far more accurate description of American foreign policy in the post Civil War era than is “American exceptionalism,” the mating call of all of the neoconservatives who took over the American foreign policy establishment in the 1980s. It should be no surprise to anyone that every one of these “chickenhawks,” as they are often called (for advocating endless war while never having been in the military themselves, for the most part), is among other things a card-carrying member of the Lincoln cult.

## CHAPTER 21

# How (and Why) the Lincoln Myth was Invented

In his 2009 book, *The Unpopular Mr. Lincoln*, historian Larry Tagg utilized thousands of primary literary sources to make his case that Abraham Lincoln was by far the most hated and reviled of all American presidents *during his lifetime*. After his death Lincoln was turned into the kindly, grandfatherly, saintly figure that he has been portrayed as ever since then. This “makeover,” as Professor Tagg explains, was the work of the Republican Party propaganda machine with significant assistance from the New England clergy.

As for how the people of the North—and the rest of the world—viewed Lincoln while he was alive, Tagg writes:

The violence of the criticism aimed at Lincoln by the great men of his time on both sides of the Mason-Dixon line is startling. The breadth and depth of the spectacular prejudice against him is often shocking for its cruelty, intensity, and unrelenting vigor. The plain truth is that Mr. Lincoln was deeply reviled by many who knew him personally, and by hundreds of thousands who only knew of him.

Larry Tagg is no neo-Confederate. He is a native of Lincoln, Illinois, and he thanks the prominent Lincoln scholar Harold Holzer in his acknowledgements. He goes on to say that Lincoln was widely denounced in

the Northern states during his administration for being “a bloody tyrant” and a “dictator” for his “arbitrary arrests, the suspension of *habeas corpus*, and the suppression of newspapers,” among other things. He quotes the abolitionist Wendell Phillips as saying that Lincoln was “a first-rate second-rate man.” Historian George Bankroft called Lincoln “ignorant, self-willed, and is surrounded by men some of whom are almost as ignorant as himself.”

The Lacrosse, Wisconsin *Democrat* newspaper advocate assassination when it editorialized in November of 1864 that “If Abraham Lincoln should be reelected for another term of four years of such wretched administration, we hope that a bold hand will be found to plunge the dagger into the tyrant’s heart for the public welfare.” The *New York Times* was just as harsh when it editorialized in May of 1864 that “No living man was ever charged with political crimes of such multiplicity and such enormity as Abraham Lincoln. He has been denounced without end as a purjerer, a usurper, a tyrant, a subverter of the Constitution, a destroyer of the liberties of his country, a reckless desperado, a heartless trifler over the last agonies of an expiring nation.” There is no place in hell, the *Times* continued, that is “full enough of torment to expiate his iniquities.”

The most interesting chapter of *The Unpopular Mr. Lincoln* is the final Epilogue entitled “The Sudden Saint.” Here Professor Tagg explains how the Republican Party, with the aid of the New England clergy, created out of thin air the myth of the “sainted” and “beloved” Abraham Lincoln. The assassination was a miracle of luck as far as they were concerned, for it put in their lap an opportunity to deify their Big Government political agenda by attaching it to the soon-to-be-deified Lincoln. As Tagg explains, the Republican Party “saw that his death was a propaganda windfall—Lincoln could be made to stand for the North, for freedom. . . .” He quotes Senator James Grimes of Iowa as saying that the party’s propaganda campaign to deify Lincoln was so successful that it “has made it impossible to speak the truth of Abraham Lincoln hereafter.”

Professor Tagg explains how it was Secretary of War Edwin Stanton who decided to use Lincoln’s funeral as a massive propaganda tool as he “made the martyr’s corpse a traveling exhibit of Southern wickedness.” The funeral procession took a 1600-mile route, and Stanton prohibited anyone to obscure the damage done by the assassin’s bullet so that the corpse would appear as gruesome as possible.

Many New England preachers who had reviled Lincoln just a few months earlier got with the program and deified him. Henry Ward Beecher

was arguably the biggest hypocrite of all of them. He had viciously attacked Lincoln in his pulpit for years, but after his death he “heaped only praise on Lincoln,” writes Tagg.

The Republican Party also continued the thuggish tactics that it had used to intimidate the Northern public during the war. “The Democratic papers quickly realized that if they didn’t repent their opposition to Lincoln,” writes Tagg, “they risked ruin by mobs like the ones that had gutted their offices in the first summer of the war.”

The Republican Party’s army of thugs also did its best to censor free speech in the North, as they had also done during the war. One observer of the Lincoln funeral “sent up a cheer for Jefferson Davis,” and “was set upon by mourners and nearly torn to pieces.” A Chicago man was overheard in the lobby of a hotel saying “it served him right” and was promptly shot to death in front of dozens of witnesses. But “there was no arrest, no one would have arrested the man” who did the shooting, says Tagg.

Americans were imprisoned all over the North for making similar statements, as Tagg documents. “The doors of local jails rattled shut behind men in every city who were heard exulting the news of Lincoln’s death.” The editor of a Maryland newspaper was “killed by a mob after he had published criticism of Lincoln.” Roving mobs of Republican Party thugs traveled from one opposition newspaper to another, as they had done during the war in the North, and “emptied their contents into the street amid the applause of an immense crowd.”

For several generations, media opposition to the Republican Party was rendered prostrate. Ministers in the South were ordered by their military occupiers during “Reconstruction” to deliver sermons deifying Lincoln and many Southern newspapers were ordered to do the same. To defy such orders meant the “terror of confiscation and imprisonment,” writes Professor Tagg. Not surprisingly, there appeared “sudden proclamations of Lincoln’s nobility” all throughout the South.

This is how the Lincoln myth was invented and explains why the average American knows almost nothing at all about the nation’s most notorious president.

## CHAPTER 22

# Centralization Lets the Worst Rise to the Top

All of the worst tyrants in world history have been enemies of states' rights, federalism, and divided sovereignty. Tyrants lust after monopolistic political power, and monopolistic political power cannot exist if the people have an escape route from it. Dissent must be crushed and avenues of dissent abolished if one is to exercise dictatorial powers over a society. Adolf Hitler articulated this view as well as any twentieth-century tyrant did. On page 566 of the 1999 Mariner/Houghton Mifflin edition of *Mein Kampf* Hitler echoed the views of Lincoln, Hamilton, Story, Marshall, and Webster when he wrote:

[T]he individual states of the American Union . . . could not have possessed any state sovereignty of their own. For it was not these states that formed the Union, on the contrary it was the Union which formed a great part of such so-called states.

This was Hitler's reiteration of the argument that Lincoln made in his first inaugural address on March 4, 1861 where he said:

[T]he Union is much older than the Constitution. It was formed in fact, by the Articles of Association in 1774. It was matured and continued by the Declaration of Independence . . . by the Articles of Confederation in 1778 . . . and establishing the Constitution. . . . It follows from these views that no State, upon its own mere motion, can lawfully get out of the Union.

Hitler wrote the above words in the context of making his own case for the abolition of states' rights in Germany, and he naturally referred to Lincoln's novel and a-historical theory to bolster his case.

Hitler mocked what he called the "so-called sovereign states" in Germany because they stood in the way of a centralized Reich with their "impotence" and "fragmentation." Such "fragmentation" had been understood by Europeans for centuries to be an important source of freedom from tyranny. Europeans had been slowly eliminating such freedom through governmental consolidation and Hitler wanted to speed up the process by turning all of Europe into one big "Reich" administered by himself.

Hitler praised German Chancellor Otto von Bismarck for proving "the greatness of his statesmanship" by gradually diminishing the sovereignty of the German states and centralizing governmental power in Germany. This was a most welcomed development, Hitler wrote, since the power of the central state in Germany was supposedly threatened by "the struggle between federalism and centralization so shrewdly propagated by the Jews in 1919–20–21 and afterward . . ."

He further condemned federalism as "a league of sovereign states which ban together of their own free will, on the strength of their sovereignty" to cede some—but not all—of their sovereignty to form "the common federation." This was an accurate description of the original American constitutional system of states' rights or federalism, and Hitler voiced his extreme opposition to it.

Bismarck did a good job of destroying most of the vestiges of federalism and states' rights in Germany, Hitler wrote, but he did not go nearly far enough. "And so today this state [Germany], for the sake of its own existence, is obliged to curtail the sovereign rights of the individual provinces more and more, not only out of general material considerations, but from ideal considerations as well." Thus, a rule "basic for us National Socialists is derived," wrote Hitler: "A powerful national Reich."

Adolf Hitler then asserted the "inevitability" argument: "Certainly all the states in the world are moving toward a certain unification in their inner organization. And in this Germany will be no exception. Today it is an absurdity to speak of a 'state sovereignty' of individual provinces." He condemned the idea of federalism as the work of "unclean party interests" and promised that the National Socialists (Nazis), moreover, would totally eliminate states' rights altogether:

Since for us the state as such is only a form, but the essential is its content, the nation, the people, it is clear that everything

must be subordinated to its sovereign interests. In particular we cannot grant to any individual state within the nation and the state representing it state sovereignty and sovereignty in point of political power.

The “mischief of individual federated states . . . must cease,” Hitler demanded. In the future of Germany the individual states would no longer be involved in “state power and policy,” he wrote. Nazism is not the “servant” of the people of “the individual federated states,” Hitler continued, while predicting that “the National Socialist doctrine” will “some day become the master of the German nation” that will “reorder the life of a people.” The people are to be servants of the state, not the other way around. Hitler believed that this could only be achieved by first abolishing states’ rights in Germany.

## Death by Government: The Missing Chapter

In recent years scholars have attempted to document the extent to which various governments during the twentieth century committed acts of mass murder against their own citizens. These are not estimates of war-related deaths, but of the murder of dissenters to the regime. The most prominent works are those by sociologist R.J. Rummel (*Power Kills* and *Death by Government*) and *The Black Book of Communism* by a collection of French authors.

The main reason for such “democide,” as Professor Rummel calls it, was to eliminate all opposition to the ruling regime and its ideology. In Russia, the Kulaks “who resisted collectivization [of their property] were shot, and the others deported,” according to *The Black Book of Communism*. When the rural population of the Ukraine resisted, Stalin created a famine that killed some six million in a few months. Virtually identical crimes were committed by the regimes of Mao Zedong, Kim Il sung, and Pol Pot, among others. In every instance, the reason for all the mass murder was the elimination of resisters to centralized political power and centralized planning of entire societies.

*The Black Book of Communism* estimated that the Soviets murdered at least 20 million of their own citizens; the Chinese socialists killed 65 million; Vietnamese socialists murdered 1 million; the North Koreans killed 2 million; 1 million perished in Eastern Europe; 150,000 in Latin America;

1.7 million in Africa; and 1.5 million in Afghanistan. In addition to this, Professor Rummel included in his estimate 21 million civilians murdered by the Nazi government.

In *Power Kills*, Professor Rummel writes that “democidal” regimes tend to become even more vicious toward their own people when their political power is “conjoined with an absolutist ideology” such as socialism. And, when the rulers of such regimes find that the continued existence of a social group is incompatible with their beliefs and goals, their totalitarian power enables them to destroy that group, he writes. War or rebellion have often provided a convenient excuse and cover for such “democide” according to Professor Rummel.

In light of this reasoning, there appears to be a glaring omission in the literature on “democide,” namely, the 350,000 or more residents of the Southern states who perished as a result of the Lincoln regime’s invasion and waging of total war on them from 1861–1865. Historians have long pegged the number of Southern war deaths at around 300,000, while historian James McPherson estimated that in addition to these war-related deaths, some 50,000 Southern civilians, mostly women and children, were also killed. There are new estimates in the historical literature that claim that the real number may be closer to 450,000.

Lincoln never admitted that the Southern states were out of the union and that secession was legitimate. He argued that the secession of the Southern states was merely a “rebellion” by a minority of fire eaters and was therefore illegitimate. He always considered every Southerner, from Robert E. Lee to the lowliest yeoman farmer, to be a U.S. citizen. His waging of total war on his own citizens, therefore, qualifies as an act of democide as defined by Professor Rummel.

The ideology that Southerners rejected was the “mystical” and perpetual union, as Lincoln called it, from which there could never be any escape. They believed that the union was voluntary, that the free and independent states were sovereign, and that they had a right to join or not join the union. Lincoln was an Uber-nationalist and disagreed, and was willing to use the powers of the state to murder his own citizens by the hundreds of thousands to “prove” himself right.

The population of the United States in 1861 was about one-tenth of what it was in the early twenty-first century. Standardizing for today’s population, the number of Southerners who perished as a result of the total war that was waged on them would be the equivalent of 3.5 million deaths. That would make the Lincoln regime significantly worse than the Pol Pot regime

in Cambodia. If the new estimates of some 450,000 Southern deaths comes to be accepted, then the Lincoln regime would be more than twice as bad as the Pol Pot and North Korean communists and four times worse than the Vietnamese communists in terms of democide.

## The Birth of American Imperialism

In *The Costs of War* (edited by John Denson), historian Joseph Stromberg referred to the Spanish-American War of 1898 as a “trial run” for the American empire. The war had nothing to do with national defense and was purely an act of imperialism on the part of the U.S. government, which gained control over Cuba, Puerto Rico, Guam, and the Philippine Islands. It led the renowned late nineteenth-century libertarian scholar, William Graham Sumner of Yale, to compose a famous essay entitled “The Conquest of the United States by Spain.” The essay described how the war transformed America from a constitutional republic into an imperialist power, just like the old Spanish Empire it defeated in the war.

Sumner also forecast what was to come, and what America is today: the policeman of the world, with a military presence in over one-hundred countries, with endless meddling in the affairs of just about everyone on the planet. As he wrote in *War and Other Essays*,

We were told that we needed Hawaii in order to secure California. What shall we now take in order to secure the Philippines? . . . We shall need to take China, Japan, and the East Indies . . . in order to ‘secure’ what we have. Of course this means that . . . we must take the whole earth in order to be safe on any part of it, and the fallacy stands exposed.

Stromberg's analysis of the importance of the Spanish-American War as a "trial run" for American imperialism is an astute analysis, but the real trial run actually occurred more than thirty years earlier during what Stromberg called the U.S. government's war against "internal independent nations," i.e., the Plains Indians. That is where the real template of American imperialism was set, with its demonization of the Indians as inhuman "wild beasts"; the mass murder of everyone and everything, women, children, and animals included; and the policy of unconditional surrender. Indeed, it may even be argued that the War to Prevent Southern Independence was itself a "trial run" for the twenty-five year war on the Plains Indians.

## Sherman's War of Extermination

As soon as the War to Prevent Southern Independence was concluded the U.S. government commenced a new war against the Plains Indians. On June 27, 1865, barely two months after the end of the war, General William Tecumseh Sherman was given command of the Military District of the Missouri, which was one of five military divisions the government had divided the country into. There was never any attempt to hide the fact that the war against the Plains Indians was, first and foremost, an indirect subsidy to the government-subsidized transcontinental railroads. Railroad corporations were the financial backbone of the Republican Party, which essentially monopolized national politics from 1865 to 1913, beginning with the election of the first Republican president, the renowned railroad industry lawyer/lobbyist, Abraham Lincoln of the Illinois Central.

General Sherman wrote in his memoirs that as soon as the war ended, "My thoughts and feelings at once reverted to the construction of the great Pacific Railway. . . . I put myself in communication with the parties engaged in the work, visiting them in person, and I assured them that I would afford them all possible assistance and encouragement." Michael Fellman, in *Citizen Sherman*, cites a letter Sherman wrote to Ulysses S. Grant in 1867 saying that "We are not going to let a few thieving, ragged Indians check and stop the progress [of the railroads]."

Dee Brown, in *Hear that Lonesome Whistle Blow*, writes that Lincoln's old personal friend Grenville Dodge, who he had appointed as a military general, initially recommended that slaves be made of the Indians so that they could be forced to dig the railroad beds from Iowa to California. The government decided instead to try to murder as many Indians as possible,

women and children included, and then to imprison the survivors in concentration camps euphemistically called “reservations.”

When he became president, Grant made his old pal Sherman the commanding general of the U.S. Army and another “Civil War” luminary, General Phillip Sheridan, assumed command on the ground in the West. “Thus the great triumvirate of the Union Civil War effort,” writes Fellman, “formulated and enacted military Indian policy until reaching, by the 1880s, what Sherman sometimes referred to as ‘the final solution of the Indian problem’” (emphasis added). Other former Union Army officers joined in the slaughter. This included John Pope, O.O. Howard, Nelson Miles, Alfred Terry, E.O.C. Ord, C.C. Augur, Edward Canby, George Armstrong Custer, Benjamin Garrison, and Winfield Scott Hancock.

“Sherman viewed Indians as he viewed recalcitrant Southerners during the war and newly freed people after: resisters to the legitimate forces of an ordered society,” writes John Marzalek, author of *Sherman: A Soldier’s Passion for Order*. “During the Civil War,” Marzalek continues, “Sherman and Sheridan had practiced a total war of destruction of property. . . . Now the army, in its Indian warfare, often wiped out entire villages. . . . Sherman insisted that the only answer to the Indian problem was all-out war—of the kind he had utilized against the Confederacy.”

Lee Kennett, author of *Sherman: A Soldier’s Life* writes that Sherman, Sheridan, Grant, and the other “Civil War luminaries” all considered Indians to be subhuman and racially inferior to whites, a belief that they used to “justify” their policy of extermination. Sherman also believed that the freed slaves would become “wild beasts” if they were not strictly controlled by whites. “The Indians give a fair illustration of the fate of the negroes if they are released from the control of the whites,” he said. Sherman sought “a racial cleansing of the land,” wrote Fellman. “All the Indians will have to be killed or be maintained as a species of paupers,” Sherman declared. Fellman documents that Sherman “gave Sheridan prior authorization to slaughter as many women and children as well as men Sheridan or his subordinates felt was necessary when they attacked Indian villages.”

Sherman and Sheridan’s troops conducted more than 1,000 attacks on Indian villages, mostly in the winter months when families would be together. Orders were given to kill everyone and everything, including dogs. A war of extermination was also waged on the American buffalo, since it was the Indians’ chief source of food, winter clothing, and other things (the Indians even made fish hooks out of dried buffalo bones).

The “Indian Wars” were actually a *continuation* of the policy of extermination that commenced by the Lincoln administration during the War to Prevent Southern Independence. One of the first attacks was the notorious Sand Creek Massacre of November 1864. There was a Cheyenne and Arapaho village located on Sand Creek in southeastern Colorado that had been assured by the U.S. government that it would be safe there. However, another Union Army “luminary,” Colonel John Chivington, carried out the government’s plan of renegeing on this promise. As described in *Crimsoned Prairie: The Indian Wars*, by S.L.A. Marshall who authored thirty books on American military history, Chivington’s orders to his troops were: “I want you to kill and scalp all, big and little; nits make lice.”

Marshall describes how the troops “began a full day given over to blood-lust, orgiastic mutilation, rapine, and destruction—with Chivington . . . looking on and approving.” Upon returning to Denver, Chivington “and his raiders demonstrated around Denver, waving their trophies, more than one hundred drying scalps. They were acclaimed as conquering heroes, which was what they had sought mainly.” “Colorado soldiers have once again covered themselves with glory,” one Republican Party newspaper in Colorado proclaimed.

An even more disgusting account of the Sand Creek massacre is given in the famous book by Dee Brown, *Bury My Heart at Wounded Knee: An Indian History of the American West*. “When the troops came up to the [squaws], they ran out and showed their persons to let the soldiers know they were squaws and begged for mercy, but the soldiers shot them all. . . . There seemed to be indiscriminate slaughter of men, women and children. . . . The squaws offered no resistance. Every one . . . was scalped.”

This type of a war of extermination or genocide was repeated hundreds of times from 1865–1890, when Sherman’s “final solution” was finally realized. Commenting on the butchering of Indian women and children by Custer, Superintendent of Indian Affairs Thomas Murphy remarked in 1868 that it was “a spectacle most humiliating, an injustice unparalleled, a national crime most revolting, that must, sooner or later, bring down upon us or our posterity the judgment of Heaven” (quoted in Dee Brown, *Bury My Heart at Wounded Knee*).

Custer found that his order to “kill or hang all the warriors” was “dangerous” to his soldiers because it meant “separating them from the old men, women, and children” (quoted in Brown, *Bury My Heart at Wounded Knee*). So he decided to just kill everyone, women and children included. Marshall, who was the U.S. government’s official historian of the European

Theater of War in World War II, called Sheridan's orders to Custer "the most brutal orders ever published to American troops." Sheridan is credited with the saying that "the only good Indian is a dead Indian," a policy that was endorsed by both Sherman and Grant (who has laughingly been portrayed by court historians recently as some kind of racial hero).

It was the barbaric behavior of these "Civil War luminaries" during the quarter century after Appomattox that was used to "justify" such things as the mass murder of hundreds of thousands of Filipinos by the U.S. Army during the 1899–1902 Filipino revolt against American imperialism. President Theodore Roosevelt "justified" this mass slaughter by calling Filipinos "savages, half-breeds, a wild and ignorant people." William Tecumseh Sherman himself could not have said it better.

## Paul Krugman's Politically-Correct "Civil War" Delusions

**W**hen James M. Buchanan was awarded the Nobel Prize in Economics in 1986 the first thing he said at his George Mason University press conference was that the award “does not make me an instant expert in everything.” Buchanan was well aware—and amused—at how previous recipients of the award had made fools of themselves by viewing the award as a license to pontificate about anything and everything, whether they knew anything about the subject or not.

No such modesty and sense of reality occupies the mind of a more recent Nobel laureate, Paul Krugman. As a *New York Times* columnist he has always done what all *New York Times* columnists do—pretend that he does in fact know everything about everything. A case in point is his March 29, 2012 *New York Times* blog entitled “Road to Appomattox Blogging.” After mentioning how the *Times* has a special “Disunion” blog to commemorate the 150<sup>th</sup> anniversary of the start of the war, Krugman gives a hilarious, elementary-schoolish rendition of his “take” on the “Civil War.”

Krugman said he has always been infatuated by the “symbolism” of Lee’s surrender at Appomattox, with “Lee the patrician in his dress uniform,” compared to General Grant, who was “still muddy and disheveled

from hard riding." Krugman is apparently unaware that in 1860, on the eve of the war, Robert E. Lee was in his thirty-second year as an officer in the United States Army, performing mostly as a military engineer. He was hardly a "patrician" or member of a ruling class. Grant, by contrast, was the overseer of an 850-acre slave plantation owned by his wealthy father-in-law. The plantation, located near St. Louis, was known as "White Haven" (which sounds like it could have been named by the KKK) and is today a national park. (On the "White Haven" Web site the National Park Service euphemistically calls Grant the "manager" of the slave plantation rather than the more historically-accurate word "overseer".)

In 1862 Lee freed the slaves that his wife had inherited, in compliance with his father-in-law's will. Grant's father-in-law's White Haven slaves were not freed until an 1865 Missouri emancipation law forced him to do so. The fact that Lee changed clothes before formally surrendering did not instantly turn the thirty-six-year army veteran into a "patrician," contrary to the "all-knowing" Krugman's assertion.

Krugman goes on to assert that the North's victory in the war was a victory in "manners" by a region that "excelled at the arts of peace." Well, not really. What the North "excelled" in was the waging of total war on the civilian population of the South. The Lincoln administration instituted the first federal military conscription law, and then ordered thousands of Northern men to their death in the savage and bloody Napoleonic charges that characterized the war. When tens of thousands of Northern men deserted, the Lincoln administration commenced the public execution of deserters on a daily basis. When New Yorkers rioted in protest of military conscription, Lincoln ordered 15,000 soldiers to the city where they murdered hundreds, and perhaps thousands of draft protesters (see Iver Bernstein, *The New York City Draft Riots*). It also recruited thousands of European mercenaries, many of whom did not even speak English, to arm themselves and march South to supposedly teach the descendants of James Madison, Patrick Henry, and Thomas Jefferson what it really meant to be an American. Lee Kennett, biographer of General William Tecumseh Sherman, wrote of how many of Lincoln's recruits were specially suited for pillaging, plundering, and raping: "the New York regiments were . . . filled with big city criminals and foreigners fresh from the jails of the Old World" (Lee Kennett, *Marching Through Georgia*).

