LIBERTY AND HARD CASES. BY TIBOR MACHAN. STANFORD, CALIF.: HOOVER INSTITUTION PRESS, 2002.

The case for liberty and the free market must be made on two fronts. On the one hand, a sound theoretical foundation supporting private property rights and limited government intervention is indispensable for such an endeavor. On the other hand, practical demonstrations of how such a system would function are also vitally important. No matter how compelling a theoretical argument against State action in the abstract may be, there remain the so-called "hard cases," which most people consider simply intractable absent government assistance, if they can even conceive of such an alternative approach at all. One commonly hears that, e.g., health care, defense, or technology are areas where the State must play a central role to remedy alleged "market failures" or to provide "public goods" that individuals, freely associating by exchanging their own property, supposedly cannot.

One such area is the prevention and relief of natural disasters, the most prominent of which (as far as resulting damage is concerned) include floods, hurricanes, and earthquakes. Such events, due to their sheer physical awesomeness and the seeming capriciousness with which they strike, do much to reinforce the impression in many people's minds that there can be *no* other approach to dealing with disasters than to have the State intervene as necessary. Still, even for those of interventionist bent, some basic questions must be answered: how far *should* the State go in helping its subjects deal with disasters, both in their aftermath and in preparations against? What responsibilities do these subjects, both as individuals and as voluntary associations, have to bear? Can provisions against such events be viewed as similar to precautions taken against other, less destructive but still unpleasant or tragic, misfortunes? These issues are of particular importance to those generally opposed to government interventions, for unless one is prepared to abandon recourse to the State altogether, the question of how far one is willing to compromise one's adherence to liberty in the face of some emergency must be addressed.

These issues are the focus of *Liberty and Hard Cases*, a short collection of essays discussing the proper role of government and the private sector in disaster relief. The contributors are supportive of the notion that the free market, *in conjunction with a limited State*, can appropriately respond to such crises, and point out the numerous ways in which government, ostensibly the selfless protector of its afflicted citizens, has in fact exacerbated the very crises it is meant to alleviate. Most of these ways are probably familiar to free-market advocates. These counterproductive interventions include subsidization of disaster insurance premiums, offers of direct relief and loans to disaster victims to live in and rebuild in high-risk areas, and compulsion of both

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insurance companies to offer policies to such at-risk individuals, and of individuals not at risk to participate in such schemes. All of these public policies have the effect of making it *appear* to those living in, say, flood plains that they are in less danger (financial as well as physical) than they actually are. Such policies allow those people to bear less responsibility than they should, and hence to assume more risk than they otherwise would. At the very least, incentives to prepare for such disasters are weakened if not removed, and government-provided benefits have a "crowding-out" effect on private relief initiatives. (As an indirect effect, by forcing insurance companies to bear more risk than they otherwise would, these companies may either get out of the business in the high-risk region altogether [if they're not eventually bankrupted], or scale back coverage in those areas that they could beneficially serve, forcing *other* people to be exposed to greater dangers than they otherwise would be. As always, there is no free lunch.)

These are of course the classic moral hazard problems of any insurance contract, but with the State involved the ramifications are much greater. By "artificially" encouraging people to engage in high-risk behavior (such as living on beachfront property in a hurricane zone) or, even worse, allowing them to potentially *repeat* their calamity (by providing them with the means to rebuild their destroyed property in the same, disaster-prone area), the State increases the likelihood and magnitude of human and material suffering from a natural catastrophe. Only the State, with its taxation powers stemming from its status as a judicial and protective monopolist, can insulate itself from such actions, in a way that no private insurance company ever could.

The contributors to this volume further point out that the bureaucracies pledged to addressing these problems typically act like any other bureaucracy: that is, their primary interest becomes that of self-preservation and empire-building, not problem-solving, and their management of actual crises reflects this appetite for expansion (usually at the expense of smaller social or political units likewise engaged in reconstruction). Indeed, government at all levels, not just those agencies directly involved in response to some disaster, invariably exploit crises to increase their power over their subjects (as has been well-documented in Robert Higgs's *Crisis and Leviathan*, a classic work cited by several of the contributors). Such realities should also be of no surprise to free marketers, and it is a central theme of this volume that, regardless of how appropriate one may deem government disaster programs, one must be ever vigilant against the "slippery slope" of losing our liberties due to the urgency of some problem that allegedly requires increased State powers (that rarely return to the pre-crisis levels, what Higgs terms the "ratchet effect").[1] Indeed, a serious part of the danger is not just from the government agencies themselves, but from the acclimation the government's subjects come to feel toward State action, and the perceived normality and acceptance of such actions. Even if governments act with good intentions, they