The North waged war on Southern civilians for four long years, murdering at least 50,000 of them. It bombed cities like Atlanta for days at a time when they were occupied by no one but civilians, and U.S. Army

soldiers looted, ransacked, and raped their way all throughout the South. The “arts of peace” indeed, Mr. Krugman.

As for the war being a victory of “manners,” as Krugman says, consider this: When the women of New Orleans refused to genuflect to U.S. Army troops who were occupying their city and killing their husbands, sons, and brothers, General Benjamin “Beast” Butler issued an order that all the women of that city were to henceforth be treated as prostitutes. “As the officers and soldiers of the United States have been subject to repeated insults from the women . . . of New Orleans,” Butler wrote in his General Order Number 28 on May 15, 1862, “it is ordered that thereafter when any female shall, by word, gesture, or movement, insult or show contempt for any officer or soldier of the United States, she shall be regarded and held liable to be treated as a woman of the town plying her avocation.” Butler’s order was widely construed as a license for rape, and he was condemned by the whole world. Butler had the “manners” of a pig and a deviant.

Krugman celebrates the victory of “a democratic nation” (the North) in his blog. But during the war the North was anything but “democratic”: Lincoln illegally suspended the writ of *Habeas Corpus* and imprisoned tens of thousands of Northern political critics without any due process; shut down hundreds of opposition newspapers; deported Congressman Clement Vallandigham of Ohio for criticizing him; threatened to imprison Chief Justice Roger B. Taney for issuing the (correct) opinion that Lincoln’s suspension of *Habeas Corpus* was unconstitutional; censored all telegraphs; rigged elections; imprisoned duly elected members of the Maryland legislature along with Congressman Henry May of Baltimore and the mayor of Baltimore; illegally orchestrated the secession of West Virginia to give the Republican Party two more U.S. senators; confiscated firearms in the border states in violation of the Second Amendment; and committed a grand act of treason by invading the sovereign states of the South (Article 3, Section 3 of the U.S. Constitution defines treason as “only” levying war *against the states*, or giving aid and comfort to *their* enemies).

Krugman is right about democracy in a sense: Democracy is essentially one big organized act of bullying whereby a larger group bullies a smaller group in order to plunder it with taxes. The “Civil War” proved that whenever a smaller group has finally had enough, and attempts to leave the game, the larger group will resort to anything—even the mass murder of hundreds of thousands and the bombing and burning of entire cities—to get its way. After all, in his first inaugural address Lincoln literally threatened “force,” “invasion,” and “bloodshed” (his exact words) in any state that refused to

pay the federal tariff, which had just been more than doubled two days earlier. He followed through with his threat. This is "the kind of nation I believe in," says Paul Krugman on his blog.

## Grand Old Tyrants

**T**he very first public statement that Abraham Lincoln made after being inaugurated as the sixteenth president was an ironclad defense of slavery: “I have no purpose, directly or indirectly, to interfere with the institution of slavery in the states where it exists. I believe I have no lawful right to do so, and I have no inclination to do so.” He then quoted the Republican Party platform of 1860 that said essentially the same thing; pledged his support for the Fugitive Slave Clause of the Constitution “with no mental reservations”; and supported a proposed constitutional amendment (the “Corwin Amendment”) that would have prohibited the federal government from *ever* interfering with slavery. In fact, it was Lincoln who instructed William Seward to see that the Corwin Amendment made it through the U.S. Senate, which it did (and the House of Representatives as well).

In the same speech, Lincoln promised a military invasion and “bloodshed” in any state that refused to collect the federal tariff on imports, which had just been more than doubled two days before his inauguration. “[T]here needs to be no bloodshed or violence, and there shall be none unless it be forced upon the national authority,” he continued. Thus, mere minutes after taking an oath to protect the constitutional liberties of American citizens, Abraham Lincoln threatened to orchestrate the murder of many of those same citizens.

What on earth was he talking about? What would cause a president to wage war on his own citizens whose liberties he had just pledged to protect? Lincoln explained in the very next sentence: “The power confided to me will be used to hold, occupy, and possess the property and places belonging to the Government and *to collect the duties and imposts*; but beyond what may be necessary for these objects, there will be no invasion, no using force against or among the people anywhere” (emphasis added). He promised to murder American citizens over tax collection.

This was necessary, in the mind of Lincoln, if he was to deliver on what his party elected him to do: to enact a high protective tariff, give away public lands mostly to mining, railroad, and timber corporations, and lavish the railroad corporations, among others, with corporate welfare. This was the old “American System” of Alexander Hamilton, which was endorsed for decades by Lincoln’s Whig Party, and finally the Republicans. The overwhelming majority of Southern congressmen had for decades been ardently opposed to all of these things. But now, they must be forced into it, or so Lincoln thought, for the sake of revenue collection. (At the time, the tariff on imports accounted for more than 90 percent of all federal tax revenues.)

Southerners (as well as Northerners) needed to be forced to pay for the empire of corporate welfare that the Republican Party hoped would keep it in power for decades. (It did—the Republican Party essentially monopolized national politics for the next half century.) That is why there had to be a war, in the minds of Lincoln and the Republican Party. They were perfectly willing to enshrine slavery explicitly in the Constitution, but there would be no compromise over collecting the newly doubled tariff.

This is also why opposition to war in the North had to be brutally repressed, as it was, and a myth of “national unity” invented. Much of the story of how the Republican Party engaged in a Stalinist spasm of political repression is told by historian William Marvel in his book, *Lincoln’s Darkest Year: The War in 1862*. (Marvel is a renowned Lincoln scholar, winner of the Lincoln Prize and the Douglas Southall Freeman Award.)

The Republican Party’s first act of political chicanery was to begin kicking out of the U.S. Senate men like Democratic Senator Jesse Bright of Indiana, who “lacked enthusiasm for Abraham Lincoln’s war against the South,” writes Marvel. Using the excuse that, in the years before the war, Senator Bright “had known and admired [fellow Senator] Jefferson Davis of Mississippi, the Republican Party accused Senator Bright, one of the most senior members of the Senate, of “retroactive treason” and expelled him with a bare two-thirds majority vote.

The *Congressional Globe* propagandized that “only a traitor would advocate peace,” and newspapers all over the North that were openly affiliated with the Republican Party (as was common during that period of time) quoted this statement. As for Northern newspapers that did not support the waging of war on their fellow Americans, the government had already begun to “squellch the most effective . . . criticism by stopping distribution, seizing equipment, and arresting publishers. Unionist mobs had collaborated in that suppression of free speech during the summer of 1861, destroying the offices of antiwar journals and attacking the editors.”

Even “Francis Scott Key’s own grandson understood how dangerous it had become to utter an unpopular opinion in the Land of the Free,” Marvel sarcastically writes. The grandson of the author of “The Star Spangled Banner” was a Baltimore newspaper editor who had been thrown into “the bowels of a coastal fort” without any due process for editorializing against the Lincoln administration’s suppression of free speech.

“The party that dominated the United States Senate intended to formalize the concept that meaningful dissent [to the political agenda of the Republican Party] amounted to treason.” After kicking Senator Bright out of office the leaders of the “Grand Ole Party” then “wished to end their day early in order to prepare for a grand party that had occupied Mary Lincoln’s attention for some weeks.” Marvel writes that White House employees quickly began calling Mrs. Lincoln “the American Queen” who, according to one senator, appeared at the party “looking like she was wearing a flower pot on her head.” Many of the generals, admirals, Supreme Court justices, and foreign counsels who attended the party, writes Marvel, considered Lincoln to be “a vulgar provincial lacking in either sincerity or statesmanlike qualities.”

Without bothering to amend the Constitution, the Republican Party in 1861 invented a brand new definition of “treason.” Treason, to Lincoln and the Republican Party, meant opposition *to them*. This was very different from the actual definition of treason in Article I, Section 3 of the U.S. Constitution: “Treason against the United States shall consist only in levying War against *them*, or in adhering to their Enemies, giving them Aid and Comfort” (emphasis added). As with all of the founding documents, “United States” is in the plural, signifying that the free and independent states (as they are called in the Declaration of Independence) are united in forming a compact of states for their own mutual benefit. The central government was to be *their agent*.

Treason under the Constitution consists of levying war against “*them*,” the states. This of course is exactly what Lincoln and the Republican Party did. Their war on the South was the very definition of treason under the U.S. Constitution. Long before George Orwell’s time, they distorted the meaning of the word to mean exactly the opposite of what the founding fathers intended it to mean. As the perpetrators of treason as defined by the Constitution, they accused *their political opponents*—those who opposed the levying of war” on the states—of treason.

Marvel writes that on his very first day in office as Lincoln’s Secretary of War Edwin Stanton “would exercise a cool, dictatorial demeanor” as he commenced to enforce the new definition of treason. The U.S. government was failing to recruit enough soldiers for its war despite the fact that it was offering enlistment “bounties” of as much as \$415. Despite the totalitarian crackdown on Northern antiwar newspapers, there was still pervasive verbal opposition to the war in Northern cities. Consequently, Stanton “unilaterally abolished” that freedom of speech on August 8, 1862, writes Marvel. Having enacted a policy of military conscription, Stanton “appointed a special judge advocate to deal with dissent and issued instructions for local and federal law officers to imprison anyone who ‘may be engaged, by act, speech, or writing, in discouraging volunteer enlistments, or in any way giving aid and comfort to the enemy . . .’” The vagueness of this order allowed the government to imprison anyone who said anything negative about Lincoln, the Republican Party, or their war on fellow citizens.

“With renewed vigor,” writes Marvel, “U.S. marshals of predominantly Republican pedigree started rounding up malcontents—almost all of them Democrats—on the excuse that their vocal disagreement with presidential policies discouraged men from volunteering.” Any Northern newspaper writers who dared to criticize the “Grand Ole Party” were treated very roughly. “In August of 1861 . . . a mob of Granite State soldiers attacked the editors of a Democratic Concord [New Hampshire] newspaper and destroyed their office.” “On August 14 Dennis Mahony, the Irish editor of the *Dubuque Herald*, was arrested by Iowa’s U.S. marshal, H.M. Hoxie—a crony of Republican governor Samuel Kirkwood. . . . Mahony had been preaching peace for months . . .” “In jail Mahony met David Sheward, his counterpart at the *Constitution and Union*, of Fairfield, Iowa.” These men joined in prison “the editors of Illinois newspapers, some Illinois judges, and a few other celebrity dissidents for the long journey to Washington,” where they were thrown into “the Old Capitol Prison.” Apparently, administration

critics from “The Land of Lincoln” had to be imprisoned in Washington, D.C. where they could be especially carefully watched.

Newspapers affiliated with the Republican Party “crowded over the administration’s latest assault on free speech,” which speaks volumes about the rotten, totalitarian mindset of the scoundrels who ran the Republican Party of the 1860s. Marvel writes of how “prominent Democrats” all throughout the North were jailed for such things as advising voters to vote for peace candidates; laughing at a local “Home Guard” company; or making “saucy” comments about Lincoln.

Even Democrats running for Congress were imprisoned before election day, as was the case of William J. Allen, a “peace Democrat from southern Illinois” who “went to jail in that mid-August orgy of repression because of opinions expressed during a political campaign.” Allen was running for reelection. Many of his fellow Democrats “were not released [from one of Lincoln’s gulags] until after the fall elections.” Some of them languished in prison “until they relinquished . . . the right to sue their arresting officers for false imprisonment.” Thousands of Northern citizens “felt the hand of some sheriff or provost marshal clutching their shoulders” (figuratively speaking), writes Marvel.

Republican Party thugs were not above beatings *and murder* of Northern civilians who dissented from the “Grand Ole Party” line. A group of Republican “volunteers in the town of Troy [Kansas] severely beat a citizen whose political observations they resented,” says Marvel. “Political animosity led to the murder of another man in southeastern Missouri.” The local Republican Party-affiliated newspaper editorialized in favor of the murder, writing that the man “had no right to be disloyal to the government” by advocating peace, equating the Republican Party with “government.” The paper also named other local citizens who would make for “acceptable targets.” Such were the origins of the “Grand Ole Party.”

All of this occurred in just the first few months of the war. During the next several years hundreds of thousands of Northern men would be enslaved by conscription; hundreds of thousands of European mercenaries would be paid to wage war on Americans from the Southern states; hundreds of opposition newspapers would be shut down; a dissenting member of Congress, Clement Vallandigham of Ohio, would be deported; hundreds of draft protesters in New York City would be shot and killed in the streets by Union army soldiers; and the entire Constitution would be ignored.

All of this “antidraft, antiwar, antiadministration sentiment” led the Republican Party to form “secret societies,” writes Marvel, that would produce a

deluge of pro-Republican propaganda for years and years after the war was over. The “Union League” was one such society. One of the things the Republican Party propaganda machine did was to manufacture the myth (i.e., lie) of “national unity” during the war, suggesting that Northerners were united in waging total war on their fellow citizens. The truth is that it was the Republican Party that waged war on the South, not a “united” Northern population. (I have written elsewhere of how there was such a desertion crisis in the Union Army that entire regiments frequently deserted on the eve of battle.) The myth of “national unity” is a Grand Old Lie.

# Fascialism: The New American System

**T**he two worst scourges of humanity in the twentieth century were socialism and fascism. Together, they wrecked much of the world economy because of their shared “fatal conceit” (F.A. Hayek’s term) that government central planners were superior to private property and free markets. Fascist and socialist governments (not that there’s much difference between them) murdered over 100 million of their own citizens, as the sociologist R.J. Rummel has documented (see his book, *Death by Government*), and instigated wars that caused the deaths of millions more.

Incredibly, the two-party duopoly that has long ruled America has adopted *both* fascism and socialism as the defining characteristics of our economic system. Call it Fascialism. It is a recipe for national economic suicide.

## Economic Fascism

Economic fascism as practiced by Italy and Germany in the 1920s and ‘30s allowed private property and private enterprise to exist, but only if it was strictly controlled and regimented by the state so that it would serve “the public interest” and not private interests. The philosophy of German

fascism was expressed in the slogan *Gemeinnutz geht vor Eigennutz*, which means “the common good comes before the private good.” “The Aryan,” Hitler wrote in *Mein Kampf*, “willingly subordinates his own ego to the community and, if the hour demands, even sacrifices it.”

Of course, it is the government that decides what constitutes “the common good.” Is there any doubt that government will now define what constitutes “the common good” in the banking and automobile industries—and in health care once it is fully nationalized?

The philosophy behind Italian fascism was virtually identical. “The fascist conception of life,” Mussolini wrote in *Fascism: Doctrines and Institutions*, “stresses the importance of the State and accepts the individual only in so far as his interests coincide with the State.”

It is remarkable how contemporary economic policy pronouncements are so often identical to those made by early twentieth-century European fascists. Mussolini complained in 1935, for example, that government intervention in the Italian economy was “too diverse, varied, contrasting. There has been . . . intervention, case by case, as the need arises.” His advisor, Fausto Pitigliani, explained that under fascism government regulation would achieve a certain “unity of aim” instead.

This is exactly how the powers that be in Washington, D.C diagnosed the so-called Great Recession: There’s been too *little* financial market regulation, they tell us, and it has been too, well, diverse and contrasting. Thus, they recommended a Super Regulatory Authority that will supposedly regulate, regiment, and control all “systemic risk taking” in the entire economy. The only debate is whether an entirely new agency should be created to achieve this “unity of aim,” or if the Fed—which caused the current economic crisis in the first place—should be given the responsibility.

Government-business “partnerships” were a hallmark of both Italian and German fascism. As Ayn Rand once noted, however, in such “partnerships” government is always the “senior partner.” Government-business “collaboration” was supposedly needed in fascist Italy, explained Fausto Pitigliani in his 1934 book, *The Italian Corporatist State*, because “the principle of private initiative could only be useful in the service of the national interest.” It is this “service of the national interest” that is the intended work of the dozens of “czars” appointed by American presidents.

Italian fascism created one gigantic bailout economy. Italian social critic Gaetano Salvemini wrote in his 1936 book, *Under the Axe of Fascism*,

that “It is the state, i.e., the taxpayer, who has become responsible to private enterprise. In Fascist Italy the state pays for the blunders of private enterprise.” “Profit remained to private initiative,” Salvemini wrote, but “the government added the losses to the taxpayers’ burden. Profit is private and individual. Loss is public and social.” Sound familiar?

Mussolini himself boasted in 1934 that “three quarters of the Italian economic system had been subsidized by government,” Salvemini wrote. The U.S. government is striving to exceed this level of plunder.

## Socialism

In the preface to the 1976 edition of his famous book, *The Road to Serfdom*, F.A. Hayek wrote that when the book was first published in 1944, socialism meant “unambiguously the nationalization of the means of production and the central economic planning which made this necessary.” But by the 1970s “socialism has come to mean chiefly the extensive redistribution of incomes through taxation and the institutions of the welfare state.” Thus, ever since the 1930s the Democratic Party in America has been the party of socialism, with the Republican Party either providing little or no effective opposition or serving as accomplices.

## In Defense of Sedition

Joe Klein of *Time* magazine once went on a network television show and accused Glenn Beck and Sarah Palin of “sedition” because of their criticisms of the Obama administration’s expenditure of trillions of dollars of corporate welfare in the form of bailouts; its Soviet-style nationalization of automobile, banking, student loan, and mortgage industries; its historically wild spending and borrowing binge; its advocacy of socialized medicine; and its plans to tax American capitalism into bankruptcy. Anyone who criticizes such things should be thrown into the Gulag, says Klein. Another talking head on the same television show as Klein screeched that Rush Limbaugh should also be indicted for “sedition” for the “crime” of criticizing King Obama’s extreme socialistic policy agenda.

Sedition, Joe Klein informed us, is a threat to “the authority of the state.” But the key question is: authority *to do what*? Does the American state have unlimited “authority” to do anything statist politicians can dream up? If they can nationalize automobile companies, banks, and the healthcare industry, do they also have the “authority” to nationalize the grocery industry, home building, steel manufacturing, and everything else? Joe Klein obviously believes so. In so doing, he supports the “authority” of a totalitarian state. Opposing totalitarian government is “sedition” according to Joe Klein and his fellow network “news” show talking heads.

The original design of the American government was that the only “authority” the central government was to have was powers delegated to it by the free, independent, and sovereign states in Article 1, Section 8 of the Constitution. All others are the responsibility of the people, respectively, and the states, according to the Tenth Amendment, which Thomas Jefferson considered to be the cornerstone of the document. These powers were delegated to the central government for the benefit of the sovereign states, who appointed the central government as their agent—mostly for issues regarding war and foreign policy—by adopting the Constitution. That’s why treason, as defined by the U.S. Constitution in Article 3, Section 3, is defined as follows: “Treason against the United States, shall consist only in waging War against *them*, or adhering to their Enemies, and giving them Aid and Comfort . . .” As in all the founding documents, “United States” is in the plural, signifying that the free and independent states were united in delegating certain enumerated powers for their own mutual benefit. Thus, “waging War against them” means the states. Waging war against the free and independent states is what constitutes treason under the U.S. Constitution.

As your author wrote in *The Real Lincoln*, the one unequivocal good that came of Lincoln’s war was the abolition of slavery. But the worst thing that came of it—the thing that was the real purpose of the war—was the centralization of virtually all political power in Washington, D.C., and the essential death of the Jeffersonian system of states’ rights or federalism that was the essence of the pre-war Constitution. After 1865, the federal government became the sole decision maker with regard to the limits of its own powers. It exercised this decision-making power through the federal judiciary and, as the Jeffersonians had always warned, it eventually declared that there were, in fact, *no* limits to its powers.

It didn’t take long for the federal government to declare the idea of natural rights, the bedrock of the Jeffersonian philosophy of government, to be null and void. It did this by adopting the income tax in 1913, along with the creation of the vast legalized counterfeiting scheme known as the Federal Reserve. The income tax effectively declares that all earned income is the property of the state, and that the state will inform us from time to time how much of our own income we may keep to live on by setting the income tax rates. The Fed and the income tax made it possible for the government to finance a limitless explosion of statism just four years later with American entry into the world-wide disaster of World War I, which led to the most destructively bloody century in all of human history.

The income tax and the Fed finally centralized all political power in Washington, as it became trivially easy for the central state to conscript millions of men for its wars, spend mind-boggling sums on things like a welfare state and the nationalization of education that have no constitutional authority whatsoever, and to easily bribe any state government that voices the least bit of dissent by threatening to withdraw federal grants to the state. More than half of the American population is bribed and manipulated in a similar manner today as recipients of myriad federal subsidies.

By the 1930s the central state was sick and tired of what it considered to be contemptible constitutional arguments that limited the size and scope of government. FDR condemned the Constitution as the irrelevant scribblings of a lost generation, and advocated massive socialistic government intervention whereby the government would magically “guarantee” everyone a high-paying job, high food prices for farmers, a “decent home,” all the medical care you could want, freedom from fear of old age, sickness, and accidents, and of course, state-funded education. This was the essence of FDR’s childish wish list of an “economic bill of rights.” Of course, government cannot promise anyone anything without also confiscating the income of someone else to pay for it. Nor can it “guarantee” any of FDR’s pit-in-the-sky wish list unless the laws of economics are repealed, which of course they can never be.

Since states’ rights had been obliterated by Lincoln’s war, there was no longer any effective opposition to totalitarian-minded political hacks like FDR. He appointed enough Supreme Court judges to create a situation that, by 1937, the Court was prepared to reverse generations of prior decisions that attempted to enforce the Constitutional constraints on government. And they succeeded: According to Andrew Napalitano, author of *The Constitution in Exile*, not a single federal law was ruled unconstitutional between 1937 and 1995. The legal scholar Bernard Siegan made the same point in *Economic Liberties and the Constitution*.

For generations, Americans have lived under a judicial dictatorship that rubber stamps all expansions of federal power, no matter how at odds they may be with the Constitution itself. The body of “constitutional law” that has developed during this time is nothing more than a bundle of tongue-twisting legalese designed to subvert and destroy any lasting vestiges of constitutional limitations on the powers of the central state.

In short, the government in Washington, D.C. has not been a government by consent since 1865. In response to the declaration by American

citizens residing in the Southern states in 1860–61 that they no longer consented to being governed by Washington, D.C., the U.S. government waged war on the entire civilian population of the South, killing some 350,000 fellow American citizens, which is more Americans than died in all other wars combined. This number includes at least 50,000 civilians. On top of that, Southern cities and towns were burned to the ground, bombed, and plundered. The plundering continued for a decade after the war during the laughingly named “reconstruction” period.

Americans—especially conservatives—delude themselves when they express the view that it might be possible to restore constitutional government. How would this happen? Who would enforce the Constitution? Why would the federal government ever give up its monopoly of constitutional interpretation and return to the pre-1865 world where all three branches of government were often given equal weight in constitutional interpretation, as well as the citizens of the free, independent, and sovereign states? The central state murdered hundreds of thousands of its own citizens in order to achieve this monopoly status, and it will never just give it up.

It is the Washington establishment, which includes its media lapdogs like Joe Klein, that is guilty of sedition. The legitimate “authority” of the state is spelled out in the U.S. Constitution. It is the Washington establishment that has abandoned that legitimate authority and granted to itself essentially unlimited powers. Therefore, there can be nothing more patriotic and “American” than *opposing everything the central state proposes doing* that would expand its scope and powers in any way. Without any kind of constitutional constraints or meaningful citizen control, the federal government is nothing more than another criminal gang, as Murray Rothbard often said. The fact that it is a very large gang does not make it any more legitimate. The TEA Party protesters and all others who oppose the oppression of the central state should ignore the puerile rantings of the Joe Kleins of the world and remind themselves of what Thomas Jefferson wrote in the Declaration of Independence when he said that men

are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and the pursuit of Happiness. — That to secure these rights, Governments are instituted among Men, deriving their just powers from the consent of the governed, — *That whenever any Form of Government becomes destructive of these ends, it is the Right of the People to alter or to abolish it, and to institute new Government . . .* (Emphasis added)

“TEA Party” activists claim that they are Taxed Enough Already. That’s not good enough. If they took their own rhetoric about constitutional government seriously, they would recognize that what is needed is at least a 90 percent *reduction* in federal taxes, not merely being satisfied with being taxed “enough already.”

Since such a tax reduction is not likely to be achieved with the cooperation of the Washington establishment, no matter who is elected president, the only real prospect for success is to take seriously the words of Thomas Jefferson, author of America’s *Declaration of Secession from the British Empire*, and organize numerous peaceful secession movements. Let them have their socialist utopia on the Potomac. The rest of us can watch with great amusement as they ruin their small society, impoverish themselves, and turn into a Third World swamp, which is what Washington, D.C. started out as several hundred years ago.

## Distorting History in Service of the State

**A** “court historian” is someone who produces statist propaganda disguised as “scholarship.” The purpose of the court historian is to provide cover, to pull the wool over the public’s eyes, to make excuses for, and glorify the state and the ruling class. A corollary purpose is to criticize or even demonize the civil society, especially the private enterprise system. In return, court historians are often given privileged positions in academe, government “research grants” to finance their careers, newspaper columns, and are turned into television and radio “celebrities.” They are the propaganda megaphones of the state.

This chapter discusses two exceptionally egregious examples of the attempted rewriting of history to glorify the state—one by one James Loewen, a sociologist associated with the left-wing hate group known as the Southern Poverty Law Center, and another one by Newt Gingrich and historian William Forstchen. Loewen fancies himself as a self-appointed historical truth teller, having published articles and books with a theme of “lies your professors taught you.” He authored a *Washington Post* article on January 9, 2011 entitled “Five Myths about Why the South Seceded” as part of the *Post*’s commemoration of the 150<sup>th</sup> anniversary of the start of the War between the States. Almost everything in the article is historically inaccurate.

In discussing the role of federal tariff policy in creating regional, North/South political tensions during the antebellum period, Loewen refers to the 1828 “Tariff of Abominations,” which led to South Carolina’s Ordinance of Nullification, whereby the state condemned the increase in the average tariff on imports to 48 percent as a blatant act of plunder (mostly at the South’s expense) and refused to collect it at Charleston Harbor. He wrote that “when, after South Carolina demanded the right to nullify federal laws or secede to protest, President Andrew Jackson threatened force.” That much is true. Loewen continued to say that “no state joined the movement, and South Carolina backed down.” That is blatantly false.

Historian Chauncey Boucher wrote in his book, *The Nullification Controversy in South Carolina*, that North Carolina and Alabama joined South Carolina with their legislatures publicly condemning the Tariff of Abominations, while Massachusetts, Ohio, Pennsylvania, Rhode Island, Indiana, and New York, whose legislatures were all heavily influenced by protectionists, issued resolutions in support of plundering the South with protectionist tariffs.

Nor is it correct to say that “South Carolina backed down,” as Loewen wrote. South Carolina and the Jackson administration reached a *compromise* that reduced the tariff rate over the succeeding ten years. They *both* “backed down,” but Loewen misleadingly claims that only South Carolina did so. Court historians have a long and pathetic history of rewriting the history of tax protests in this way. In Loewen’s case, he has a secondary motivation for fibbing about history: He wants Americans to believe that, unlike all other wars in world history, the American “Civil War” had nothing to do with economic conflict. He is a purveyor of the cartoonish theory of American history that Southern racism was the sole cause of the war, which was prosecuted by racially enlightened Republicans from Northern states.

Loewen then spread a mind-boggling falsehood about the role of tariff policy in precipitating the “Civil War.” “Tariffs were not an issue in 1860, and Southern states said nothing about them,” he wrote in the *Post*. “Why would they?, he asked. “Southerners had written the tariff of 1857, under which the nation was functioning. Its rates were lower than at any point since 1816.” Every word of this narrative is false.

A protectionist tariff was a part of the Republican Party platform of 1860, whereas Southerners were such staunch free traders that protectionist tariffs were literally outlawed in the Confederate Constitution (see Marshal DeRosa’s *The Confederate Constitution of 1861*). Lincoln’s official campaign

poster featured pictures of himself and his vice presidential running mate Hannibal Hamlin over the protectionist caption of “Protection for Home Industry.” In a speech delivered in Pittsburgh, Pennsylvania shortly before taking office, Lincoln declared that “no other issue” was more important to the nation than raising the federal tariff rate. He said this as part of the protectionists’ campaign to get President James Buchanan to sign the legislation enacting the Morrill Tariff of 1861, which he did two days before Lincoln’s inauguration. Once the war had commenced, Lincoln announced a naval blockade of the Southern ports and gave only one reason for it: it was his duty, he said, to collect the federal tariff tax.

In his first inaugural address Lincoln announced that it was his duty “to collect the duties and imposts” and that “beyond that” there would not be any “invasion” (his word) or “bloodshed” (his word) in any state. He literally threatened war over tariff collection. Abraham Lincoln was not going to back down to tax protestors from South Carolina or anywhere else, as Andrew Jackson had done. It is undeniable that tariff policy was an extremely important issue to Abraham Lincoln in 1860, contrary to Loewen’s assertion.

The most egregious falsehood spread by Loewen is to say that the tariff that was in existence in 1861 was the 1857 tariff rate, which was in fact the lowest rate of the nineteenth century. The issue was not that tariff rate, but the *Morrill Tariff* rate, which was more *than twice as high* (32.6% vs. 15%). At a time when tariffs accounted for at least 90 percent of all federal tax revenue, the tax rate was more than doubled by the law that passed the U.S. House of Representatives during the 1859–60 legislative session, and then the U.S. Senate in the 1860–61 session, and signed into law on March 2, 1861. The words “Morrill Tariff” do not appear anywhere in Loewen’s *Washington Post* article.

Loewen was also dead wrong when he claimed that Southerners said “nothing” about the tariff prior to the outbreak of the war. Confederate President Jefferson Davis emphasized tariff policy in *his* first inaugural address (delivered in Montgomery, Alabama on February 18, 1861) as much as Lincoln did in his. He said this:

An agricultural people, whose chief interest is the export of a commodity required in every manufacturing country, our true policy is peace, and the freest trade, which our necessities will permit. It is alike our interest, and all those to whom we would sell and from whom we would buy, that there should be the fewest practicable restrictions upon the interchange of commodities.

There can be but little rivalry between ours and any manufacturing or navigating community, such as the Northeastern States of the American union. It must follow, therefore, that a mutual interest would invite good will and kind offices. If, however, passion or the lust of dominion should cloud the judgment or inflame the ambition of those states, we must prepare to meet the emergency . . .

Thus, in Lincoln's first inaugural address he announced that protectionism was the cornerstone of the U.S. government's economic policy, and that he was willing to launch an "invasion" of "any state" that resisted. In Jefferson Davis's first inaugural address he announced that the Confederacy's economic policy was the exact opposite: the "freest trade" possible. When he said in the above quotation that "we must prepare to meet the emergency" he was saying that he knew the North would be willing to go to war over tax collection this time, unlike the Tariff of Abomination crisis some thirty years earlier, and that the South should "prepare" for a possible invasion. And James Loewen would have us believe that no one on either side said anything at all, whatsoever, about the tariff issue in the months leading up to the war.

The rest of Loewen's *Washington Post* article was no more accurate. For example, it is well known that only a very small percentage of Confederate soldiers were slave owners. The obvious question then becomes: why did they fight? They not only did not own slaves, but many of them were yeoman farmers who were harmed by the institution of slavery because the large, slave-owning plantations competed unfairly with them. And many more were deprived of job opportunities in farming because of the fact that much of that work was performed by slaves.

Rather than consulting scholarship on why Confederate soldiers fought, Loewen fabricated a ludicrous answer to the question of why Confederate soldiers who did not own slaves fought: they supposedly expected to magically become wealthy slave plantation owners after the war, he said! This is what passes for historical "scholarship" in the *Washington Post*. If Loewen had read James McPherson's book, *What They Fought For: 1861–1865*, he would know that the average Confederate soldier said in letters home that he was fighting against an aggressive foreign government that was invading his country, bombing and burning his towns, and threatening harm to his family and friends.

Left-wing hate group activists are not the only court historians when it comes to the subject of Lincoln and his war. Neoconservatives consider

“The Myth of Father Abraham” to be an essential ingredient in their warfare state ideology and seem willing to say and write just about anything to perpetuate their mythology. An example of this phenomenon was a February 9, 2009 article on the Web site Newsmax.com by Newt Gingrich and William Forstchen entitled “What Would He Say to Us Today?” The article was yet another rendition of the neocon tactic of suggesting that Abe Lincoln would approve of their political agenda if he were alive today. If “Father Abraham” would approve, how could *anyone* object? Dozens, maybe hundreds, of articles have been written by neocon political activists along the lines of this general theme. (The neocons are not alone in this venture; Mario Cuomo and Harold Holzer wrote an entire book entitled *Lincoln on Democracy* arguing that Lincoln would be a “social democrat,” a.k.a., socialist like them, if he were alive today.)

Gingrich and Forstchen engage in the typical deification of Lincoln by calling the Lincoln Memorial in Washington, D.C. “his throne” that is “modeled after Grecian temples.” This of course is true: King Lincoln does have a Zeus-like appearance sitting there in his D.C. “throne” (although historian Clyde Wilson more accurately described this symbol of the American state as “a corporate lobbyist sitting in an armchair”).

Gingrich and Forstchen call the Lincoln Memorial “our American temple to democracy.” Of course, the American founding fathers feared and even loathed democracy, described by James Madison as “the violence of faction” in *Federalist* #10. The last thing in the world a James Madison or a Thomas Jefferson would have done would have been to support the building of a temple to democracy. The whole purpose of the Constitution, Madison wrote in *Federalist* #10, was to control and restrain democracy, or “the violence of faction.”

In reality the Lincoln Memorial is a temple that celebrates the *destruction* of the Jeffersonian idea that “governments derive their just powers from the consent of the governed.” Such destruction is hardly democratic. It was the South, after all, that no longer consented to being governed by Washington, D.C. in 1861. It was Lincoln and the Republican Party that held the position that government in America was *not* voluntary; that, contrary to Jefferson’s words in the Declaration of Independence, the people do *not* have a right to “alter or abolish” their own government; and that the federal government does have a “right” to invade, murder hundreds of thousands, and bomb and burn entire American cities and towns to the ground to enforce this view.

Gingrich and Fortschen claim that all of this bloodshed, death, mayhem and destruction is how America became “united.” Theirs is a very odd definition of “united” and is more reminiscent of how the *Soviet* Union was “united” than the original American union. If one person holds a gun to another person’s head and asks that person if he agrees with him then, yes, one can say that at least rhetorically the two are “united” in their opinion.

It is a tenet of Anglo-Saxon law that contracts consummated under force or fraud are not legal or legitimate. The same can be said of the American union in the post-1865 era.

Perhaps the biggest whopper told by Gingrich and Fortschen is that Lincoln “was a man of deep abiding faith.” That would be shocking news to Lincoln’s wife and closest friend and law partner, William Herndon, both of whom attested that Lincoln never became a Christian. In preparing his biography of Lincoln Herndon asked Mary Todd Lincoln about this and she said that her late husband “had no faith. . . . He never joined a church [and] . . . he was never a technical Christian” (see Edgar Lee Masters, *Lincoln the Man*, p. 150). This fact is well known by Lincoln scholars despite the absurd statement made by Gingrich and Fortschen. For example, in her book *Team of Rivals*, Doris Kearns-Goodwin wrote at length about the fact that Lincoln was never a believer. The spin that Goodwin placed on this fact was that we should all feel even more sorry for poor old Abe because he must have suffered more than most since he did not believe in an afterlife.

Lincoln’s war was a total war waged on the civilian population of the South as well as the combatants of the Confederate Army. Lincoln knew of every atrocity and is praised by historians for his role in micromanaging the waging of total war on citizens of the Southern states. He rewarded generals like Sherman and Sheridan who did not excel as military strategists but were invaluable to Lincoln as terrorists who murdered civilians, bombed and burned cities and towns populated only by civilians, and looked the other way while their troops stole millions of dollars worth of private property—everything from silverware to livestock. Lincoln was also famous for experimenting with bigger and bigger weapons of mass destruction to be used on American cities like Richmond, Virginia, Atlanta, Georgia, and Charleston, South Carolina, where literally thousands of artillery shells fell in periods of only a few days at times when there was no enemy army present.

Gingrich and Fortschen apparently believed that Americans are completely unaware of these facts when they wrote that Lincoln had “a deep

sense of love and compassion for everyone. He even knelt and prayed with a wounded Confederate soldier in a hospital”; “his eyes filled with pain over the suffering of others”; and he “was known for extreme gentleness to an injured animal.” They provide no references for such outlandish statements, only saying that they come from “stories” (but do not even reveal the sources of the “stories”).

Gingrich and Fortschen also mislead their readers into believing that Lincoln was enlightened on the issue of race by saying that he “was the first American president to invite and socially greet a delegation of African-Americans into the White House.” Lincoln did hold a meeting with a group of free black men in the White House, but it was not the first of such meetings according to Professor Henry Louis Gates of Harvard University. The purpose of the meeting was not to make a statement about racial equality, as the Gingrich/Fortschen article misleadingly implied. Exactly the opposite is true: The purpose of the meeting, which is described in *Lincoln’s Selected Writings and Speeches* in the entry for August 14, 1862, was to urge the free black men to “lead by example” and self-deport themselves out of the U.S. “You and we are different races,” Lincoln sagely observed. “We have between us a broader difference than exists between almost any other two races. . . . This physical difference is a great disadvantage to us both . . . and affords a reason at least why we should be separated. . . . It is better for us both, therefore, to be separate.”

He then urged the men to go to Liberia, stating that there was already a colony of American black people there (established in the early nineteenth century by the American Colonization Society), although most of the original colonists had perished. Lincoln tried to assure the men that such a venture would be advantageous even though most of them would also probably perish from disease or starvation. If they procreated before hand, Lincoln surmised, then someday their descendants would probably outnumber them. The free black men wisely turned down Lincoln’s generous offer to pay for their deportation to Liberia.

The false history of Lincoln and his war has long been used to prop up the idea of “American exceptionalism,” which in turn has become an all-purpose excuse or rationalization for the U.S. government’s imperialistic military adventures around the world.

SECTION 4

# Money and the State



## Central Banking as an Engine of Corruption

**M**uch has been written about the famous debate between Thomas Jefferson and Alexander Hamilton over the constitutionality of America's first central bank, the Bank of the United States (BUS). This was where Jefferson, as secretary of state, enunciated his "strict constructionist" view of the Constitution, making his case to President George Washington that since a national bank was not one of the powers specifically delegated by the states to the central government, and since the idea was explicitly rejected by the constitutional convention, a central bank is unconstitutional. Treasury Secretary Hamilton notoriously responded by inventing the notion of "implied" as opposed to explicit, delegated powers in the Constitution.

George Washington signed legislation creating the BUS not because of the strength of Hamilton's argument but because of a shady political deal. The nation's capital was being relocated from New York to Virginia, and Washington wanted the border of the new District of Columbia to abut his property at Mount Vernon. In return for redrawing the district's border (presumably enhancing his property value), Washington signed the Federalists' legislation creating the BUS.

America's first central bank was borne of a corrupt political deal, but that particular act of political chicanery pales in comparison to what Hamilton and his fellow nationalists really had in mind for the country.

As Murray Rothbard wrote in *The Mystery of Banking*, Hamilton and his political compatriots, especially the politically-connected defense contractor Robert Morris, wanted

to reimpose in the new United States a system of mercantilism and big government similar to that in Great Britain, against which the colonists had rebelled. The object was to have a strong central government, particularly a strong president or king as chief executive, built up by high taxes and heavy public debt.

An especially important part of what Rothbard called “the Morris scheme” was “to organize and head a central bank, to provide cheap credit and expanded money for himself and his allies.”

Hamilton was essentially Robert Morris’s plant in the Washington administration whose assignment was to create a British-style “mercantilist” economic system that would primarily benefit plutocrats like Morris at the expense of nearly everyone else. As explained by historian Douglas Adair, an editor of *The Federalist Papers*:

[W]ith devious brilliance, Hamilton set out, by a program of class legislation, to unite the propertied interests of the eastern seaboard into a cohesive administration party, while at the same time he attempted to make the executive dominant over the Congress by a lavish use of the spoils system. In carrying out his scheme . . . Hamilton transformed every financial transaction of the Treasury Department into an orgy of speculation and graft in which selected senators, congressmen, and certain of their richer constituents throughout the nation participated.

What Professor Adair is talking about here is how Hamilton went about nationalizing the old government debt. New government bonds were issued and the old debt was to be cashed out at face value. This plan immediately became public knowledge in New York City among all the political insiders in and around the government, but news of it “spread only slowly, via horseback and sailing vessel, to the rest of the country,” wrote John Steele Gordon in his book, *Hamilton’s Blessing*.

Thus, a tremendous arbitrage opportunity was created for the New York/Philadelphia political insiders like Robert Morris and his business and political associates, including many members of Congress. In his classic book, *Jefferson and Hamilton*, historian Claude Bowers described how many members of Congress and other political insiders took advantage of hundreds of unsuspecting Revolutionary War veterans who had been partly paid for their service in government bonds by purchasing the

bonds from them for as little as two percent of par value. As Bowers described the scene,

expresses with very large sums of money on their way to North Carolina for purposes of speculation . . . splashed and bumped over wretched winter roads. . . . Two fast-sailing vessels, chartered by a member of Congress . . . were ploughing the waters southward on a similar mission.

Many members of Congress became instant millionaires, according to Bowers. Robert Morris is said to have made millions on the scheme, and Hamilton himself participated in it.

Upon observing this Hamiltonian caper, Jefferson came to the conclusion that Hamilton was intentionally creating a system of institutionalized corruption in order to purchase the political support in Congress for his party's big-government mercantilist agenda of protectionist tariffs, corporate welfare, and central banking. In a February 4, 1818 essay written long after Hamilton's 1804 death, Jefferson claimed that "Hamilton's system had two objects. 1<sup>st</sup> as a puzzle, to exclude popular understanding & inquiry. 2ndly, as a machine for the corruption of the legislature." With regard to the corruption accusation, Jefferson explained that Hamilton had

Avowed the opinion that man could be governed by one of two motives only, force or interest: force he observed, in this country, was out of the question; and the interests therefore of the members [of Congress] must be laid hold of, to keep the legislature in unison with the executive. And with grief and shame it must be acknowledged that his machine was not without effect. . . . Some members [of Congress] were found sordid enough to bend their duty to their interests, and to look after personal, rather than public good.

"Men thus enriched by the dexterity of a leader [like Hamilton]," Jefferson wrote, "would follow of course the chief who was leading them to fortune, and thus become the zealous instruments of all his enterprises."

But the problem facing Hamilton, Jefferson believed, was that the political support which he "purchased" with the public debt arbitrage scam was only temporary. "It would be lost with the loss [by retirement or death] of the individual members [of Congress] whom it had enriched." Therefore, Jefferson reasoned, "some engine of influence more permanent must be contrived." This permanent engine of "influence" or corruption, he said, "was the Bank of the U.S." A central bank, once established, would instantly create a political constituency behind it and would be

difficult to destroy. Jefferson feared that it could become a permanent engine of political bribery and corruption in the service of expanding the size and scope of government beyond the bounds of the Constitution. Thomas Jefferson concluded that “Hamilton was not only a monarchist, but for monarchy bottomed on corruption,” with a central bank being the centerpiece of the kind of corrupt regime that Hamilton aspired to create.

Jefferson came to this conclusion based on Hamilton’s behavior, and on his words as well. In his February 4, 1818 essay Jefferson recalled a personal conversation involving himself, Hamilton, Secretary of War Henry Knox, President John Adams, and Attorney General Edmund Randolph in 1791, the year the BUS came into being. He recalled how President Adams said of the British constitution, “purge that constitution of its corruption, and give to its popular branch equality of representation, and it would be the most perfect constitution ever devised by the wit of man.”

Hamilton then objected to this statement by saying: “Purge it of its corruption, and give to its popular branch equality of representation, & it would become an impracticable government; as it stands at present, with all its supposed defects, it is the most perfect government which ever existed.”

Thus, to the Machiavellian Hamilton the existence of corruption in the British government was a good thing, not a bad thing, for it helped to centralize political power in the executive. Hamilton was “so bewitched & perverted by the British example,” Jefferson wrote, “as to be under thoro’ conviction that corruption was essential to the government of a nation.” And the creation of a central bank was the essential ingredient of such corruption.

## CHAPTER 31

# States' Rights vs. Monetary Monopoly

Americans were not always slaves to government bureaucracy in the way that they are today. One of the best historical examples of this is how Americans once utilized the Jeffersonian states' rights tradition of nullification and interposition to assist President Andrew Jackson in his battle to defund the Second Bank of the United States, the successor of the first Bank of the United States (BUS).

The BUS originally had a twenty-year charter (beginning in 1791) that was not renewed by Congress because the bank did exactly what the Jeffersonians feared it would do: It created 71 percent price inflation in its first five years, generated boom-and-bust cycles, and corrupted politics. It was resurrected by Congress in 1816 to ostensibly help to monetize the war debt related to the War of 1812.

In the same year that the BUS was resurrected—1816—Indiana and Illinois amended their state constitutions to prohibit the BUS from establishing branches within their jurisdictions. North Carolina, Georgia, and Maryland joined in the battle by imposing heavy taxes on BUS branches that existed within their borders. Their obvious intent was to tax them out of business. The whole story is told by James J. Kilpatrick in his book, *The Sovereign States: Notes of a Citizen of Virginia*.

Understanding that such taxes could destroy the BUS the federal government brought suit in Maryland (*McCulloch vs. Maryland, 1819*), confident that Chief Justice John Marshall, a pro-bank nationalist who idolized

Alexander Hamilton, would rule in its favor. And so he did, famously coining the slogan, “the power to tax is the power to destroy.”

But that was back in the day when the opinion of the Supreme Court was viewed as just the opinion of the Supreme Court and not a commandment handed down from God, as it is today. In the 1820s Americans were still of the opinion that there were *three* branches of government, not just one (the judicial), and that all three branches should have an equal say on constitutional issues, as should the citizens of the sovereign states through acts of nullification, if need be. The Constitution, after all, is silent on the subject of who is to be “the” arbiter of constitutionality and certainly does not give sole responsibility to the federal judiciary.

Despite Marshall’s opinion that the BUS was constitutional and that state taxes on it were illegitimate, numerous states continued to harass the bank. Ohio imposed a \$50,000 per year tax on each of two branches of the BUS. When the bank refused to pay up the Ohio state auditor ordered a deputy, one John L. Harper, to collect the tax. As Kilpatrick explains it:

[O]n the morning of September 17, Harper made one last request for voluntary payment. When this was denied, he leaped over the counter, strode into the bank vaults, and helped himself to \$100,000 in paper and specie. He turned this over to a deputy . . . stuffing this considerable hoard into a small trunk, with which the party thoughtfully had come equipped.

The Ohio legislature considered Marshall’s opinion, and the existence of a national bank, to be a dire threat to citizen sovereignty and a dangerous precedent for all Americans, not just the people of Ohio. It issued a proclamation that: “To acquiesce in such an encroachment upon the privileges and authority of the States, without an effort to defend them, would be an act of treachery to the State itself, and to all the states that compose the American Union.”

The Ohio state legislature stated that it was aware of the “theory” that the Supreme Court should be the lone interpreter of the Constitution—a theory that was invented by John Marshall, by the way. But it also declared that “to this doctrine . . . they can never give their assent,” writes Kilpatrick. The Ohio legislature quoted Jefferson’s Kentucky Resolutions to bolster its case that each party to a constitutional contract has an equal right to interpret the Constitution for themselves. John Marshall was wrong, they said, and considered themselves to be under no obligation to acquiesce in his “ruling.”

The Ohio legislature then promised to return the \$100,000 if the BUS left the state. If not, it threatened a law that would forbid “the keepers of our jails” from imprisoning any person “committed at the suit of the Bank of the United States”; prohibit Ohio courts from “taking acknowledgements of conveyance where the Bank is a party”; and forbade “our courts, justices of peace, judges and grand juries from taking any cognizance of any wrong alleged to have been committed upon any species of property owned by the Bank.” It then denounced the Supreme Court and Chief Justice John Marshall for their violation of the constitution.

The BUS fought back, having federal marshals arrest and imprison the Ohio state treasurer. While in prison the keys to the state government’s vaults were physically taken from him and federal bureaucrats helped themselves to the \$100,000. This infuriated Ohioans even more, and they continued to oppose the Bank, as did many other states. Kentucky and Connecticut adopted the Ohio position on the Bank; South Carolina imposed a special tax on stockholders in the Bank within the state; the New York and New Hampshire legislatures enacted resolutions urging that the bank not be re-chartered. As James J. Kilpatrick concluded:

In the face of this unrelenting warfare, the bank could not survive. Withdrawal of the public deposits began in August of 1833, under Jackson’s order; and when Pennsylvania Governor Wolf, who had been one of the Bank’s staunchest supporters, denounced the institution in March of 1834, public opinion was fatally influenced against the Bank. The Pennsylvania senate adopted fresh resolutions urging that the Bank not be re-chartered. The following month, the United States House of Representatives adopted the same view, and the Bank’s days came to an end.

President Andrew Jackson is generally credited with vetoing the re-charter of the Second Bank of the United States, which he certainly did. But he had a lot of help in his long, drawn-out political battle, and that help came from the people of the free, independent, and sovereign states who opposed any move in the direction of granting a monetary monopoly to the politicians in Washington, D.C.

## How Central Banking Hides the Costs of War

**L**udwig von Mises believed that the generation of price inflation by central banks was an “indispensable means of militarism” because it renders the repercussions of war much less obvious. “War weariness” would set in much more quickly if wars were financed by direct taxation instead.

American politicians have always resorted to the legalized counterfeiting of central banking to finance wars, the most expensive of all government programs. If citizens had a clearer picture of the true costs of war they would be more inclined to oppose aggressive intervention and to force all wars to quicker conclusions.

Government can finance war (and everything else) by only three methods: taxes, debt, and the printing of money. Taxes are the most visible and painful, followed by debt finance, which crowds out private borrowing, drives up interest rates, and imposes the double burden of principal and interest on taxpayers. Money creation, on the other hand, makes war seem costless to the average citizen, who is more likely to blame the higher prices caused by the central bank on “greedy corporations” than their real source, the state.

As a general rule, the longer a war lasts, the more centrally planned and governmentally-controlled the entire economy becomes. And it remains so to some degree after the war has ended. War is the health of the state, as Randolph Bourne famously declared, and the growth of the state means

a decline in liberty and prosperity. As Robert Higgs wrote in *Crisis and Leviathan*, for example, the effects of World War I were massive government collusion with organized special-interest groups; the nationalization or *de-facto* nationalization of the ocean shipping and railroad industries; the increased federal government intrusion in labor and capital markets, communications, and agriculture; and enduring changes in constitutional doctrines regarding military conscription and civil liberties, especially freedom of speech.

Inflationary war finance often leads to calls for price controls, which inflict even greater damage on the private enterprise system by generating shortages of goods and services. The state uses the excuse of shortages that it created to grant itself even more powers to allocate the shortages however it sees fit. Inflating the currency as a method of war finance is often a first step in the adoption of what is essentially economic fascism.

Paper and printing is said to have been invented in China, but American politicians were probably the first to use government paper money. It was adopted by the colonial government of Massachusetts in 1690. As Murray Rothbard wrote in *A History of Money and Banking in the United States*, the Massachusetts government at that time was accustomed to launching “plundering expeditions” against the prosperous French in Quebec. Some of the loot was typically used to pay mercenary soldiers, but when some of the plundering expeditions failed to come up with any plunder and the mercenary soldiers threatened mutiny, the Massachusetts government printed 7,000 British pounds in paper notes to pay them. The government promised to redeem the paper money in gold or silver, but took *forty years* to do so. Meanwhile, the public was so suspicious of the notes that they depreciated by 40 percent in the first year after they were issued.

By 1740 every colony except for Virginia had followed Massachusetts’ lead in issuing fiat paper money. The results were dramatic price inflation, a depreciated currency, and boom-and-bust cycles. During the American Revolution a form of centralized banking was adopted when the Continental Congress issued the “Continental” in 1775. Because it was not backed by anything of value, the Continental depreciated so severely that it was virtually worthless by 1781. “Not worth a continental” became a popular slang phrase.

Some of the states attempted to deal with the inflation caused by the massive printing of Continentals with price-control laws. The predictable effect (to students of economics) was shortages so severe that George Washington’s army almost starved in Pennsylvania. The situation became

so desperate that the Continental Congress issued a resolution on June 4, 1778 urging all the states to abolish their price control laws.

Within three months the army was well provided for as a result of this change in policy, wrote Robert Scheuttinger and Eamon Butler in *Forty Centuries of Wage and Price Controls: How Not to Fight Inflation*.

Despite the economic calamities caused by America's first foray into centralized control of the money supply, at the end of the Revolutionary War the nation's first central bank—the Bank of North America—was created, with defense contractor/Congressman Robert Morris implanted as its president. Centralized banking might have been ruinous for the general public, but political insiders like Morris profited handsomely. The bank was given a monopoly license to issue paper currency, and it used most of its newly created money for loans to the federal government. In so doing, it inflated its currency so rapidly that within one year the market lost all confidence in the bank and it was privatized.

Alexander Hamilton was the real founding father of central banking, as the Federal Reserve Board declares in one of its publications. His Bank of the United States, established in 1791, was partly intended to finance “sudden emergencies” like war, in Hamilton's own words. The BUS was not re-chartered in 1811 when its original charter ran out, but the federal government still devised a way to monetize the war debt. It encouraged the creation of dozens of private banks, then in 1814 declared a “suspension of specie payment.” That is, banks were not required to redeem their paper currency in gold or silver. Thus, under the direction of the U.S. Congress, banks were encouraged to inflate their currencies at will for two-and-a-half years. Price inflation during the war years averaged 35 percent.

To help pay off the war debt the BUS was re-chartered in January of 1817 and empowered to issue a national paper currency, purchase public debt, and receive deposits of U.S. Treasury funds. Murray Rothbard explained the politics of the re-chartering of the BUS in his *History of Money and Banking in the United States*:

The Second Bank of the United States was pushed through Congress . . . particularly by Secretary of the Treasury Alexander J. Dallas . . . a wealthy Philadelphia lawyer [and] close friend, counsel, and financial associate of Philadelphia merchant and banker Stephen Girard, reputedly one of the two wealthiest men in the country. . . . Girard was the largest stockholder of the First Bank of the United States, and during the War of 1812 Girard became a very heavy investor in the war debt of the federal

government. . . . [A]s a way to unload his public debt, Girard began to agitate for a new Bank of the United States.

The Second BUS “launched a spectacular inflation of money and credit,” wrote Rothbard, coupled with a heavy dose of bank fraud. It promptly created “the Panic of 1819,” the first real Depression in American history where large-scale unemployment in cities appeared for the first time. Rothbard noted in his book, *The Panic of 1819*, that unemployment in the manufacturing of handicrafts in Philadelphia fell from 9,700 persons in 1815 to only 2,100 in 1819.

After President Andrew Jackson vetoed the re-chartering of the Second BUS, the Bank became defunct, but the nationalist advocates of central planning through central banking never gave up. They finally succeeded during the Lincoln administration with the Legal Tender Act of 1862, which empowered the secretary of the Treasury to issue paper “greenbacks” that were not redeemable in gold or silver during the war years. The National Currency Acts of 1863 and 1864 created a system of nationally chartered banks that could issue bank notes supplied to them by the new comptroller of the currency. The Acts also placed a 10n percent tax on competing state bank notes to drive them out of business and establish a federal monetary monopoly.

The predictable effect was significant price inflation with greenback dollars devalued to the extent that they were worth only 35 cents in gold after one year. All of the negative economic effect of inflation—devaluation of private wealth, unfair redistribution of income from creditors to debtors, and hindrance to rational economic calculation—damaged the Northern war effort, but not by as much as that in the South. The North funded most of the Civil War with public borrowing; the South funded most of the war by printing Confederate dollars. Consequently, price inflation in the Confederacy averaged more than 2,200 percent per year.

The Federal Reserve Board was finally created in 1913 and was instrumental in financing America’s disastrous and futile participation in World War I. The Fed did not just print greenbacks, as was the case during the Civil War. It printed enough money to purchase more than \$4 billion in government bonds that were used to finance the war. The amount of money in circulation doubled between 1914, the first year of the Fed’s existence, and 1920. The price level also doubled during those same years, generating an enormous hidden tax on American taxpayers by cutting the value of privately-held wealth in half and depressing real wages.

The boom created by the Fed's war financing inevitably caused a bust—the Depression of 1920. The first year of the Depression of 1920 was even worse than the first year of The Great Depression a decade later. Gross Domestic Product declined by 24 percent from 1920 to 1921, while the number of unemployed Americans more than doubled, from 2.1 million to 4.9 million. The Great Depression of 1920 lasted only that one year, however, thanks to President Warren Harding's inspired policy of cutting both government spending and taxes very dramatically.

In all the wars that followed World War II central banking has inflicted essentially the same kind of damage on American society: price inflation, economic chaos, reduced real wages, price controls and other destabilizing and impoverishing government controls and regulations, and ideological attacks on capitalism rather than on the real culprit, the Fed.

Adam Smith recognized the advantage of financing wars with taxes as opposed to public debt when he wrote in *The Wealth of Nations* that “Wars would in general be more speedily concluded, and less wantonly undertaken” with tax financing. “The people feeling, during the continuance of the war, the complete burden of it, would soon grow weary of it, and the government, in order to humor them, would not be under the necessity of carrying it on longer than it was necessary to do so.”

Central bank inflation renders the costs of war even more invisible than debt financing does and is therefore even more disastrous from the perspective of the taxpaying public.

## How the Fed Creates Unemployment

**M**onetary policy under the direction of the Federal Reserve Board has a history of creating *and* destroying jobs. The reason for this is that the Fed, like all other central banks, has always been a generator of boom-and-bust cycles in the economy. Why this is so is explained in three classic treatises in Austrian economics: *The Theory of Money and Credit* by Ludwig von Mises; *Monetary Theory and the Trade Cycle* by F.A. Hayek; and *Prices and Production* by Hayek. Murray Rothbard's *America's Great Depression* also contains a lucid exposition of the Austrian business cycle theory. Hayek was awarded the Nobel Prize in Economics in 1974 for this work, among other things.

When the Fed expands the money supply it not only is prone to creating price inflation, but it also sows the seeds of recession or depression by artificially lowering interest rates, which can ignite a false or unsustainable economic “boom period.” Lower interest rates induce people to consume more and save less. But increased savings and the subsequent business investment that it finances is what fuels economic growth and job creation.

Lowered interest rates and wider availability of credit caused by the Fed's expansionary monetary policy causes businesses to invest more in (mostly long-term) capital projects, primarily in real estate in the early 2000s boom period. There is an accompanying expansion of employment in those industries. But since the lower interest rates are caused by the Fed's expansion of the money supply and not an increase in savings by the public

(i.e., in the free market), businesses that have invested in long-term capital projects eventually discover that there is not enough consumer demand to justify their investments. (The reduced savings in the past means that consumer demand is weaker in the future). This is when the “bust” occurs.

The economic damage done by the boom-and-bust policies of the Fed occur in the boom period when resources are misallocated in the ways described here. The “bust” period is actually a necessary cure for the economic miscalculations that have occurred, as businesses liquidate their unsound investments and begin to make decisions on realistic, market-based interest rates. Prices and wages must return to reality as well in order for a genuine economic recovery to occur.

Government policies that bail out businesses that have made these bad investment decisions will only delay or prohibit economic recovery while encouraging more of such behavior in the future (the “moral hazard problem”). This is how short recessions can be turned into much longer ones, or depressions. Worse yet is when the Fed creates even more monetary inflation in response to the problems it caused by inflating the money supply in the first place. In doing so it may set off another boom-and-bust cycle.

It is obvious that the artificially low interest rates that were the official policy of the Greenspan Fed beginning in 2000 created an unsustainable boom in the housing market. Thousands of new jobs were in fact created—and then destroyed—giving an updated meaning to economist Joseph Schumpeter’s phrase “creative destruction.” Many Americans who obtained jobs and pursued careers in housing construction and related industries realized that those jobs and careers were not sustainable after all. They were fooled by the Fed. Thus, the Fed was not only responsible for causing the high unemployment rates (officially as high as 10 percent, but as high as 17 percent if “discouraged workers” are counted as unemployed), but also a mismatch in labor markets. That is, the skills that all the people in these industries acquired were no longer in demand; they lost their jobs and were forced to retool and re-educate themselves, or languish in unemployment or on welfare.

The Fed has been generating boom-and-bust cycles from its inception in 1914. Total bank deposits more than doubled from 1914 to 1920 (thanks mostly to the Fed’s financing of U.S. participation in World War I) and created a false boom that turned into a bust with the Depression of 1920 where GDP fell by 24 percent from 1920 to 1921, and the number of unemployed Americans more than doubled, from 2.1 million to 4.9 million (as documented by Richard Vedder and Lowell Galloway in their book, *Out of*

*Work*). This was a more severe depression than the first year of the Great Depression a decade later.

Murray Rothbard demonstrated in his book, *America's Great Depression*, that it was not restrictive monetary policy from 1929 to 1932 that fueled the Great Depression, as Milton Friedman and Anna Schwartz argued in their treatise, *A Monetary History of the United States*. Rather, it was the *expansionary* monetary practice of the Fed during the 1920s that generated another boom-and-bust cycle, with the bust being the primary cause of the Great Depression.

Giving the Fed the responsibility of maintaining low unemployment makes as much sense as giving arsonists the responsibility of fighting and building house fires.

## The Myth of a “Libertarian” Fed

One of the more absurd spectacles during the “Great Recession” was how so many commentators blamed the crash on a Fed that was “too libertarian” and not enough of a central planning board. Business historian John Steele Gordon wrote in the *Wall Street Journal* that the cause of the crash was the “baleful” influence of Thomas Jefferson and his anti-central banking views that still live on today. Wall Street stockbroker Henry Kaufman wrote in the *Financial Times* that “libertarian dogma” had led the Fed astray. This comment was repeated by many others who appeared to assume that: (1) Since Fed Chairman Alan Greenspan had been a protégé of Ayn Rand’s forty years earlier; and (2) since Ayn Rand is associated with *laissez faire*; then (3) the Fed under Greenspan’s chairmanship was not in any way involved in regulating financial markets or in orchestrating boom-and-bust cycles with its monetary policies.

A bigger absurdity has never been published in such august publications as the *Wall Street Journal* and *Financial Times*. All one needs to do to realize this is to search the Web for a Fed publication entitled “The Federal Reserve System: Purposes and Functions.” In addition to recklessly manipulating the money supply and causing boom-and-bust cycles that sometimes result in Great Depressions, the Fed has “supervisory and regulatory authority over a wide range of financial institutions and activities.”

Those functions were not put on hold in any way during the Greenspan chairmanship.

- Bank holding companies
- State-chartered banks
- Foreign branches of member banks
- Edge and agreement corporations
- U.S. state-licensed branches, agencies, and representative offices of foreign banks
- National banks
- Savings banks
- Nonbank subsidiaries of bank holding companies
- Thrift holding companies
- Financial reporting procedures
- Accounting policies of banks
- Business “continuity” in case of economic emergencies
- Consumer protection laws
- Securities dealings of banks
- Information technology used by banks
- Foreign investment by banks
- Foreign lending by banks
- Branch banking
- Bank mergers and acquisitions
- Who may own a bank
- Capital “adequacy standards”
- Extensions of credit for the purchase of securities
- Equal opportunity lending
- Mortgage disclosure information
- Reserve requirements
- Electronic funds transfer

- Interbank liabilities
- Community Reinvestment Act sub-prime lending demands
- All international banking operations
- Consumer leasing
- Privacy of consumer financial information
- Payments on demand deposits
- Fair Credit reporting
- Transactions between member banks and their affiliates
- Truth in lending
- Truth in savings

All of this massive financial market regulation and regimentation was in full force during the Greenspan era. None of it could be even remotely considered to be “libertarian” or “Jeffersonian” in any way. The Fed is a central planning agency, and the above list is a list of some of its hundreds of central planning tools. Like all attempts at central planning, it only destabilizes the economy while propping up the politically-connected plutocracy with cheap credit, bailouts, and other forms of corporate welfare.

## The Myth of the “Independent” Fed

**E**ver since its founding in 1913 the Fed has portrayed itself as an “independent” agency operated by selfless public servants striving to centrally plan the U.S. economy through monetary policy. In reality, however, a non-political government enterprise is as likely as a cat that barks like a dog or a dog that meows. Yet the myth of the “independent” and apolitical Fed persists and the economics textbooks have helped perpetuate the myth for decades.

From 1948 until the 1980s the biggest-selling principles of economics textbook was *Economics* by Paul Samuelson. It sold over four million copies and was used to teach generations of college students their basic economics. There were a few exceptions, but most other textbooks were mere clones of Samuelson’s book, amplifying Samuelson’s influence on the economic thinking of the average, college-educated person. The 1989 edition of Samuelson’s text, co-authored with William Nordhaus, said this about the Fed:

The Federal Reserve’s goals are steady growth in national output and low unemployment. Its sworn enemy is inflation. If aggregate demand is excessive, so that prices are being bid up, the Federal Reserve may want to slow the growth of the money supply, thereby slowing aggregate demand and output growth. If unemployment is high and business languishing, the Fed may consider increasing the money supply, thereby raising aggregate

demand and augmenting output growth. In a nutshell, this is the function of central banking, which is an essential part of macro-economic management in all mixed economies.

Perhaps the second largest-selling economics textbook during the Samuelson era was *Economics* by Campbell McConnell, which echoed Samuelson's view of Fed bureaucrats being selfless (and quite ingenious if not omniscient) public servants faithfully pursuing "the public interest."

Because it is a public body, the decisions of the Board of Governors [of the Fed] are made in what it perceives to be the public interest . . . the Federal Reserve Banks are not guided by the profit motive, but rather, they pursue those measures which the Board of Governors recommends . . . . The fundamental objective of monetary policy is to assist the economy in achieving a full employment, noninflationary level of total output.

Note that the Fed is evaluated by these textbook authors according to its supposed good intentions. There was never any serious analysis of the Fed's actual record in achieving these glorious objectives in either of these textbooks. One would look in vain, for example, to find a chart showing that by 1989 decades of price inflation caused by the Fed had caused the U.S. dollar to lose some 90 percent of its value since the Fed's inception in 1913. The above statements are mere wishes, not statement of facts. Like all government institutions, the Fed has always been manipulated by politicians for their benefit, first and foremost, not for the benefit of the "public interest," which in any event is impossible to define and exists nowhere but in the heads of naïve, state-worshipping commentators like Campbell McConnell.

## The Fed as a Political Tool

When the Fed was founded it was controlled by two groups, the Governors' Conference, composed of the twelve regional Fed bank presidents, and the seven-member Federal Reserve Board in Washington. In 1935 the Fed was reorganized to concentrate nearly all power in Washington with the Federal Reserve Board. President Franklin Roosevelt succeeded in "packing" the Federal Reserve Board just as he attempted to "pack" the U.S. Supreme Court after the Court ruled the First New Deal (1933–1935) to be unconstitutional. So much for an "independent" and apolitical Fed.

Roosevelt appointed Marriner Eccles, a strong supporter of irresponsible deficit spending and inflationary finance, as Fed Chairman. Eccles

supported such fiscally-irresponsible policies even before John Maynard Keynes provided an academic rationalization of them with his famous book, *The General Theory of Employment, Interest and Money*, first published in 1936. The Roosevelt Fed was most likely controlled during those years by Eccles's political mentor, Treasury Secretary Henry Morgenthau, Jr., and thus ultimately Roosevelt himself.

It should be obvious to anyone that presidents are always inclined to politicize the "independent" Fed with their appointment powers: they will appoint as Fed chairmen people whom they believe will promote policies that are to their liking and, most importantly, will help them remain in office. Congress also has a hand in the inherent politicization of the Fed by letting presidents know whether or not it will support and vote for the president's appointee.

A history of Fed politicization was published in the April 1978 edition of the academic *Journal of Monetary Economics* by economist Robert Weintraub. Weintraub showed how the Fed fundamentally shifted its monetary courses in 1953, 1961, 1969, 1974, and 1977—all years in which the presidency changed hands. Fed policy always changes to accommodate presidential preferences, for Fed Chairmen must do so if they wish to be reappointed.

For example, President Eisenhower let it be known in public speeches that he wanted slower growth of the money supply. The money supply grew by only 1.73 percent during his administration, the lowest rate in a decade. Then President Kennedy announced publicly that he advocated faster monetary growth. From January 1961 to November 1963 the basic money supply grew by 2.31 percent.

President Lyndon Johnson demanded even faster monetary growth to help finance his expansion of the welfare state coupled with an expansion of the warfare state with the Vietnam War. Money supply growth more than doubled to 5 percent during the Johnson administration as the Fed accommodated his wishes just as it had done with his predecessors. These wildly-varying rates of monetary growth all occurred under the same Fed chairman, William McChesney Martin, who obviously was more interested in pleasing his political masters than in implementing an independent and consistent monetary policy. Ironically, during this time economist Milton Friedman and his "Chicago School" colleagues became famous for advocating a "monetary rule" whereby the money supply would grow annually by a fixed percentage. It is ironic because Friedman and his Chicago School colleagues prided themselves as being astute political analysts as well as

good technical economists. Indeed, Friedman's colleague George Stigler was awarded the Nobel Prize in economics for, among other reasons, his research in the economic analysis of governmental behavior. With such a reputation as students of politics as well as economics, one would think that Friedman would have recognized the folly of believing in an apolitical Fed that could ever implement his "monetary rule."

William McChesney Martin's successor, Arthur Burns, was such a staunch supporter of President Richard Nixon's that he lost all professional credibility by endorsing Nixon's disastrous wage and price controls (a gimmick that Nixon thought would help his reelection chances but which is universally condemned by academic economists). Even though his staff informed him in the Fall of 1972 that the money supply was forecast to grow by an extremely inflationary 10.5 percent in the third quarter of that election year, Burns saw to it that the money supply grew even faster than that. The growth rate of the money supply in 1972 was the fastest for any one year in the post World War II era up to that point and helped reelect Richard Nixon. This was an example of what economists call the "political business cycle"—the phenomena whereby monetary and fiscal policy are used to pump up the economy temporarily just before a national election to give the public a perception of increased prosperity in hopes that they will vote for the incumbent politicians.

When President Ford called for slower growth in response to the price inflation that was ignited by the Burns Fed under President Nixon, the Fed complied with a 4.7 percent monetary growth rate. Then when Democratic President Jimmy Carter publicly announced his wishes for faster monetary growth, Burns once again complied by stepping up the growth rate to 8.5 percent annually. Carter did not reappoint Burns, but the Fed tried to help Carter get reelected just as it had assisted Nixon by pumping up the money supply at an annual rate of 16.2 percent in the five months preceding the 1980 presidential election according to Robert Weintraub's research.

President Reagan personally met with Fed Chairman Paul Volcker to let Volcker know that he would support slower monetary growth to deal with the inflation rate that was in the 13 percent range at the time. Volcker dutifully complied and his successor, Alan Greenspan, developed the reputation of being perhaps the most "accommodating" (to presidents) Fed chairman of all time. As Robert Weintraub warned, a Fed chairman who ignores the publicly-stated wishes of a president does so at his own peril.

Politicians do not always pressure Fed chairmen to assist with their reelections alone and by themselves. They are often doing the bidding of all the special-interest groups of the welfare/warfare state that benefit from government spending programs financed through money creation and price inflation (which is usually blamed on “greedy corporations”). These special-interest groups, in turn, provide votes and campaign “contributions” for the politicians. As economist Robert J. Gordon of Northwestern University wrote in the academic *Journal of Law and Economics* in 1975 in an article about the “demand for inflation,” the acceleration of monetary growth (and subsequent price inflation) “are not thrust upon society by capricious or self-serving government, but rather represent the vote-maximizing response of government to the political pressure exerted by potential beneficiaries of inflation.”

The Fed plays politics with Congress and the executive branch in other ways as well. Writing in the *Journal of Monetary Economics* in 1980, economist Edward Kane described how the Fed sometimes volunteers to function as a political scapegoat for politicians, in return for being allowed to amass a huge slush fund by earning interest income from the government securities that it purchases from its open-market operations. As Kane wrote:

Whenever monetary policies are popular, incumbents can claim that their influence was crucial in their adaptation. On the other hand, when monetary policies prove unpopular, they can blame everything on a stubborn Federal Reserve and claim further that things would have been worse if they had not pressed Fed officials at every opportunity.

The myth of the “independent Fed” is a smokescreen that is intended to keep the public in the dark about the true functions of the Fed as a financier of the political careers of congressional and executive branch incumbents and of the welfare/warfare state that enhances and consolidates their power. The talk by economists about how the Fed supposedly promotes economic stability is flatly contradicted by the Fed’s historical record of failure to stabilize either prices or unemployment. It is uninformed hokum at best and intentionally-crafted propaganda at worst.

# Why the Government is Responsible for the Sub-Prime Mortgage Meltdown

**T**he hordes of mortgage defaults and foreclosures that occurred in the “sub-prime” housing market during the “Great Recession” was the direct result of the Fed’s “easy money” policy along with thirty years of government policy that forced mortgage lenders to make bad loans to un-creditworthy borrowers. When the Greenspan Fed pursued the policy of keeping interest rates as close as possible to zero in the wake of the sharp stock market decline at the turn of the century, the banking system inevitably responded by extending more and more mortgage loans to marginally-qualified borrowers.

When interest rates were higher and were not artificially lowered by the Fed, banks lent money for houses according to the creditworthiness of the borrowers. But when interest rates are artificially lowered by the Fed a whole new class of potential borrowers is added, namely, people with poor or below-average credit ratings who become just barely qualified for mortgage loans as a result of the lower interest rates, which translate into lower monthly loan payments. Many thousands of these marginal borrowers defaulted once the recession hit and their incomes dwindled. Others who had taken out adjustable rate mortgages found that, since they were always on

the precipice of not being able to make their monthly payments, the small increase in interest rates that occurred caused them to default.

In addition to the Fed's monetary policies stimulating the unsustainable sub-prime mortgage market, the government's 1977 Community Reinvestment Act (CRA) also played a prominent role. This Carter administration law compelled banks to make mortgage loans to low-income borrowers and to what supporters of the law call "communities of color" that they believe will have trouble acquiring mortgage loans based on traditional economic criteria, i.e., they are economically unqualified to borrow money to buy a house.

The original proponents of the CRA were the hardcore, extreme leftists who supported the Carter administration, especially such "neighborhood organizations" as "ACORN" (Association of Community Organizations for Reform Now). Barack Obama worked as a lawyer and "community organizer" for ACORN after leaving Harvard Law School.

So-called "community groups" like ACORN benefit *themselves* from the CRA through a process that sounds a lot like legalized extortion. The CRA is enforced by four federal government agencies: the Fed, the Comptroller of the Currency, the Office of Thrift Supervision, and the Federal Deposit Insurance Corporation. The law is set up so that any proposed bank merger, branch expansion, or branch creation can be postponed or cancelled by any of these four bureaucracies if a CRA "protest" is issued by a "community group" like ACORN. This can cost banks great sums of money and the "community groups" use this concern by the banks as leverage to enrich themselves. They demand that the banks give *them* millions (and sometimes billions) of dollars along with promises to make additional millions (or billions) in bad loans to unqualified, sub-prime borrowers in return for a withdrawal of the protest.

A man named Bruce Marks (pronounced like "Marx") became quite notorious as a Boston "community organizer" from pressuring banks in that city to earmark literally billions of dollars to his "Neighborhood Assistance Corporation of America." He once boasted to the *New York Times* that he had "won" commitments from banks as a result of CRA protests totaling \$3.8 billion. That was just one "community group" in one city.

As a result of the CRA banks in every city in America were forced to hold a portfolio of bad loans. In order to compensate themselves for this additional systemic risk imposed on them by the Fed, many banks increased lending fees associated with mortgage loans, forcing qualified borrowers to subsidize some of their losses from the CRA-inspired bad

loans. They also did what banks have always done—charge higher interest rates for the inherently riskier, sub-prime loans.

The community groups screamed that such practices were discriminatory and “predatory” and lobbied for anti-predatory lending laws that would prohibit such fees. They succeeded in many states, forcing banks to “eat” the losses from the sub-prime loans.

A sort of “smoking gun” in this entire CRA charade is an influential Boston Fed publication entitled “Closing the Gap: A Guide to Equal Opportunity Lending.” There is a gap, you see, between the lending abilities of: (a) people who have enough income to afford a mortgage loan of a certain amount; and (b) those who do not have enough income to qualify for the same loan. Of course, by this criterion there is also an automobile gap, a grocery gap, a two-week vacation gap, etc. The Boston Fed study threatens to use the coercive powers of the state to close the “housing gap” by stepping up pressures on mortgage lenders so that they would make orders of magnitude more bad loans to unqualified borrowers.

In addition to making more bad loans, the Fed urged banks to make more use of racial hiring quotas in their hiring decisions, presumably under the theory that minority loan officers would be more inclined to sign off on more of these bad loans to fellow racial minorities.

The Boston Fed claimed that its document was only offering “lending guidelines,” but it is very clear that failure to obey the Fed’s “guidelines” could lead to serious financial penalties for any mortgage lender. The report stated in bold letters that

Failure to comply with the Equal Credit Opportunity Act or Regulation B can subject a financial institution to civil liability for actual and punitive damages in individual or class actions. Liability for punitive damages can be as much as \$10,000 in individual actions and the lesser of \$500,000 or 1 percent of the creditor’s net worth in class actions.

*All* mortgage lenders—banks, independent mortgage companies, etc.—were told that they needed to pay close attention to “such laws and regulations as the Equal Credit Opportunity Act (Regulation B), the Fair Housing Act, the Home Mortgage Disclosure Act (Regulation C), and the Community Reinvestment Act.” A “conscientious [bank] Board will recognize the potential liability associated with noncompliance.”

The Fed instructed mortgage lenders to ignore traditional measures of creditworthiness when it came to “minority and low-income consumers.”

Traditional underwriting standards were said to contain “arbitrary or unreasonable measures of creditworthiness” such as proof of income. Instead, lenders were instructed to adopt “special standards” of lending that were supposedly “appropriate to the economic culture of urban, lower-income, and non-traditional consumers.” For example, traditional underwriting standards take into consideration such things as age, location, and condition of a house, but these should be abandoned according to the Fed when it comes to minority and low-income borrowers.

Traditional ratios of mortgage payments to monthly income should also be ignored, instructed the Fed. But not to worry: The Fed also promised mortgage lenders that the risk associated with making billions of dollars of bad loans to unqualified borrowers would be erased because Fannie Mae and Freddie Mac would purchase the loans from them and then bundle and “securitize” them for sale on “the secondary market” for mortgages.

Of course, the Fed also instructed mortgage lenders that “lack of credit history” should also be ignored when it comes to minority and low-income borrowers. “Successful participation in credit counseling” is an adequate substitute for an actual credit history, said the Fed.

For “normal” borrowers, shopping around for a dishonest property appraiser who cooks the books to accommodate his clients involves criminal penalties. But not for the Fed’s mascots—minority and low-income borrowers. If a “sub-prime” borrower has a property appraisal problem that might hold up his loan, then the Fed will gladly hope to find “another experienced appraiser” who would presumably cook the books for the sub-prime borrower.

Having generated the prospect for a banking crisis by forcing billions of dollars of bad loans on mortgage lenders in the name of increasing home ownership, the government sought to prevent such a crisis through the “magic” of “securitization.” Beginning in the mid-1990s Fannie Mae and Freddie Mac were instructed by Congress to step up the purchasing of CRA loans from mortgage lenders, bundling them, and selling them as “securities” on so-called secondary markets.

Fed Chairman Ben Bernanke boasted of the alleged wisdom and moral superiority of this policy in a March 30, 2007 speech entitled “The Community Reinvestment Act: Its Evolution and New Challenges.” The speech was part of the government’s celebration of the thirtieth anniversary of the Act. According to Bernanke,

Securitization of affordable housing loans expanded, as did the secondary market for these loans, in part reflecting a 1992 law

that required the government-sponsored enterprises, Fannie Mae and Freddie Mac, to devote a large percentage of their activities to meeting affordable housing goals.

In addition to the 1992 law that Bernanke refers to here, the 1994 Riegle-Neal Interstate Banking and Branching Efficiency Act loosened up the regulatory barriers to bank mergers, which greatly enhanced the clout and bank accounts of the leftist “community groups” like ACORN. As Bernanke went on to explain: “[A]dvocacy groups increasingly used the public comment process to protest bank applications on CRA grounds.” There was, in other words, an explosion of the type of legalized extortion activity that the CRA was always intended to generate. Not surprisingly, “banks began to devote more resources to their CRA programs,” said Bernanke.

That’s not all. In 1995 the U.S. Treasury Department decided that the government itself should get directly involved in the bad-loan-to-unqualified-borrowers business by using billions of taxpayer dollars to capitalize so-called “Community Development Financial Institutions” that would lend directly to “sub-prime” borrowers. It was also at this point—1995—that the government, with the Fed as its enforcement arm, began pressuring banks to abandon the traditional loan qualification criteria for low-income and minority borrowers, such as savings and credit history, income verification, and the size of the loan relative to monthly income.

By 2003 one financial institution, Countrywide Bank, had made so many CRA loans—in excess of \$600 billion worth—that the Fannie Mae Foundation gave Countrywide a special award and publicly held the company out as a role model for all other banks. Countrywide filed for bankruptcy shortly thereafter, drowning in an ocean of bad CRA loans.

SECTION 5

# Workers and Unions



# The Political Economy of Government Employee Unions

**A**n important reason why so many state and local governments in the U.S. seem to be in a perpetual state of financial crisis with their politicians constantly scheming to raise hidden (and not-so-hidden) taxes is that they provide most of their so-called “services” through unionized government-run monopolies.

Government employee unions have vastly more power than do private-sector unions because the entities they work for are mostly monopolies. When the employees of a grocery store, for example, go on strike and shut down the store or grocery chain, consumers can shop elsewhere, and the grocery store management is perfectly free to hire replacement workers. In contrast, when a city teachers’ or garbage truck drivers union goes on strike, there is no school or garbage collection as long as the strike goes on. This gives the government union enormous bargaining power as elected officials must then deal with the rabid complaints of voters about the absence of schools or garbage collection and are pressured to quickly give in to the union’s demands.

In addition, government school teachers often are tenured after only two or three years and civil service regulations make it extremely costly, if not impossible, to hire replacement workers. Thus, when government bureaucrats go on strike they have the ability to completely shut down the entire “industry” that they work in indefinitely. This is the primary reason

why the expenses of state and local governments have skyrocketed in recent decades.

For decades, researchers have noted that the more money that is spent per pupil in the government schools, the worse is the performance of the students. Similar outcomes are prevalent in all other areas of government. As economist Milton Friedman once wrote, government bureaucracies—especially unionized ones—are like economic black holes where increased “inputs” (i.e., money spent on government programs) lead to declining “outputs” (i.e., student performance, poverty, etc.). The more that is spent on government schools, the less educated are the students. The more that is spent on welfare, the more poverty there is, and so on. This is the exact opposite of normal economic life in the free market whereby increased inputs lead to *more* and better products and services, not less.

There is no market feedback mechanism in government that rewards product improvement (with profits) and cost cutting while punishing (with losses) cost over-runs and declining product or service quality, for there are no profits and losses in an accounting sense in government. In fact, the incentives are perverse in government: The worse government bureaucracies perform, the *more* money they typically get for their budgets after having made the excuse that their poor performance is not inherent, but only caused by not enough money.

There are many studies in the economics literature showing that government bureaucrats are paid higher salaries and benefits than are their equally-educated private-sector counterparts. The enormous power of government employee unions effectively transfers the power to tax from voters to the unions and is therefore patently undemocratic. Because government employee unions can so easily force elected officials to raise taxes to meet their “demands,” it is they, and not the voters, who control the rate of taxation. They are the beneficiaries of a particular form of taxation without representation (not that taxation *with* representation is any better). This is why some states have laws prohibiting strikes by government employee unions.

Politicians are caught in a political bind by government employee unions: If they cave in to their wage demands and raise taxes to finance the demands, then they increase the chance of being kicked out of office in the next election by angry taxpayers. The “solution” to this dilemma has long been to offer government employee unions moderate wage increases but spectacular pension promises. This allows the politicians to pander to the

unions while deferring the costs to the future, long after they have moved on to higher office or retired from politics.

Government employee unions are not even primarily interested in the well-being of union members but of the union itself as an organization. The union bosses run the unions for their own personal benefit, primarily. Consequently, they use civil service regulations as a tool to protect the job of every last government bureaucrat no matter how incompetent or derelict he is. Fewer government bureaucrats means lower union dues and diminished prospects for extravagant salaries and perks for the union bosses. This is why government employee unions always challenge in court (or threaten to) the attempted dismissal of all bureaucrats, sometimes even ones who are accused of criminal behavior.

Firing an incompetent government school teacher, for example, can take months or years of legal wrangling. Politicians discovered many years ago that the more convenient strategy is to actually reward the incompetent bureaucrat with a higher-paying administrative job that the incompetent employee will gladly accept. That solves the problem of parents who complain that their childrens' math teacher cannot do math while eliminating the possibility of a lawsuit by the union. That is why government school administrative offices are bloated bureaucratic monstrosities filled with teachers who can't teach but who are given the responsibilities of "administering" the entire school system instead. No private school could survive under such a perverse system.

Government employee unions are also champions of "featherbedding"—the hoary union practice of forcing employers to hire more than the number of people necessary to do the job. If this occurs in the private sector, the higher wage costs will make the firm less profitable or cause it to go bankrupt because there is competition. No such thing happens in government monopolies. Featherbedding is a "win-win" strategy for politicians and bureaucrats but a source of plunder of the taxpayers. The unions collect even more union dues while the politicians get to take credit for handing out more patronage jobs. The taxpayers get higher tax bills.

Every government employee union is a political machine that lobbies relentlessly for higher taxes, increased government spending, more featherbedding, and more pension promises while demonizing hesitant taxpayers as uncaring enemies of children, the elderly, widows and orphans, the poor, etc. It is the old socialist trick that Frédéric Bastiat wrote about in his famous book, *The Law*. The unions portray advocates of school privatization not as legitimate critics of a failed system, for example, but as haters

of children. They treat critics of the welfare state not as people who are concerned about how the welfare state has destroyed work incentives and decimated families, but as haters of the poor.

Unionized, government-run monopolies have turned Americans into the servants rather than the masters of their governments. They have provided shoddier and shoddier “services” for more and more money, year in and year out. They are textbook examples of the failures of socialism and should be abolished. Any services that they provide for which there is an actual demand can be provided with superior quality and lower costs by private, competitive markets.

## The Inherent Violence of Unions

Imagine starting up a coffee shop that becomes successful and profitable. Then imagine that, as is par for the course in competitive markets, competing coffee shops pop up and begin competing for your customers with lower prices. You respond by attempting to murder the competitors, assaulting them and their employees with knives, baseball bats, clubs and fists, vandalizing their cars and places of business, setting fire to their buildings, spiking their coffee stores with rat poison, throwing rocks at them as they leave their coffee shops, and even dynamiting their buildings.

Would such practices be considered to be a part of the peaceful free-market economy? Of course not; the above-mentioned acts are pure thug-gery and criminality. They are also among the inherent defining characteristics of the American union movement.

A basic understanding of elementary labor economics, and of the history of unionism, explains why violence has always been an *inherent* feature of private-sector unions. Historically, the main “weapon” that unions have employed to push wages above competitive rates through individual, employee/employer bargaining has been the strike or strike threat. But in order for a strike to be effective, and for unions to have any relevance at all to workers, some form of violence and coercion must be employed to keep competing replacement workers from the labor market. As explained by Dr. Morgan Reynolds, a former chief economist at the U.S. Department of Labor, in his book *Power and Privilege: Labor Unions in America*:

A union's problem is painfully obvious: organized strikers must shut down the enterprise, close the market to everyone else—uncooperative workers, union members, disenchanted former strikers, and employers—in order to force wages and working conditions above free-market rates. If too many individuals defy the strikers . . . then unionists often resort to force. Unionists ultimately cannot impose noncompetitive wage rates . . . unless they can prevent employers from hiring consenting adults on terms that are mutually satisfactory. Unions must actively interfere with freedom of trade in labor markets in order to deliver on their promises.

Thus, strikes—and unions in general—represent a conflict between unionized and non-unionized labor, not between “labor and management.” According to Reynolds, among the tactics that unions have traditionally employed against non-union workers, who they describe as “scabs” and “rats,” are mass picketing, insults, threats, throwing rocks and bottles at them, car chasing, abusive phone calls, physical assaults, property destruction, and even murder.

Union violence is in fact far worse than Reynolds's description of it. In 1983 the Industrial Research Unit of the Wharton School at the University of Pennsylvania published a 540-page book entitled *Union Violence: The Record and the Response by Courts, Legislatures, and the NLRB* by Professors Armand J. Thieblot, Jr. and Thomas R. Haggard. The book notes that employers have also resorted to violence in labor disputes, but that does not mean that two wrongs make a right. There have been books written about employer violence; Thieblot and Haggard document union violence which, as Reynolds has said, is *inherent* in labor unions.

Surveying newspaper accounts and judicial records for a period of several decades, the authors write that the accounts of union violence are

full of examples of murder, assault with intent to kill, destruction of property, arson, sabotage, mayhem, shooting, stabbing, beating, stoning, dynamiting, intimidating, threatening—in short, physical, verbal, and psychological abuse of every sort.

The police and the judicial system often look the other way when unions are the perpetrators of violence and property destruction. They do this because the police are unionized themselves, and consider striking workers to be their “union brothers.” And the judicial system is just as inefficient and corrupt in dealing with union violence as it is in dealing with anything else.

Thieblot and Haggard explain why violence and coercion are inherent features of unionism: they are used as an organizing tool; to engender fear and compliance with union demands; as a bargaining device; as an attention getter that they hope will generate pressure for a settlement in their favor; as an enforcement mechanism to keep strikers in line; as a warning to employers who might consider contracting with non-union companies; as a means of preventing non-union companies from working during strikes; and as a means of generating fear in general, just like any criminal gang would in order to intimidate any potential competitors.

Thieblot and Haggard surveyed hundreds of National Labor Relations Board cases and thousands of other judicial documents and newspaper accounts of union violence over several decades and concluded that “judging from the listings, violence seems to be an inherent part of labor relations and the collective bargaining process, or at least its use is widely distributed. The 2,598 incidents in the data base involve 131 different unions.” The overall purpose of the violence, they further conclude, is “to attain union objectives through the blatant and often unpunished use of force and coercion.”

## The False Ideological Foundation of Unionism

**L**udwig von Mises wrote in his treatise, *Human Action*, that the main ideological foundation of labor unionism, and of government labor policy that is based on it, consists of such “garbled ideas” as the myth that employers have “superior bargaining power” over workers.

In labor markets competition among entrepreneurs assures that there is a close association between worker compensation and the marginal productivity of labor. More precisely, compensation is determined by the workers’ “marginal revenue product,” which is the multiple of marginal physical product—how many physical goods or services the worker produces in a given time period—and the final price paid by consumers for those articles.

Workers therefore become more valuable to employers if their marginal productivity increases, which is caused by capital investment by employers (which makes labor more productive and hence more valuable), technological improvements which are usually the result of employer investments in research and development, and improved human capital, which is the result of education, training, experience, and learning of all sorts.

Workers also become more valuable to employers if say, consumer demand is strong, which drives up the price of the good or service they work at producing. This increases their marginal revenue product as well, since the demand for labor is a “derived demand,” being derived from the consumer demand for the goods and services that the labor is used to produce.

If an employer attempts to exploit some or all of his employees, in a competitive, capitalistic labor market he will merely create a profit opportunity for his rivals, thereby harming his own business. If an employee's marginal revenue product is say, \$500 per week but he or she is paid only \$200 per week, then it will pay competing entrepreneurs to hire that worker away for \$300, then for \$400, or higher, because they will still be earning a profit by doing so. As Mises wrote in *Human Action*, "There will be people eager to take advantage of the margin between the prevailing wage rate and the marginal productivity of labor. Their demand for labor will bring wage rates back to the height conditioned by labor's marginal productivity."

Even if some employers do exploit their employees by paying them less than their marginal revenue product, it is not at all clear that this would primarily benefit the employer, if it benefited them at all. Product market competition may well force them to pass on these cost savings to consumers in the form of lower prices, which would actually benefit wage earners by increasing their real wages.

The only conceivable way that the exploitation of workers could work is if there was a universal cartel of employers that operated an ironclad cartel void of cheating by cartel members, whereby all the employers agreed to pay exploitative wages. The only known instance of such a scenario—and of universal worker exploitation—was socialism, where the state was the monopoly employer. It has never occurred—and could not ever occur—under capitalism because of the well-known cheating proclivities of cartel members. "It has been demonstrated that at no time and at no place in the unhampered market economy can the existence of such cartels be discovered," Mises wrote in *Human Action*.

Proponents of the "capitalists have superior bargaining power" fable also embrace the fallacy that "labor" is homogenous. Mises explained the significance of this as well:

What is sold and bought on the labor market is not "labor in general," but definite specific labor suitable to render definite services. Each entrepreneur is in search of workers who are fitted to accomplish those specific tasks which he needs for the execution of his plans. He must withdraw these specialists from the employments in which they happen to work at the moment. The only means he has to achieve this is to offer them higher pay. Every innovation which an entrepreneur plans . . . requires the employment of workers hitherto engaged somewhere else.

In reality, union representation often harms many workers, contrary to the assertions of the “superior bargaining power” fallacy. For one thing, unions can only benefit some of their members—the ones who are not priced out of their jobs by above-market, unionized wage rates. Other union members, typically those with the least job experience and seniority, will lose their jobs. As they seek work in other areas, including the non-union work force, they will tend to depress wages there. In general, virtually all gains by unionized workers come at the expense of non-union workers.

A general consequence of unionization is a reduction in the dispersion of wages as the wages paid to the most productive workers are dragged down toward the median while the wages of the least productive workers are pushed up in excess of their marginal productivity levels. Unionization therefore penalizes the hardest-working and the most ambitious while subsidizing the less productive and ambitious workers. This is one among many reasons why employers sometimes go to great lengths to avoid unionization: rewarding mediocrity and penalizing superior work performance is a recipe for business failure.

# Markets, Not Unions, Give Us Leisure and Safety on the Job

**I**n *Human Action* Ludwig von Mises wrote that, in his time, labor unions had always been the primary source of anti-capitalistic propaganda. Your author was reminded of this by a bumper sticker that read: “The Union Movement: The People Who Brought You the Weekend.”

In reality, the average work week had been declining for generations before unions began lobbying for maximum-hour legislation. The halving of the average work week from 61 hours in 1870 to around 35 hours today (according to the U.S. Department of Labor) was caused by capitalism, not unionism. As Mises explained: “In the capitalist society there prevails a tendency toward a steady increase in the per capita quota of capital invested. . . . Consequently, the marginal productivity of labor, wage rates, and the wage earners’ standard of living tend to rise continually.”

Of course, this is only true of a capitalist economy where private property, free markets, and entrepreneurship and economic freedom prevail. The steady rise in living standards in capitalistic countries is due primarily to the benefits of entrepreneurial risk taking and investment, technological advance, and a better-educated workforce (no thanks to government schools, which have progressively *dumbed down* the American population). Labor unions routinely take credit for all of this while pursuing policies that impede the very institutions of capitalism that are the cause of their own prosperity and their very existence.

The shorter work week is a capitalist invention because as capital investment causes the marginal productivity of labor to increase over time, less labor is required to produce the same level of output. Or, the same effort can produce more output. As competition becomes more intense, especially in the age of “globalization,” employers compete for the best employees by offering them better pay and shorter hours. Those employers who did not offer shorter work weeks were compelled by the forces of competition to offer higher compensating wages or become uncompetitive in the labor market.

Capitalistic competition is also the main reason for the reduction and, in some societies, elimination of child labor. Young people originally left the farms to work in harsh factory conditions because it was a matter of survival for them and their families. But as workers became better paid—thanks to capital investment and subsequent productivity improvements—more and more people could afford to keep their children home and in school. Union-backed legislation prohibiting child labor came long after the decline in child labor had already commenced.

Moreover, child labor laws were always motivated by a desire on the part of unions to kick young workers, who did not belong to unions, out of their jobs, not to “protect” them. In parts of the Third World today, the alternative to child labor is begging, crime, child prostitution, or starvation and homelessness. Nothing is more hypocritical than labor unions advocating child labor laws while pretending to be motivated by the well-being of children. They are motivated by a desire to monopolize the labor force with unionized labor at the expense of young, non-union workers.

Unions also boast of having championed safety regulation by the Occupational Safety and Health Administration (OSHA) over the past three decades. The American workplace has indeed become safer over the past century, but this was also due to the forces of competitive capitalism, not union-inspired legislation or regulation.

An unsafe or dangerous workplace is costly to employers because they must pay a compensating difference (i.e., a higher wage) to attract workers. Employers therefore have a powerful financial interest in improving workplace safety, especially in manufacturing industries where wages often comprise the majority of total costs. In addition, employers must bear the costs of lost work, retraining new employees, and government-imposed workman’s compensation whenever there is an accident on the job. Not to mention the threat of expensive lawsuits.

Investments in technology, from air-conditioned farm tractors to the robots used in automobile factories, have also made the workplace safer. Unions have *opposed* many types of such safety-improving technology on the grounds that it supposedly “destroys jobs.”

Unions have long been in the forefront of lobbying efforts to increase the regulation and taxation of businesses, i.e., of capital. Regulation and taxation hamper the market economy, reduce the rate of return on capital investment, divert managerial attention away from management and in the direction of filling out government paperwork, and consequently makes everyone—including unionists—worse off economically. Everyone except for the government bureaucrats whose paychecks are derived from such regulatory regimentation, that is.

The slower productivity growth that is caused by union-supported regulation and taxation of business leads to slower growth of output in the economy, which in turn causes prices in many industries to be higher than they would otherwise be. All of this is harmful to the “workers” who unions claim to “represent” by reducing their real wages. Anti-capitalist propaganda is also anti-worker propaganda.

## The Union Conspiracy Against Walmart Employees

**B**eginning in the 1990s it became an article of faith among countless college students (and many others) that Walmart was an evil institution that no decent person should ever do business with. Guest speakers appeared on campuses all throughout America to denounce Walmart's alleged oppression of the poor and the working class. It was all a part of a union-organized smear campaign directed mainly at non-union Walmart *employees*. It is part of an attempt to either pressure Walmart to unionize or to destroy it as a low-priced competitor to higher priced, unionized stores.

The seemingly never-ending propaganda campaign against Walmart is what is known as a “corporate campaign” in the academic literature on labor unions. There are very few strikes by unions these days, since striking workers can so easily be replaced by replacement workers. So-called “corporate campaigning” has taken the place of strikes as labor unions’ weapon of choice.

There are several rationales for corporate campaigns. For one, they are a way of unionizing a workforce without involving the workers, who may not wish to be unionized. The idea is to use every means possible to impose costs on a company and scare away its customers with negative propaganda, portraying the company as some kind of social outlaw. One tactic is to issue thousands of written complaints about the company to regulators, who must then investigate the complaints, forcing the company to spend huge

sums on legal fees. The union will also issue press releases about how many complaints have been made about the company, never mentioning that it—the union—was the source of the contrived complaints! This can cost a company a large portion of its customers if the publicity is bad enough. In the 1990s a corporate campaign against another non-union seller of groceries, Food Lion, caused the grocery chain to shut down dozens of stores. The stores were subsequently reopened after customers discovered that the United Food and Commercial Workers' Union's (UFCW) slanders against Food Lion were untrue.

In the state of Maryland the demonization of Walmart by the UFCW gave the state legislature enough “cover” to pass a law forcing Walmart—but no other corporation operating in the state—to increase the amount of health insurance that it provides for its employees.

The ultimate goal of corporate campaigns, such as the one waged against Walmart, is to get the company to sign a union contract without ever involving the employees, a process that labor union scholars call “pushbutton unionism.”

The UFCW has been at the forefront of the corporate campaign against Walmart because Walmart's grocery prices are significantly lower than all of the unionized grocery stores. The “problem” facing the UFCW is that as more and more customers shop at Walmart for groceries, employment in the grocery industry will also shift from the higher-priced, unionized grocery chains to non-union Walmart, causing the union a loss of membership and, most importantly, a decline in the union dues revenues that are necessary to pay the exorbitant salaries and perks of the union bosses.

## How “Sweatshops” Help the Poor

One of the oldest myths about capitalism is the notion that factories that offer the poor higher wages to lure them off the streets (and lives of begging, stealing, prostitution, or worse) or away from back-breaking farm labor somehow impoverishes and exploits them. They are said to work in “sweatshops” for “subsistence wages.” That was the Marxist-inspired claim made by socialists in the nineteenth century, and it is still made today by various neo-Marxists, most of whom have never themselves performed manual labor and experienced breaking a sweat while working.

The greed and selfishness of unions in this generations-long, anti-capitalistic crusade has always been transparent: Unions cannot exist without somehow prohibiting competition by non-union labor; hence the demonization of non-union factories as “sweatshops.”

American unions are not the least bit concerned with the plight of the poor in Third World countries. They are concerned about the financial health of their union organizations. If the unions had their way, the workers in Third World “sweatshops” operated by American corporations would all be thrown out of work and forced to survive on begging, stealing, or worse. This is the “moral high ground” that union propaganda has created on college campuses all across America where they have instigated “anti-sweatshop” campaigns, seminars, and protests.

The fraudulent nature of the anti-sweatshop campaign was revealed in a 2007 article in the *Journal of Labor Research* by economists Ben Powell and David Skarbek who presented the results of a survey of “sweatshops” in eleven Third World countries. In nine of the eleven countries, “sweatshop” wages in foreign-owned factories located there were higher than the average local wage. In Honduras, where almost half of the working population lives on \$2/day, “sweatshops” paid more than *six times* that amount—\$13.10/day. “Sweatshop” wages were more than double the national average of wages in Cambodia, Haiti, Nicaragua, and Honduras according to Powell and Skarbek.

It is never the workers in countries like Honduras who complain about the existence of a non-union factory that offers them an immediate 500 percent pay increase. The people benefit as consumers as well as workers in such situations, since there are also more (and cheaper) consumer goods sold in their countries. Capital investment of this sort is infinitely superior to the alternative of “foreign aid.” So-called foreign aid is always a government-to-government transfer of funds that empowers the state in the recipient countries, even when the state is a corrupt and oppressive regime. Market-based capital investment is always far superior to politicized capital reallocation.

Foreign investment in the Third World also has the potential of transferring business knowledge to countries where it previously did not exist. It is not just technology that is transferred, but knowledge about business practices and the entire culture of capitalism and wealth creation. Without it no nation can make progress against poverty.

The existence of foreign-owned factories in poor countries creates what economists call “agglomeration economies.” The location of a factory will cause many businesses of all types to sprout all around the factory to serve the factory itself as input suppliers and to serve the employees as well (with restaurants, etc.). Thus, it is not just factory jobs that are created. A successful investment in a poor country will also signal to other potential investors that there is a stable environment for investment there, which can lead to even more investment, job creation, and greater prosperity.

Capital investment by foreign investors in poor countries will also cause wages to rise there by increasing the marginal productivity of labor. Discouraging such investment, which is the goal of the anti-sweatshop movement, will do the opposite and cause wages to stagnate or decline.

One of the strongest virtues of the existence of “sweatshops” in the Third World is that they weaken the power of American unions. With few

exceptions, unions have been at the forefront of anti-capitalist ideology and supporters of growth-stifling government interventionism. Thus, the weaker they become, the better off all American workers will be.

The best way of supporting the Third World poor as a single individual is to purchase more of the products produced by the capitalist enterprises that have located there.

SECTION 6

**Truth and Lies about Markets**



## The Truth about the “Robber Barons”

**T**he late nineteenth century is often referred to as the time of the “robber barons.” It is a staple of history books to attach this derogatory phrase to such figures as John D. Rockefeller, Cornelius Vanderbilt, and the nineteenth-century railroad operators such as Grenville Dodge, Leland Stanford, Henry Villard, James J. Hill, and others. To most historians writing on this period, these entrepreneurs committed thinly veiled acts of larceny to enrich themselves at the expense of their customers. Once again we see the image of the greedy, exploitative capitalist, but in many cases this is a distortion of history.

As common as it is to speak of “robber barons,” most who use that term are confused about the role of capitalism in the American economy and fail to make an important distinction—the distinction between what might be called a market entrepreneur and a political entrepreneur. A pure market entrepreneur, or capitalist, succeeds financially by selling a newer, better, and/or less expensive product on the free market without any government subsidies, direct or indirect. The key to his success as a capitalist is his ability to please the consumer, for in a capitalist society the consumer ultimately calls the economic shots. By contrast, a *political entrepreneur* succeeds primarily by influencing government to subsidize his business or industry, or to enact legislation or regulation that harms his competitors.

The American economy has always included a mix of market and political entrepreneurs—self-made men and women as well as political

connivers and manipulators. Sometimes people who have achieved success at one point in their lives through market entrepreneurship become political entrepreneurs at another point in their lives. Market entrepreneurship is a hallmark of capitalism, whereas political entrepreneurship is not. It is using the state's coercive powers to plunder one's customers and competitors. It is a form of "mercantilism," the very type of political system that Adam Smith criticized in his famous 1776 book, *An Inquiry into the Nature and Causes of the Wealth of Nations*.

## Railroading versus Being Railroaded

Most business historians have assumed that the transcontinental railroads would never have been built without government subsidies. The free market would have failed to provide the adequate capital, or so the theory asserts. The evidence for this theory is that the Union Pacific and Central Pacific railroads, which were completed in the years after the War Between the States, received per-mile subsidies from the federal government in the form of low-interest loans as well as massive land grants. But there need not be cause and effect here: the subsidies were not needed to cause the transcontinental railroads to be built. We know this because, just as many roads and canals were privately financed in the early nineteenth century, a market entrepreneur named James J. Hill built his own privately-financed transcontinental railroad, The Great Northern. Hill boasted that he built The Great Northern without any government subsidy, not even the right of way through public lands. He paid cash for the right of way of his railroad, even through Indian lands.

Hill strongly opposed government favors being granted to his competitors. In *James J. Hill and the Opening of the Northwest*, biographer Albro Martin quoted Hill as saying, "The government should not furnish capital to these companies, in addition to their enormous land subsidies, to enable them to conduct their business in competition with enterprises that have received no aid from the public treasury."

James J. Hill was no "baron" or aristocrat. His father died when he was fourteen so he dropped out of school to work in a grocery store for four dollars a month to help support his widowed mother and his siblings. As a young adult he worked in the farming, shipping, steamship, fur-trading, and railroad businesses. He learned the ways of business in these settings, saved his money and eventually became an investor and manager of his own enterprises.

Hill got his start in the railroad business when he and several partners purchased a bankrupted Minnesota railroad that had been run into the ground by the government-subsidized Northern Pacific (NP). The NP had been a patronage "reward" to bankster Jay Cooke, who in the War Between the States had been one of the U.S. government's leading financiers. But Cooke and his NP associates built their railroad recklessly; the government's subsidies and land grants were issued on a per-mile-of-track basis, so Cooke and his cohorts had financial incentives to build as quickly as possible, which only encouraged shoddy work. Consequently, by 1873 the NP had fallen into bankruptcy. The people of Minnesota and the Dakotas, where the railroad was being built, considered Cooke and his associates to be "derelicts at best and thieves at worst," according to historian Michael Malone, author of *James J. Hill: Empire Builder of the Northwest*.

It took Hill and his partners five years to complete the purchase of the railroad (the St. Paul, Minneapolis, and Manitoba), which would form the nucleus of a railroad that he would eventually build all the way to the Pacific Ocean. He had nothing but contempt for Cooke and the NP for their shady business practices and their corruption and quickly demonstrated a genius for railroad construction. Under Hill's direction the workers began laying rails twice as quickly as the NP crews had done, and even at that speed he built what everyone at the time considered to be the highest-quality line. He was a meticulous cost cutter and his cost reductions were passed onto his customers in the form of lower rates. Hill understood that the farmers, miners, timber interests, and others who patronized his railroad would either succeed or fail along with him. His motto was, "We have got to prosper with you or we have got to be poor with you."

In keeping with this philosophy Hill encouraged crop diversification among the farmers along his route, educating them on the economic dangers of being dependent on a single crop. He provided free seed grain and even cattle to farmers who had suffered from drought and depression. He transported immigrants to the Great Plains for a mere ten dollars if they promised to farm near his railroad, and he donated land to towns for parks, schools, and churches.

Hill's rates fell steadily, year after year, and when farmers began complaining about the lack of grain storage space near his railroad line he instructed his company managers to build larger grain storage facilities. He refused to participate in price-fixing conspiracies with other railroad owners, and reveled in "the role of rate-slasher and disrupter of [such]

pooling agreements,” wrote Burton Folsom in *Entrepreneurs versus the State*.

Folsom describes Hill’s compulsion for excellence in the following way:

Hill’s quest for short routes, low grades, and few curvatures was an obsession. In 1889, Hill conquered the Rocky Mountains by finding the legendary Marias Pass. Lewis and Clark had described a low pass through the Rockies back in 1805; but later no one seemed to know whether it really existed or, if it did, where it was. Hill wanted the best gradient so much that he hired a man to spend months searching western Montana for this legendary pass. He did in fact find it, and the ecstatic Hill shortened his route by almost one hundred miles.

Because of such behavior, historian Michael Malone wrote that The Great Northern was “the best constructed and most profitable of all the world’s major railroads.”

In sharp contrast, the government-subsidized transcontinental railroads were a carnival of corruption and inefficiency. For each mile of track, the government gave the Union Pacific (UP) and Central Pacific (CP) railroads, which it had created, land grants as well as below market rate subsidized loans of \$16,000 per mile for track built on flat land; \$32,000 for hilly terrain; and \$48,000 in the mountains. Consequently, the UP and CP built winding, circuitous routes in order to pocket more and more subsidies. According to Burton Folsom, they stressed speed and not workmanship and always used the cheapest building materials. They were so corrupt and inefficient, Folsom wrote, that they built tracks on several feet of ice and snow and “Naturally, the line had to be rebuilt in the spring.”

Instead of spending their time brainstorming for ways to cut costs, shorten routes, and encourage economic prosperity alongside their rail lines, the executives of the UP and CP were more likely to wine and dine politicians and bureaucrats with grandiose gourmet dinners on train cars that often included a buffalo hunt from the train after dinner.

Many members of Congress demanded separate rail lines to their congressional districts as a condition of voting for the subsidies, resulting in a map of the UP and CP routes looking like a bowl of spaghetti. Moreover, because regulations always accompany any government subsidies to businesses, the UP and CP managers could not make any significant business decisions without the direct interference by the U.S. Congress. The result was gross economic inefficiency, corruption, and bankruptcy.

Hill continued to cut his rates for decades, and excelled at offering volume discounts to his largest customers. The less efficient, government-subsidized railroads hated him for this, for Hill's price cutting exposed their inefficiency and incompetence. The government got its revenge for Hill's price cutting with the Interstate Commerce Act of 1887 that banned "rate discrimination" such as volume discounts, and was followed by the Hepburn Act of 1906 which explicitly made it illegal to charge different rates to different customers. They banned price cutting, in other words, by forcing everyone to charge the same higher rates. Since Hill and his customers were the biggest beneficiaries of the Great Northern's price cutting, they were the biggest losers from this legislation.

There was no "robbery" on the free market in the late nineteenth/early twentieth century railroad business. The real crooks were the operators of the government-subsidized railroads and their political patrons in the Congress and the executive branch of government.

## The Truth about the Sherman Antitrust Act

**A**n old myth of economics is that in the late nineteenth century, a period of *several decades* of price *deflation*, monopoly was running rampant in American industry. There was supposedly “rampant cartelization” occurring, as legal scholar Richard Posner wrote in his book, *Antitrust Economics*. According to the “mainstream” view (but not the view of Austrian School economists), this “rampant” monopolization, like all forms of monopolization, supposedly led to reductions in output and subsequently higher prices. Consumers are said to have been victimized by the free market run amok with monopoly.

A corollary to this mythology is that, in the public interest, the federal government stepped in and rather heroically saved American consumers from the rapacious monopolists by enacting the Sherman Antitrust Act of 1890. Thus, antitrust law is said to be a “public interest” law in response to monopoly as a form of “market failure.” Every bit of this story is a complete falsehood.

In an article published in the June 1984 issue of the *International Review of Law and Economics* your author showed that American industry during the last decades of the nineteenth century was in fact extremely competitive and that the real purpose of the Sherman Antitrust Act was to stifle rather than to protect competition.

In the late 1880s Senator John Sherman (brother of General William Tecumseh Sherman) and his congressional colleagues began accusing

various industries of “restraining trade” and charging monopolistic prices for their products. Indeed, the language of the Sherman Antitrust Act outlaws “conspiracies in restraint of trade.” The accusations are made all throughout the *Congressional Record* of the 51<sup>st</sup> Congress. These industries included salt, zinc, steel, bituminous coal, steel rails, sugar, lead, liquor, twine, iron nuts and washers, castor oil, cotton seed oil, leather, linseed oil, and matches.

These industries were all accused of conspiring to “restrain trade” or reduce production levels in order to prop up prices in the decade prior to the 1890 Sherman Act. Thanks to such sources of information as *Historical Statistics of the United States*, one can safely conclude that these accusations were pure hogwash. The decade prior to the Sherman Act was a part of what economic historians call the “second industrial revolution” in America. As such, real GDP grew by 24 percent from 1880 to 1890. The U.S. economy was about one fourth larger at the end of the decade, which is hardly a sign of “rampant” restraints of production and trade.

By contrast, the industries accused of becoming monopolized for which real (inflation-adjusted) output data are available grew by 175 percent during that decade. In other words, industries accused by Sherman and others of “restraining trade” *increased* trade more than *seven times faster* than the rest of the economy, which itself was growing very vigorously. There was no “restraint of trade,” conspiratorial or otherwise in these industries. Among the more rapidly expanding industries that were ludicrously accused of restraining trade were steel (258 percent), coal (153 percent), steel rails (142 percent), and petroleum (79 percent). These same trends continued in the decade after passage of the Sherman Act as the “monopolized” industries continued to grow faster than the rest of the economy.

In terms of prices, it should be noted that the decade prior to the passage of the Sherman Act was a period of price deflation in which the consumer price index fell by 7 percent from 1880 to 1890. Prices in the supposedly “monopolized” industries fell even faster. For example, the price of steel rails fell by 53 percent; the price of refined sugar fell from 9 cents per pound in 1880 to 7 cents in 1890 and to 4.5 cents by 1900. The price of lead dropped 12 percent from 1880 to 1890; and the price of zinc fell by 20 percent during that time.

In sum, the historical evidence shows that, by the government’s own standard of monopolization—restraint of trade and rising prices—there was no monopoly problem in America during the decade preceding the passage of the Sherman Antitrust Act. The real problem for consumers was

government interventionism, spurred on by special-interest lobbying by less-than-successful, sour grape business competitors, that threatened to interfere with the extraordinary production expanding, new product creating, and price cutting policies of the most dynamic firms in American industry at the time. That was the real purpose of the Sherman Antitrust Act.

## The Real Purpose of the Sherman Act

One function of the Sherman Act was to divert public attention away from a more certain source of monopoly power, government itself, particularly the long-standing Republican Party policy of high protectionist tariffs. The average tariff rate in 1857—on the eve of the start of Republican Party hegemony that would last for more than fifty years—was 15 percent according to Frank Taussig in his *Tariff History of the United States*. By the middle of the Lincoln administration the average tariff rate approached 50 percent and remained in that high, protectionist range, with a few ups and downs, until the federal income tax was adopted in 1913. The “anti-monopoly” Sherman Act made no mention of how protectionist tariffs restrained trade despite the fact that the trade-diminishing aspects of protectionist tariffs had been common economic knowledge in the world since at least Adam Smith’s publication of *The Wealth of Nations* in 1776.

During the congressional debates over the Sherman Act Sherman himself complained that the output-expanding and price-cutting “trusts” in the above-mentioned industries “subverted the tariff system” that was designed to “protect . . . American industries.” Think about that. The only thing that could “subvert” the protectionist tariff system would be lower prices since the whole purpose of tariffs is to “protect” consumers from low prices. What tariffs “protect” American industry *from* is competition. The Sherman Act was therefore always inherently an anti-competitive law.

Even more damning than Sherman’s words is the fact that just three months after the Sherman Act was passed by Congress Sherman sponsored legislation that was labeled by journalists as the “Campaign Contributors Tariff Bill.” This was the McKinley tariff bill that increased the average tariff rate from 38 percent to 49.5 percent. On October 1, 1890 the *New York Times* editorialized that “The Campaign Contributors’ Tariff Bill now goes to the president for his signature . . . and the favored manufacturers, many of whom proposed and made the [tariff] rates which affect their products, will begin to enjoy this legislation.”

This caused the *New York Times*, which had originally supported the Sherman Act, to reverse its position. In the same editorial the *Times* wrote that “That so-called Anti-Trust law was passed to deceive the people and make the way for the enactment of this . . . law relating to the tariff. It was projected in order that the party organs might say to the opponents of tariff extortion and protected combinations, ‘Behold! We have attacked the Trusts. The Republican Party is the enemy of all such rings.’”

In other words, the Sherman Act was a political fig leaf designed to fool the public into believing that the Republican Party, which was founded as the party of protectionism, central banking, and corporate welfare, had somehow changed its fundamental purpose for existing and was now a libertarian, pro-consumer organization. This of course was all a big lie, as the *New York Times* explained at the time.

## The Myth of “Natural” Monopoly

One of the things that every college student who takes a course in principles of economics is taught is that the so-called public utilities (electricity, water supply, natural gas, etc.) have been government-regulated monopolies ever since the early twentieth century because government stepped in to save Americans from the evils of free-market or “natural” monopolies. The story goes like this: In industries with large fixed costs (such as the expense of building an electric power plant) the cost of serving each customer declines precipitously once the plant is up and running. This is called “economies of scale.” This is said to have been true of all of the public utilities in the early twentieth century.

The supposed problem is that one large company might achieve such low costs (and prices) that it will be able to drive all other competitors from the market and hence become a “natural” monopoly. It will, at that point, charge monopolistic prices. A corollary to this “market failure” theory is that government stepped in and created licensed, “franchise monopolies” on purpose, and then regulated prices “in the public interest,” which presumably means at a level that is not monopolistic.

There is no evidence of any kind that this story is true. There never was any evolution in the direction of free market or “natural” monopoly. Public utility monopolies were all created by government, for the benefit of government and its corporate welfare state allies in the electric power, water supply, natural gas, and other industries.

In his book *Efficiency, Competition, and Public Policy*, economist Harold Demsetz quoted fellow economist Burton Gehling as saying:

Six electric light companies were organized in the one year of 1887 in New York City. Forty five electric light enterprises had the legal right to operate in Chicago in 1907. Prior to 1895, Duluth, Minnesota was served by five electric lighting companies, and Scranton, Pennsylvania, had four in 1906. . . . During the latter part of the nineteenth century, competition was the usual situation in the gas industry in this country. Before 1884, six competing companies were operating in New York City . . . competition was common and especially persistent in the telephone industry. . . . Baltimore, Chicago, Cleveland, Columbus, Detroit, Kansas City, Minneapolis, Philadelphia, Pittsburgh, and St. Louis, among other larger cities, had at least two telephone services in 1905.

The real story (as opposed to the fable told in introductory economics textbooks) of how public utility monopoly came about was explained in a 1936 book by economist George T. Brown entitled *The Gas Light Company of Baltimore*. It is a case study of the creation of public utility monopoly in Baltimore, Maryland, but its lessons apply to all cities in America.

The history of the Gas Light Company of Baltimore is that, from its founding in 1816, it constantly struggled with new competitors. Its response was to compete in the marketplace but also to lobby the state and local government authorities to deny the granting of corporate charters to its competitors. There may have been economies of scale in the industry, but they did not prohibit vigorous competition.

Brown cites an 1851 editorial in the *Baltimore Sun* as declaring that “competition is the life of business” as the paper welcomed news of several new competitors in the gas light business. By 1880 there were three competing gas and light companies in Baltimore that fiercely competed with each other. They did attempt to merge and operate as a monopolist in 1888, but a fourth competitor foiled their plans when “Thomas Alva Edison introduced the electric light which threatened the existence of all gas companies,” wrote Brown. From that point on there was competition between gas and electric companies.

When monopoly did appear it was solely because of government intervention. For example, in 1890 a bill was introduced into the Maryland legislature that “called for an annual payment to the city from the consolidated Gas Company of \$10,000 a year and 3 percent of all dividends

declared in return for the privilege of enjoying a 25-year monopoly.” In other words, the creation of public utility monopoly was a share-the-monopoly-loot scheme between politicians and corporations at the expense of the hapless taxpayers and consumers. Some of the economics textbooks do euphemistically refer to this scheme as a form of “indirect taxation.”

Consumers suffer from paying monopolistic prices and the poor service that all government-run or supported monopolies are famous for. The blame is placed on “greedy corporations” who are happy to take the blame as long as the politicians who place the blame on them keep their monopoly in place. George T. Brown concluded in his book that “the development of utility regulation in Maryland typified the experience of other states.”

Another economist who was skeptical of the “natural monopoly” story was Horace M. Gray, an assistant dean at the University of Illinois who published an article entitled “The Passing of the Public Utility Concept” in the *Journal of Land and Public Utility Economics* in 1940. “During the nineteenth century,” Gray observed, it was believed by some that “the public interest would best be promoted by grants of special privilege to private persons and to corporations” in many industries. Of course, it was those private persons and corporations who spread the absurd tale that their special privileges were really in “the public interest” and not just their own personal self interests.

Advocates of this “public interest” nonsense advocated patents, direct subsidies, protectionist tariffs, land grants to railroads, and monopoly franchises for “public utilities.” Hundreds of monopoly franchises were awarded all over the U.S. in share-the-loot monopoly schemes just like the one in Maryland in the late nineteenth and early twentieth centuries. From that time on, wrote Gray, “the public utility status was to be the haven of refuge for all aspiring monopolists who found it too difficult, too costly, or too precarious to secure and maintain monopoly by private action alone.”

Gray entertainingly pointed out how virtually every aspiring monopolist in the U.S. claimed that whatever enterprise he was involved in was a “public utility” and should therefore be granted monopoly status by the state. This included the radio, real estate, milk, airline, coal, oil, and agricultural industries, to name but a few. In fact “the whole NRA (National Recovery Act) experiment may be regarded as an effort by big business to secure legal sanction for its monopolistic practices.” Here Gray was referring to the fact that the 1933 National Recovery Act was an attempt to *raise* prices by creating government-enforced cartels in every manufacturing

industry, complete with thousands of price-code police who enforced the government’s price floor regulations.

The role of “mainstream” economists in this whole scheme was to construct what Gray called a “confused rationalization” for “the sinister forces of private privilege and monopoly.” It is this “confused rationalization” that is still to this day taught in all of the introductory economics textbooks.

Not all cities in America participated in the share-the-monopoly-loot scheme of “regulated” public utility monopoly, and not all economists became apologists for it. In his book, *Direct Utility Competition: The Natural Monopoly Myth*, University of Illinois economist Walter J. Primeaux described how direct competition existed in the electric utility industry for decades. Buttressed by hundreds of pages of statistical analysis, Primeaux concluded that in those cities where there was direct, head-to-head competition (as opposed to market-sharing schemes where one company served half of a city and another company served the other half), there was vigorous competition, lower costs and prices, and no more “excess capacity” than in the monopoly cities. He concluded that the theory of natural monopoly fails on every count: competition existed for decades; price “wars” were not threatening to the survival of the companies; there is better customer service and lower prices; and consumers themselves prefer competition over monopoly, whereas the public utility executives generally hold the opposite view. What a surprise!

Economist Thomas Hazlett arrived at similar conclusions based on his research on the cable television industry. In a 1990 article in the *Journal of Law and Economics* Hazlett documented how about three dozen cities allowed direct competition in the cable industry as of 1990 despite the fact that cable television at the time was defined as a “natural monopoly.” In those cities where competition was permitted prices were on average 23 percent lower, more channels were offered, and customer service was superior to the monopoly franchise cities.

The theory of natural monopoly is an economic fiction. Horace M. Gray had it right when he wrote that “by a soothing process of rationalization men are able to oppose monopolies in general but to approve certain types of monopolies. . . . [And] since these monopolies were ‘natural’ and since nature is beneficent, it followed that they were ‘good’ monopolies” and “government was therefore justified in establishing ‘good’ monopolies.”

## The Virtues of Tax “Loopholes”

**B**oth of the major political parties in the U.S. long ago adopted the rhetoric of the socialist left with regard to tax deductions. The mortgage interest deduction, the state and local tax deduction, and all others are routinely denigrated as either “loopholes” that need to be slammed shut or as sources of endless confusion.

Every president has said virtually the exact same thing about tax “loopholes” for many decades now. In 2004, for example, the Bush administration announced that it wanted to “simplify the nation’s tax laws” by eliminating many tax deductions that benefit “special interests.” Translating from Washingtonese, “special interests” means hard-working taxpayers. In addition, the Washington establishment always includes the language of “revenue neutrality” whenever there is talk of tax reform. “Revenue neutrality” means that under no circumstances should the federal government ever collect a penny less in tax revenue year over year. Corporations may have declining profits or incur losses, and individual families may suffer the loss of jobs and income, but under no circumstances should government *ever* “suffer” from any reductions in the amounts of money that is plundered from the working class.

The underlying premise of all such talk is that the state has a “right” to all income that is produced, and that “loopholes” deprive it of some of that income and should therefore be eliminated. This is in fact the premise behind all forms of direct taxation. As explained by Frank Chodorov in his

book, *The Income Tax: Root of All Evil*, the state is essentially saying to its citizens: “Your earnings are not exclusively your own; we have a claim on them, and our claim precedes yours; we will allow you to keep some of it, because we recognize your need, not your right; but whatever we grant you for yourself is for us to decide.” Furthermore, “the amount of your earnings that you may retain for yourself is determined by the needs of government, and you have nothing to say about it.”

When the federal income tax amendment was adopted in 1913, wrote Chodorov, “the absolute right of property in the United States was violated.” And “that, of course, is the essence of socialism. Whatever else socialism is . . . its first tenet is the denial of private property . . . all socialists, beginning with Karl Marx, have advocated income taxation, the heavier the better.”

Academic economists—even some of those who call themselves “free market” economists—have provided plenty of intellectual support for tax policy socialism. The most fundamental argument that they make is that by creating tax deductions taxpayers are induced to waste time learning how to take advantage of those deductions, which often requires the employment of tax accountants and attorneys.

Worse yet, the existence of tax deductions spawns lobbying efforts for even more deductions. The problem with all this, the academic economists say, is that compared to an ideal world of a simple tax system, there is a great amount of “deadweight loss,” which is also called “social cost” or social waste. All of that time spent trying to avoid taxes could have alternatively been spent producing goods and services, and is thus a drain on the nation’s economy, or so they say.

Such rhetoric is ideologically loaded despite the economics profession’s pretensions of scientific objectivity. The underlying premise is that government has taken too little of the peoples’ income, and that “simplifying” the tax code, and taking more income in taxes, would somehow be more “efficient.”

But private individuals always spend their own money more efficiently than government bureaucrats do. Thus, the absurd premise of the “mainstream” economists’ argument is exactly the opposite of the truth, namely, that “efficiency” can be obtained by letting government bureaucrats spend more of the peoples’ hard-earned income.

The time spent by citizens trying to legally avoid taxes is in fact a good investment of their time: It is an investment in being able to keep, spend, and save their own income. The very fact that citizens continue to engage

in such activities on a large scale, year after year, is a demonstration of the activity's inherent efficiency in the minds of taxpayers.

As Murray Rothbard pointed out in his book, *The Logic of Action Two*,

Every economic activity that escapes taxes and controls is not only a blow for freedom and property rights; it is also one more instance of a free flow of productive energy getting out from under parasitic repression. That is why we should welcome every new loophole, shelter, credit, or exemption, and work, not to shut them down but to expand them to include everyone else . . .

Ludwig von Mises echoed this view at a 1952 meeting of the Mont Pelerin Society when he said: "Let us be grateful for the fact that there are still such things as those the honorable gentleman calls loopholes. Thanks to these loopholes this country is still a free country and its workers are not yet reduced to the status and the distress of their Russian colleagues."

The opponents of tax deductions not only deny the right of private property—the very definition of a socialist—but they also appeal to egalitarianism, the second most important ingredient in socialism. They do this by complaining of the "unfairness" of the fact that not every single person in society benefits from particular tax deductions. If everyone does not benefit, then no one should benefit, is their mantra.

Rothbard responded to this argument as well by saying that proponents of the free society should never complain about the alleged unfairness of tax deductions, but rather should work to see to it that more citizens can enjoy them. Rothbard also pinpointed another flaw in the arguments of "mainstream" public finance economists when they argue that if tax deductions are given only to some industries but not all of them, then such policies will lead to more resources being utilized by those industries than would be the case in a genuinely free market where no tax deductions existed.

The "mainstream" public finance economists omit an essential point, said Rothbard. "What is the alternative," he asked. "If investment, energy, or other [tax] credits or deductions are abolished, resources will not automatically go into more productive areas; instead, they go into government, via higher taxes" and "will simply be wasted, thrown down the rat hole of unproductive and profligate government spending."

The "mainstream" economists usually ignore this argument completely, and indeed they usually ignore the entire spending side of the government's budget when discussing such things. This allows them to pretend to be "scientific" and "objective" when in fact they are anything but.

Nobel laureate economist Milton Friedman once said that he was in favor of any kind of tax reduction at any time, and for any reason. On this topic Friedman was an “Austrian” in that his opinion was identical to that which was held by Rothbard and Mises.

## Macroeconomists Discover Economics and Debunk the New Deal (Again)

**I**t took several decades but macroeconomic model builders, who consider themselves to be the elite of the economics profession, have finally discovered freshman-level principles of economics and have used that discovery to finally debunk FDR's New Deal. (Beginning in the 1930s Austrian School economists like Henry Hazlitt recognized the truth about the New Deal: It made the Great Depression deeper and longer lasting.)

This new realization on the part of the economics profession's elite came about in the form of an article in the August 2004 *Journal of Political Economy*, one of the top-tier academic journals in the profession. The article was entitled "New Deal Policies and the Persistence of the Great Depression: A General Equilibrium Analysis," by UCLA economists Harold L. Cole and Lee E. Ohanian. "Real gross domestic product per adult," they wrote, "which was 39 percent below trend at the trough of the Depression in 1933, remained 27 percent below trend in 1939." And, "Similarly, private hours worked were 27 percent below trend in 1933 and remained 21 percent below trend in 1939." In other words, the New Deal never even came close to ending the Great Depression, contrary to several generations of government propaganda taught to every American public school child.

Cole and Ohanian—and the rest of the macroeconomic model-building club—seem surprised if not shocked by this realization. But this should be no surprise to anyone who has studied the reality of the Great Depression (as opposed to studying mathematical models of depressions). U.S. Census Bureau statistics show that the official unemployment rate was still 17.2 percent in 1939 despite seven years of “saving capitalism from itself” by the FDR regime. Per capita GDP was lower in 1939 than in 1929 (\$847 vs. \$857), as were personal consumption expenditures (\$67.6 billion vs. \$78.9 billion), according to Census Bureau data. In addition, net private business investment was *minus* \$3.1 billion from 1930 to 1940.

Because “mainstream” macroeconomic models are so befuddling and nonsensical, even the elite of the economics profession seem bewildered by their belated discovery of the truth about the New Deal. Cole and Ohanian label as “striking” the fact that the recovery from the Great Depression during the FDR regime was “very weak” (a dramatic understatement). It is “striking” to them because “these data contrast sharply with neoclassical theory . . .” That is, they have spent their entire professional careers spinning out journal article after journal article based on fanciful mathematical “models” that often have no association whatsoever with economic reality. After doing that for several decades and receiving numerous awards and honors from their fellow physics envious in the economics profession, they finally got around to looking around outside to try to discover a few facts about the economic world. Lo and behold, they discovered what the Austrian economists had known for seventy years—New Deal interventionism made the Great Depression *worse*.

The “neoclassical” theory of depressions is admittedly useless according to Cole and Ohanian, who expressed shock over their discovery of its uselessness. It also employs an absolutely comical version of the English language. It may be thought of as a Frankenstein Monster theory of depressions. As explained by Cole and Ohanian, “The weak recovery [from the Great Depression] is puzzling because the large negative shocks that some economists believe caused the 1929–33 downturn—including monetary shocks, productivity shocks, and banking shocks—became positive after 1933.” Thus, according to the “neoclassical” theory, the economy during a depression is somewhat like a prostate Frankenstein Monster, with economists playing the part of mad scientist recommending that the beast be “shocked” back to life with bursts of deficit spending by government. Or if shocking the beast back to life doesn’t work, perhaps he can be injected with a syrum that can do the trick. Such as “injections” of government

spending or easy credit that may cause the economy to come “roaring” back, to use the language of neoclassical macroeconomic model builders.

“The monetary base increased more than 100 percent between 1933 and 1939,” the authors write, making the case that such a “monetary shock” should have returned the economy to normalcy. They invoke the authority of well-known macroeconomists Robert Lucas and Leonard Rapping, who once proclaimed that “positive monetary shocks should have produced a strong recovery, with employment returning to its normal levels by 1936.” But of course it did not.

As Murray Rothbard showed in his book, *America’s Great Depression*, it was the easy money policies of the late 1920s that caused a bubble in the economy that eventually burst, causing the Great Depression. The only wise thing to have done was to have allowed the liquidation of hundreds of overcapitalized businesses to occur, cut taxes and spending, and deregulate. Instead, the Fed increased the money supply by 100 percent in a failed attempt to create another bubble while the president and Congress implemented an explosion of government interventionism. That was the first time in American history that a depression was responded to with government interventionism rather than governmental retrenchment, and the result was a seventeen-year long Great Depression, the worst in history.

Cole and Ohanian apparently decided that the classroom lessons they had been teaching their undergraduate UCLA students were not just useless model-building exercises after all, but can sometimes be used to explain real-world economic events. In particular, they recalled that elementary microeconomics teaches that cartels are groups of businesses that attempt to artificially prop up prices by collectively agreeing to restrict supply on the market. They also recognized what Austrians recognized from the very beginning of the New Deal in 1933—that the “First New Deal” (1933–35) was an attempt to cartelize all of manufacturing and agriculture with government-imposed output restrictions and price codes that fixed prices above free-market levels.

“New Deal cartelization policies are a key factor behind the weak recovery,” they wrote, “accounting for about 60 percent of the difference between actual output and trend output.” Translating from economesse, this means that if government enforces restrictions on the production of goods and services in the economy, there will be fewer people employed producing goods and services in the economy. Thus, the New Deal “cartelization” policies caused unemployment to be *higher* than it otherwise would have

been. It is truly astounding that it took the “mainstream” of the economics profession seven decades to come to this simplistic realization.

Unlike Austrian economists, who have a tradition of being widely read in economics, history, philosophy, and other disciplines, the “mainstream” of the economics profession is incredibly narrow minded, with your typical academic economist specializing in some trivial aspect of a trivial mathematical model-building exercise. His “knowledge” of economics tends to be only the last couple of years worth of articles in the very top journals on his trivialized specialty. He rarely, if ever, reads an entire book, let alone write one. In this regard the most disappointing thing about the Cole-Ohanian discovery is that they do not even cite the pioneering research on the subject, namely, the book *Out of Work: Unemployment and Government in Twentieth-Century America* by Richard Vedder and Lowell Gallaway, first published in 1993. Vedder and Gallaway arrived at all the same conclusions that Cole and Ohanian arrived at but in much greater detail and in a much more informed way. They estimated that because of New Deal interventionism, by 1940 the unemployment rate was eight percentage points higher than it would otherwise have been and concluded that “The Great Depression was very significantly prolonged in both its duration and its magnitude by the impact of the New Deal programs.” In addition to the cartelization policies of the First New Deal, Vedder and Gallaway explain how the “Second New Deal” made labor much more expensive to employers with minimum wage laws, laws that empowered labor unions, and payroll taxes for unemployment insurance and Social Security. Since the law of demand has never been repealed, it is obvious that government policies that force the price of labor up will lead to a reduction in the number of laborers employed as it prices the less productive members of the workforce out of jobs. It is sloppy scholarship, at best, for Cole and Ohanian to not even mention the Vedder/Gallaway book, and scandalous at worst.

Cole and Ohanian reach essentially the same conclusions as Vedder and Gallaway did, but expressed them in the convoluted language of the “top” economic journals, as opposed to the plain English that can be found in *Out of Work*. They concluded that

New Deal labor and industrial policies did not lift the economy out of the Depression. . . . Instead, the joint policies of increasing labor’s bargaining power and linking collusion with paying high wages prevented a normal recovery by creating rents and an inefficient insider-outsider friction that raised wages significantly

and restricted employment . . . the abandonment of these policies coincided with the strong economic recovery of the 1940s.

This last sentence is also a theme of the work of another Austrian-inspired economist, Robert Higgs, who is also ignored by Cole and Ohanian. At least the “mainstream” of the economics profession is finally beginning to realize what the Austrians have always known—that government interventionism is what caused the Great Depression, and it was post-war capitalism that cured it.

# Will Socialism Make You Happier? The Trojan Horse of “Happiness Research”

**N**ow that no thinking person believes that either socialism or government interventionism can do anything but destroy prosperity, totalitarian statisticians around the world are changing their tune and saying that prosperity doesn't really matter after all; what matters is how happy we are. And, they say, *that* is what government can be really, really good at—making us happy. Consequently, they argue, there should be no more limits on governmental powers, for limiting governmental powers will limit our very happiness.

This is the theme of a United Nations-commissioned “World Happiness Report” edited by leftist academic Jeffrey Sachs of Columbia University in 2012. The report cites the tiny country of Bhutan as being the first to adopt a “gross national happiness” index (in 1972). Among the things that the United Nations apparently believes makes the Bhutanese people especially happy is their government's *national* dress code and its institutionalized employment discrimination against residents who are not native-born Bhutanese. The United Nations report also cites Greece as one of the happiest

countries on earth despite the fact that when the report was published the Greek government was bankrupt and there were riots in the streets of Athens over that fact.

A large body of academic literature has sprung up in the area of so-called “happiness research,” and is being used to make the case for a return to socialist central planning. The research is based on several assumptions that were long ago discarded by the economics profession as dangerous nonsense. The assumptions are that “utility” or one’s perceived wellbeing is “cardinal” or measurable; that interpersonal utility comparisons can be made; and that it is possible to derive an objective and measurable “social welfare function” or “happiness index.”

Having long ago given up on the argument that socialism is superior to capitalism in terms of the organization of production and economic activity, some “happiness” researchers now assert that affluence is actually a “disease” that generates mass unhappiness in a society. There is even a pseudo-scientific book on the subject entitled *Affluenza*. rr

The assertions about the supposed ability of happiness researchers to finally measure utility simply ignore all the reasons that have been accepted for decades by the economics profession as to why utility is “ordinal” instead of cardinal and not measurable. As Murray Rothbard wrote in an article entitled “Toward a Reconstruction of Utility and Welfare Economics”:

The concept of demonstrated preference is simply this: that actual choice reveals, or demonstrates, a man’s preferences; that is, that his preferences are deducible from what he has chosen in action. Thus, if man chooses to spend an hour at a concert rather than a movie, we deduce that the former was preferred, or ranked higher on his value scale. . . . This concept of preference, rooted in real choices, forms the keystone of the logical structure of economic analysis, and particularly of utility and welfare analysis.

Rothbard continued to explain the folly of relying on public opinion surveys, as opposed to the actual demonstrated preferences of economic decision makers by saying the following:

One of the most absurd procedures based on a constancy assumption [i.e., the assumption that people never alter their preferences] has been the attempt to arrive at a consumer’s preference scale not through observed real action, but through quizzing him by questionnaires. *In vacuo*, a few consumers are questioned at length on which abstract bundle of commodities

they would prefer to another abstract bundle, and so on. Not only does this suffer from the constancy error, no assurance can be attached to the mere questioning of people when they are not confronted with the choices in actual practice. Not only will a person's valuation differ when talking about them from when he is actually choosing, but there is also no guarantee that he is telling the truth.

It is unlikely that "happiness" researchers administer lie detector tests to their questionnaire respondents (not that lie detector tests are one hundred percent accurate).

The one economist who is arguably the leader in the field of happiness research is Professor Bruno Frey of the University of Zurich. When your author asked him at a conference in Prague in 2008 about the age-old criticisms of replacing actual demonstrated preferences with questionnaires, his response was that his data are "no worse" than GDP data. He did not answer the question, in other words. But in fact, much of the happiness research data are much, much worse.

European socialists (Frey is not one of them) outside of the field of economics have gone even further with their happiness research. A European bestseller is a book entitled *The Spirit Level: Why Equality is Better for Everyone*, by Richard Wilkinson and Kate Pickett. This book is a perfect example of the misuse of statistics by two British epidemiologists. It is an abuse of statistics because the entire book is a fishing expedition for simple correlations between the degree of material inequality in a country and myriad other variables. The authors do not even attempt multiple regression analysis; instead, they present contrived statistical correlations implying that greater material equality (presumably caused by more massive income redistribution by European welfare states) supposedly leads to improvements in community life, mental health, drug use, physical health, obesity rates, intelligence, teenage births, recycling, violence, imprisonment, social mobility, dysfunctionality, anxiety, and self esteem. One critic of this research mocked its "if you torture the data long enough it will confess" methodology by publishing a chart showing a positive correlation between recycling rates and suicide rates and concluding that the more one recycles, the more likely one will commit suicide.

According to Wilkinson and Pickett's "research," the happiest people on earth during the twentieth century must have been the citizens of the Soviet empire, including all of the Eastern and Central European communist satellite countries in the post-war era, for "equality" was always the

chief goal of all forms of socialism. As F.A. Hayek commented in *The Road to Serfdom*, the end of socialism was always egalitarianism; only the means changed over time, beginning with government ownership of the means of production and transforming to income redistribution through a welfare state and a “progressive” income tax.

These happiness researchers never make any mention at all of the well-documented pathologies created by welfare statism, such as the destruction of the work ethic, family breakup, the growth of dysfunctionality caused by a welfare state that removes people from the working population, etc.

Bruno Frey is not known as a socialist, but in a June 2002 survey article on happiness research published in the *Journal of Economic Literature* entitled “What Can Economists Learn from Happiness Research” (with Alois Stutzer) Frey and Stutzer celebrated what they believe to be a resurrection of the social welfare function idea. In the article they wrote that “It seems that, at long last, the so far empirically empty social welfare maximization . . . is given a new lease on life.” They cite “research” that claims that although income has increased dramatically since World War II, “happiness” has not. Their implication is the nonsensical notion that work, savings, investment, and entrepreneurship—the ingredients of economic prosperity—do not produce happiness, yet human beings continue to strive mightily, day in and day out, to succeed at these tasks.

Socialists always embraced the ideas of a social welfare function and interpersonal utility comparisons because they argued that if the government plunders a more affluent person and gives some of the money to a less affluent person (keeping a share for “administrative expenses), then “social welfare” can be increased. This was supposedly because of the economic law of diminishing marginal utility. An affluent person has a lot of money, therefore, he places a relatively low marginal or additional value on the last dollar earned. A poor person who does not have much money, on the other hand, places a relatively high marginal value on having another dollar. Therefore, the argument goes, (legally) robbing a rich man of a dollar may cause him to lose say, only one “util” of utility, whereas giving that dollar to a poor man might increase his utility by say, ten utils. The end result is a net gain of nine utils, or an increase in “social welfare.” The economics profession long ago abandoned such nonsense, but Frey and Stutzer seem excited over the prospect of resurrecting the social welfare function idea disguised as a “happiness function.”

Another absurd conclusion of the “happiness” literature that is documented by Frey and Stutzer is the notion that “wealthier people impose a

negative external effect on poorer people but not vice versa. The supposed “negative external effect” is the envy by poorer people. But it has always been true that intellectuals, not the poor, have been the chief advocates of egalitarianism. Most poor people want to become richer. It is the intellectual class that is so often obsessed with envy and hatred of people who are more financially successful than they are. That they can manipulate survey questions that are used to make it appear that this view comes from “the poor” and not themselves does not make this statement untrue.

Moreover, welfare parasites do in fact impose very real negative externalities on their more hard-working and productive, taxpaying hosts who are plundered by the state in the name of welfare statism.

Frey and Stutzer also claim that Keynesian central planning may also be bolstered by happiness research. During the 1970s the academic economics profession largely abandoned Keynesianism when it failed to explain “stagflation” or the simultaneous increase in both inflation and unemployment. Keynesians never did come up with an explanation based on any Keynesian economic model. The old, so-called Phillips curve model, which was used to make the argument that government spending could “purchase” lower unemployment at the expense of more inflation, was dead.

Frey and Stutzer seem quite excited over the prospects for a resurrection of the Phillips Curve central planning apparatus based on happiness research. “If unemployment rises by 5 percentage points,” they wrote, “the inflation rate must decrease by 8.5 percentage points to keep the population equally satisfied.” The false assumption in this statement is that it is possible after all for government to alter inflation and unemployment rates in some kind of pushbutton fashion.

Happiness research also informs us that “welfare payments should be increased to compensate for a larger family,” they write, “so as to maintain the subjective well-being of the family.” Again, there is no mention of the harsh negative effects of welfare statism on the work ethic, the family, self esteem, etc. Nor is there any mention of the effects on the happiness of the plundered taxpaying class that must pay higher taxes to finance a bigger welfare state. To happiness researchers, affluence is a disease, so the less affluence the healthier is “society.”

Frey and Stutzer also call work effort, savings, investment, and entrepreneurship “socially wasteful” if it all results in some people becoming more successful than other people. “The high-income recipients, as winners of these races, should be more heavily taxed,” they write. “Raising everybody’s

income does not increase everybody's happiness," but improving one's income "in comparison to others does," they conclude. It is not a surprise that Frey and Stutzer also remark that the lifelong socialist John Kenneth Galbraith might be considered to be the "father" of happiness research.

Many of the pseudo-scientific sounding conclusions of happiness research are extraordinarily simple minded and downright comical. Consider the following examples from the Frey/Stutzer article:

- "Persons with higher income have more opportunities to achieve what they desire." .
- British lottery winners . . . reported higher mental wellbeing the following year."
- "There is more to subjective wellbeing than just income level." Something no one has ever disputed.
- "On average, persons living in rich countries are happier than those living in poor countries." Therefore, we should tax the rich countries and send the money to the governments of the poor countries, every happiness researcher would conclude.
- "Happiness of unemployed persons is much lower than that of employed persons."
- "Experiencing unemployment makes people very unhappy."
- "Freedom and happiness are positively related."
- "Happy people smile more during social interactions."
- "People receiving an inheritance reported a higher mental wellbeing in the following year." Shocking.
- "Persons with higher incomes . . . can buy more material goods and services." Shocking.

An excellent critique of happiness research is a book by Christopher Snowden entitled *The Spirit Level Delusion: Fact-Checking the Left's New Theory of Everything*. The author concludes that:

Apologists for Marxism have made myriad excuses for their ideology's failure to provide the same standard of living and liberty as was enjoyed in capitalist nations. Until recently, few have

been so brazen as to claim that lowering living standards and curtailing freedom were the intended consequences, let alone that people would be happier with less of either. In that sense, books like *The Spirit Level* represent a departure for the left. Limiting choice, reducing wealth and lowering aspirations are now openly advocated as desirable ends in themselves.

Thus, “happiness research” is part of a crusade to persuade the public that poverty and servitude to the state are superior to prosperity and freedom. It is a new version of what twentieth-century communists referred to as “socialism with a smiling face” during the last, dying days of totalitarian communism.

# The Canard of “Asymmetric Information” as a Source of Market Failure

**T**he voluminous literature on “market failure” is, for the most part, a collection of thousands of illustrations of the Nirvana Fallacy—comparing real-world markets to an unattainable utopian ideal (perfect competition), and then denouncing markets because they fall short of utopia or Nirvana. Having “proven” that markets “fail,” the analyst then proposes government intervention under the *assumption* that no such failures will infect government. Markets may not be perfect, but government is assumed to be. This method of analysis is still pervasive despite the public choice “revolution” and its emphasis on the economics of government failure.

Austrian economists have long understood that such a method of analysis is deeply flawed for numerous reasons, not the least of which is that the whole perfect competition/perfect information apparatus simply ignores most or all of the actual market process. In perfect competition there is no competition, as Hayek explained in his book, *Individualism and Economic Order*, since all the features of real-world competition, such as advertising, innovation, and price cutting, are assumed away with the perfect information assumption.

An especially egregious example of a deeply flawed theory of market failure is the notion of asymmetric information, first associated with the

economist Bruce Akerloff. Since sellers typically have better information about the product or service being sold than do buyers, the theory goes, they are able to easily swindle consumers by selling them "lemons." The basic problem with this theory is that it gets the economic world exactly backward: asymmetric information is essentially another way of saying "the division of labor," the whole basis of trade and exchange and the *success* of markets.

In *Human Action* Ludwig von Mises properly called the division of labor "the fundamental social phenomenon" (along with human cooperation in general). Cooperative action among individuals is more productive and efficient than "self-sufficient individuals," wrote Mises, because of several fundamental facts: the innate inequality of all human beings with regard to their abilities in the workplace; the unequal distribution of "nature-given, non-human opportunities of production on the surface of the earth"; and the fact that almost all production processes require some kind of team work that no single person could accomplish.

In describing the evolution of the division of labor and specialization in the market process, Mises further wrote of how it "intensifies the innate inequality of men" since "practice of specific tasks adjust individuals better to the requirements of their performance; men develop some of their inborn faculties and stunt the development of others. . . . [P]eople become specialists." Thus to Mises, the division of labor is nothing less than the source of human civilization. "What distinguishes man from animals is the insight into the advantages that can be derived from cooperation under the division of labor," he wrote. Without the advantages of the division of labor the average person would live like a "primitive savage."

Mises wrote all of this during the machine age, where the language of "division of labor" was appropriate. Brawn had not yet been replaced by brains as the primary human input in production, as it has progressively done during today's information age. Hayek also lived almost all of his life in the machine age, but he anticipated the information age and spent most of his life studying and writing about the use of knowledge in society. Hence for Hayek—and for everyone in today's information age—the phrase "division of knowledge" may be more precise than "division of labor." As Hayek himself explained in his famous essay, "The Use of Knowledge in Society":

We need to remember only how much we have to learn in any occupation after we have completed our theoretical training, how big a part of our working life we spend learning particular

jobs, and how valuable an asset in all walks of life is knowledge of people, of local conditions, and of special circumstances. . . . The shipper who earns his living from using otherwise empty or half-filled journeys of tramp-steamers, or the estate agent whose whole knowledge is almost exclusively one of temporary opportunities, or the *arbitrageur* who gains from local differences of commodity prices—are all performing eminently useful functions based on special knowledge of circumstances of the fleeting moment not known to others.

Ask yourself these questions: Who knows more about home building—home builders or home buyers? Who knows more about supplying grocery stores with fresh meat—ranchers and farmers, or average consumers? Who knows more about manufacturing automobiles—automotive engineers employed by automobile manufacturers, or car purchasers? Who knows more about producing and marketing articles of clothing—clothing manufacturers and distributors or clothing shoppers?

The point of these rhetorical questions is that *all* information about all products and services is asymmetrical in successful, capitalist economies because of the division of knowledge (and labor) in society. If we all had symmetrical information about all of the above tasks, none of the above-mentioned businesses and occupations would exist. It is neither desirable nor possible for everyone to have symmetrical information. To paraphrase Mises, what distinguishes man from animals is the insight into the advantages that can be derived from cooperation under the existence of asymmetric information and the division of knowledge in society.

In fact, Mises criticized the notion of asymmetric information as an alleged flaw of the market, although he did not use that exact language. “In an economic system in which every actor is in a position to recognize correctly the market situation with the same degree of insight,” he wrote, “the adjustment of prices to every change in the data would be achieved at one stroke. It is impossible to imagine such uniformity in the correct cognition and appraisal of changes in data except by the intercession of superhuman agencies.” We would have to assume that “every man is approached by an angel informing him of the change in data,” Mises continued. Moreover, even if market participants did possess the same data and information, they are bound to “appraise it differently.”

Indeed, differences in information—and different interpretations of the meaning and importance of information to each individual—is the sole cause of trade and exchange. Trade and exchange take place because

different individuals value the same physical goods (or services) differently. Those different subjective evaluations are derived from informational differences in the minds of buyers and sellers—from asymmetric information, in other words.

Like most other “market failure” models, the asymmetric information/lemons model studiously ignores real-world markets. Even Akerloff’s widely cited “lemons” argument—that the used car market would eventually disappear because of consumer mistrust of used-car dealers—was always dead wrong. It was wrong because it ignored the existence of product warranties in real-world used car markets. Akerloff asserted that used car markets would become progressively dominated by lower and lower quality cars (if the market did not disappear altogether) because of the ease with which used car salesmen can sell “lemons” to ill-informed buyers. But even at the time Akerloff first made that argument (the 1970s) thirty-day warranties were quite standard in U.S. used car markets. Thirty days is plenty of time to determine whether or not a car is a “lemon.” Indeed, today there are companies like CarMax that offer seven-day, no-questions-asked return policies on all used cars that they sell, thereby eliminating any possibility of lemons problems. The free market had already solved the “lemons problem” when Akerloff (and the rest of the mainstream of the economics profession) discovered its existence.

The Akerloff-inspired asymmetric information literature also ignores the implications of the dynamic nature of competition. If a used car dealer is known to be dishonest, he creates a profit opportunity for a competitor in doing so. In a competitive market more honest car dealers will take market share away from the less honest ones, precisely the opposite of the outcome predicted by Akerloff. Brand name is a valuable asset to any business—perhaps its most valuable asset—but this is ignored or downplayed by the asymmetric information/market failure literature. Competition will not eliminate dishonesty, but it does penalize it while rewarding honesty in business dealings. In addition, word-of-mouth communication, publications like *Consumer Reports*, and myriad online information sources make it increasingly easy for consumers to educate themselves about the sellers of almost every product on the market in today’s world.

## The Real Asymmetric Information Problem

Asymmetric information is simply another way of saying the division of knowledge and labor exist in human society. When potential problems

do arise, such as superior knowledge on the part of a used car dealer, marketplace competition provides a solution, as described above. No such solutions exist in government, however, which is where asymmetric information is a serious problem. In this case we are dealing with the well-established fact that, in their capacity as voters, people tend to be “rationally ignorant” of almost all of what government does. In fact, government is so pervasive that no human mind could possibly comprehend the tiniest fraction of one percent of what government in a country the size of the U.S. does. Consequently, special-interest groups dominate all democratic governments; government spending, taxing, borrowing and regulatory powers are essentially unlimited; and rent seeking runs amok. The result of all of this in recent years has been unprecedented budget deficits and even the impending bankruptcy of entire governments, from California to Greece.

Foreign policy is a single case in point of the severe asymmetric information problems in government: All of the negotiations, discussions, and strategy sessions that might lead an entire nation into war are always done by a few people in the executive branch of government in complete secrecy from any citizens. The citizens must then rely on whatever they are told by the spokesmen for the government regarding the supposed reasons for the war. The entire world now knows, for example, that the reason given for the U.S. invasion of Iraq in 2003—that Saddam Hussein had “weapons of mass destruction” and intended to use them in the U.S.—was false. Rational ignorance gives politicians infinitely more latitude to lie to the public compared to the most dishonest used car dealer in the world.

In markets, dishonest business people can be quickly penalized with the loss of business or bankruptcy. (In addition to losing customers, suppliers will also abandon dishonest business associates.) It is quite the opposite in government. Unseating a dishonest member of Congress is virtually impossible because the entire U.S. Congress has been so gerrymandered, and incumbents have given themselves such monopolistic advantages (dozens of staffers who are essentially tax-financed permanent campaign staff; free mailing privileges; dozens of subcommittees that are used to dole out pork barrel spending, etc.), that congressional re-election rates have averaged over 90 percent for the past half century in the U.S. ([www.opensecrets.org/bigpicture/reelect.php](http://www.opensecrets.org/bigpicture/reelect.php)).

Even if this were not true, members of the U.S. House of Representatives remain in office for two years; U.S. senators for six years; and presidents for four years. By contrast, a consumer can switch products in an

instant if he decides that a company's advertising was deceptive. The real asymmetric information problem is a problem of government failure, not market failure.

## The Real Ethics Problem in America

**U**nder the dubious proposition that the Great Recession was caused by a sudden outburst of greed (as though greed did not always exist), a new growth industry in America is the teaching of “business ethics” at the university level. This is about as appropriate, however, as instruction in marital fidelity by Tiger Woods or a course on fine dining by Jeffrey Dahmer.

There are some exceptions, but business ethics courses tend to cherry pick isolated examples of unethical behavior in the business world and insinuate that such behavior is *inherent* in *all* businesses. This ignores the reality of how markets work and misinforms students. Dishonest business people will be punished financially as customers cater to their competitors while suppliers refuse to do business with them. In cases of negligence, such as an oil spill, chief executives often lose their jobs, the company is sued, and the firm’s stock price plummets. Such market feedback mechanisms do not guarantee ethical behavior, but they do reward it with customer loyalty—and profits. No such feedback mechanism exists in government—which is where much larger ethical problems exist.

Business ethics courses typically combine anti-business moralizing with advocacy of more government regulation of business and, subsequently, a greater politicization of society. In doing so they actually *encourage* unethical behavior because it is politics, not markets, that is *inherently* im-

moral. The founding fathers understood this, which is why Thomas Jefferson once said that government needed to be “bound by the chains of the Constitution.” To James Madison, the Constitution was needed “to restrain the violence of faction.” In his *Farewell Address* George Washington warned of “cunning, ambitious, and unprincipled men” who tend to dominate politics. Thomas Paine viewed government as “a necessary evil,” at best.

What were these men talking about? Well, they understood that when government uses its legal monopoly on coercion to confiscate one person’s property and give it to another, it is engaging in what would normally be called theft. Calling this immoral act “democracy,” “majority rule,” or “progressive taxation” does not make it moral. Under democracy, rulers confiscate the income of productive members of society and redistribute it to various supporters in order to keep themselves in power. The government also pays *itself* very well out of these confiscated funds. Today the average federal bureaucrat makes about double the salary and benefits of his or her private-sector counterpart according to the U.S. Department of Labor. State and local government bureaucrats make about one-and-a-half times their private-sector counterparts.

In order to finance a campaign a politician must promise to steal (i.e., tax) money from those who earned it and give it to others who have no legal or moral right to it. There are (very) few exceptions, but politicians must also make promises that they know they can never keep (i.e., lie). This is why so few moral people are elected to political office. The most successful politicians are those who are the least hindered by strong moral principles. They have the least qualms about confiscating other peoples’ property in order to maintain their own power, perks, and income. In his bestselling 1944 book, *The Road to Serfdom*, Nobel laureate economist F.A. Hayek described this phenomenon in a chapter entitled “Why the Worst Get on Top.”

Successful politicians tend to be extremely egotistical with inflated self images, an enlarged sense of importance, and a misguided sense of aggression. It is misguided because it is not directed at serving their fellow citizens, as is the case with marketplace competition, but at serving *themselves*. They are showcases of the *Seven Deadly Sins*: *self-pride* trumps humility; *envy* poisons the heart of every crusader for “income redistribution”; *wrath* is what one experiences by opposing the ruling elite; *sloth* has long been associated with government bureaucracy; *greed* for power over others is politics personified; *gluttony* is frequently on display with

the ostentatious lifestyles and conspicuous wealth of the Washington establishment; Bill Clinton's impeachment and Newt Gingrich's resignation as House Speaker over adulterous affairs proved once again that the leaders of the Washington establishment are not unfamiliar with the seventh deadly sin of *lust*. (Their bigger sin is the lust for power over others—and other governments.)

In short, universities perform a disservice with their relative neglect of the real ethical problem in America—the politicization of society and the growth of government—while greatly exaggerating ethical problems in private enterprise.

## The Myth of Government Job Creation

**M**illions of Americans remained unemployed several years into the “Great Recession” because our politicians perpetuate a dangerous myth—the myth of government job creation. Government spending cannot create jobs on net; it can only destroy private sector jobs in order to create government jobs. The taxes, government debt, or inflationary money creation by the Fed that finances government job creation depresses the private sector and destroys job creation there in order to finance government-sector jobs. It is robbing Peter to pay Paul.

Politicians perpetuate the myth of government job creation because the government jobs that are created are seen by the average voter, whereas the private-sector jobs that are destroyed (or never created) are not. Moreover, it is not unusual for government overhead costs to be so high that more than \$100,000 is extracted from the private sector to finance a single \$35,000 a year government job. Thus, several private sector jobs are destroyed to create one political patronage job.

It is illegal for politicians to pay people in cash in return for their votes, but it is not illegal for politicians to arrange for voters to receive government paychecks in return for their support. Each government job is worth several votes in the eyes of a politician, as the employee’s spouse, adult children, and relatives are sure to vote for the job-dispensing pol. When a politician brags

that a program has “created 200,000 (government) jobs,” what really occupies his thinking is that the program has probably generated a half million *votes* at election time.

Government spending has *never* reduced unemployment overall; quite the contrary—it always *increases* unemployment because it crowds out so much private sector job creation. In 1929 President Herbert Hoover devoted 13 percent of the federal budget to “emergency” public works spending. This is twice as much as the Obama administration’s “stimulus” spending as a percentage of the budget. It only made things worse.

Despite all the New Deal spending during the 1930s, including the employment of some ten million people in government jobs, official unemployment was 15.7 percent in 1940, on the eve of World War II. That’s more than five times the 2.9 percent unemployment rate in 1929 at the start of the Great Depression. Nor did the explosion of government spending during World War II cause of the end of unemployment. There were about 5.5 million unemployed people in America in 1940. By 1943 over 8 million had been drafted into the military, with two million more conscripted in the next two years. It was the draft, not the “stimulus” of war, that ended unemployment during the war years.

Massive *reductions* in government spending have always created economic prosperity and genuine job creation. When World War II ended the federal budget was slashed from \$98.4 billion in 1945 to \$33 billion by 1948 while some ten million men and women were decommissioned from the military. This is what created the post-war economic boom. Because of such dramatic cuts in government spending, the private components of GDP—private consumption and investment spending—rose by 30 percent in 1946, the largest one-year increase in the private components of GDP in American history. The elimination of wartime price controls and cuts in business taxes also spurred economic growth.

Government “stimulus” spending has never been anything but one giant vote-buying scheme. A 1938 report by the U.S. Senate Committee on Campaign Expenditures discovered that in many states the recipients of Works Progress Administration jobs were required to register as Democrats, pledge to vote for Democrats, and even donate 2 percent of their salaries to the Roosevelt reelection campaign as a condition of employment. Republicans have undoubtedly played the same game over the years.

In their book, *The Political Economy of the New Deal*, economists William Shughart and Jim Couch conducted a statistical study of New Deal spending patterns and concluded that the main determinant of where

the spending was allocated was the potential for the spending to get FDR reelected. Thus, the poorest part of the country, the solidly Democratic South, received relatively little assistance compared to areas where there were “big-city machines, organized labor, and other constituencies” that were likely to support FDR’s reelection. The formula for economic recovery is to do exactly the opposite of what most administrations have done since the 1930s and follow Harry Truman’s example instead by dramatically cutting back on the size and scope of government.

## The Myth of the Male/Female “Wage Gap”

**M**arriage affects men and women differently in terms of their earning abilities. There are exceptions, but in general women are more likely to drop out of the workforce for a period of time because of child rearing and other chores (that most men shirk). Consequently, they fall behind their male counterparts in terms of human capital accumulation, productivity, *and wages*. This, far more than discrimination, is why male wages exceed female wages *on average*.

But that’s not the only reason. The book *Why Men Earn More: The Startling Truth Behind the Pay Gap—And What Women Can Do About It*, by Warren Farrell, and Professor James T. Bennett’s *The Politics of American Feminism: Gender Conflict in Contemporary Society* provide much greater detail.

Warren Farrell boasts of having been elected to the board of directors of the New York City branch of the National Organization for Women (NOW) three times. The author of the foreword to Farrell’s book, Karen DeCrow, is a former NOW president who works as an employment discrimination lawyer. “Men are not involved in a nefarious plot to keep female wages down,” she declares.

In *The Politics of American Feminism* Professor Bennett paraphrases more than twenty reasons why men earn more than women, as discussed and documented in great detail in *Why Men Earn More*.

Cumulatively, they go a long way toward explaining the “wage gap,” although neither Bennett nor Farrell believes that wage discrimination by gender is completely nonexistent. Nor is it limited to male discrimination against women. The reasons, based on *generalizations* that are supported by voluminous statistics, are:

- Men go into technology and hard sciences more than women.
- Men are more likely to take hazardous jobs than women, and such jobs pay more than cushier and safer jobs.
- Men are more willing to expose themselves to inclement weather at work, and are compensated for it (“compensating differences” in the language of economics).
- Men tend to take more stressful jobs that are not “nine-to-five.”
- Many women prefer personal fulfillment at work (child care professional, for example) to higher pay.
- Men are bigger risk takers than women, in general. Higher risk leads to higher reward.
- The worst working hours pay more, and men are more likely to work these hours than women.
- Dangerous jobs (coal mining) pay more and are more male dominated.
- Men tend to “update” their work qualifications more than women do.
- Men are more likely to work longer hours, and the pay gap widens for every hour past 40 per week.
- Women are more likely to have “gaps” in their careers, primarily because of child rearing and child care. Less experience means lower pay.
- Women are nine times more likely than men to drop out of work for “family reasons.” Less seniority leads to lower pay.
- Men work more weeks per year than women.
- Men have half the absenteeism rate than women.

- Men are more willing to commute long distances to work.
- Men are more willing to relocate to undesirable locations for higher-paying jobs.
- Men are more willing to take jobs that require extensive travel.
- In the corporate world men are more likely to choose higher-paying fields such as finance and sales, whereas women are more prevalent in lower-paying fields such as human resources and public relations.
- When men and women have the same job title, male responsibilities tend to be greater.
- Men are more likely to work by commission; women are more likely to seek job security. The former has more earning potential.
- Women place greater value on flexibility, a humane work environment, and having time for children and family than men do.

One message that Farrell has for women is that if they really want to get paid more, they should pay more attention to these determinants of higher pay and less to Quixotic crusades for “comparable worth legislation” or “diversity training” that demonizes male employees but does nothing for them. This is the kind of practical advice a top-notch economist would offer, but such advice is usually drowned out on today’s college campuses by politically-correct lynch mobs who, as Professor Bennett says of academic feminists, “find it far easier to simply smear those who point out the phantom nature of the wage gap.”

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