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[1]If anything, the contributors probably downplay the risks from agencies such as FEMA (Federal Emergency Management Agency). One does not have to be a right-wing conspiracy theorist to recognize that such agencies are at least as sinister as they are bumbling. Likewise, editor Machan's characterization of government interventions as "paternalistic" (p. xviii) may be apt in some circumstances, but the State's true nature may be a bit more unsavory than that. Furthermore, issues of corruption and patronage are, for the most part, only alluded to, but surely the logrolling and pork-barreling that accompany any sizeable disaster are enormous.

always run the risk of undermining the culture of self-rule and responsibility that must be the basis for any free society.

These points are all well-taken, and the contributors do a good job of presenting and defending them. That is the strength of the volume, in making the case that with government assistance, no matter how welcome, there always comes a cost to the free society that may not be so desirable in the long term. (However, the authors tend to speak in terms of rather vague notions like "individual sovereignty" or "classical liberalism" rather than the more straightforward and justifiable concept of private property rights.) In discussing "what is wrong" and "what shouldn't be done," the book succeeds. In discussing "what is to be done," the book achieves mixed results (at least from an Austrian perspective), in this reviewer's opinion.

The first essay, "The Role of Government in Responding to Natural Catastrophes" by N. Scott Arnold, deals with the problem of insuring against disasters, and the impact that governments (mainly at the Federal level) have had on the private insurance industry in states such as Florida and California (where, respectively, the concern is with hurricanes and earthquakes). These moral-hazard aspects have already been brought up, and Arnold details the manner in which the political process has led to greater State regulation, mandated benefits, and the like. However, Arnold makes some questionable claims about the nature of insurance, and about the ability of the market to provide such services.

Specifically, he argues that the risks facing private insurance companies covering disasters are correlated, so that the occurrence of one claim against a company is usually associated with the occurrence of several other claims (thus threatening bankruptcy), and that "informational asymmetries" between insurer and insured prevent the realization of mutually beneficial transactions due to the fact that low-risk people will not buy insurance at the price it must be set to cover high-risk people (so that there is "market failure": insurance companies either cannot enter into policies with the low-risk individuals, or they must prudently limit their coverage of high-risk individuals who want such policies). As such, there is some limited role for government in rectifying these problems faced by the private sector. Given these claims, it would probably be good to briefly discuss the Austrian conception of insurance.

The mathematics of probability theory is frequently used as a way of quantifying risk and uncertainty. However, risk and uncertainty are not the same things. Ludwig von Mises (1998, chap. 6) distinguishes between two types of probability that acting man may resort to: class probability and case probability. Mises (p. 107) explains:

> Class probability means: We know or assume to know, with regard to the problem concerned, everything about the behavior of a whole class of events or phenomena; but about the actual singular events or phenomena we know nothing but that they are elements of this class.

In contrast, Mises (p. 110) holds that: "Case probability means: We know, with regard to a particular event, some of the factors which determine its outcome; but there are other determining factors about which we know nothing."

Mises categorically distinguishes these two types of probability. As an illustration of class probability, he uses the example of a lottery, where we *know* that a certain number of tickets will be winners, but we do not know *which* of the tickets will win.[2]

[2]See also Rothbard (1997), p. 229.

This type of probability is amenable to mathematical methods, but *only* as a *representation* of something we *already* know (or assume to know); such methods add nothing to our knowledge of *particular* outcomes. If we had additional information about these, we would be able to form *different* classes of outcomes, with the same types of representations but again without any additional knowledge of outcomes regarding individual members of those classes (beyond the fact of their class membership). Case probability, however, is not amenable to any mathematical methods. Here one must rely crucially on one's understanding of the particular problem at hand to make a judgment about the likely outcome (see also Hoppe 1997).

In Mises's conception, risk is a form of class probability and can be quantified, whereas uncertainty is a form of case probability and cannot be quantified.[3] In particular, it is only risk, and not uncertainty, that can be insured against. To quote Mises (1998, pp. 108–09) again:

> Let us assume that ten tickets, each bearing the name of a different man, are put into a box. One ticket will be drawn, and the man whose name it bears will be liable to pay 100 dollars. Then an insurer can promise to the loser full indemnification if he is in a position to insure each of the ten for a premium of ten dollars. He will collect 100 dollars and will have to pay the same amount to one of the ten. But if he were to insure one only of them at a rate fixed by the calculus, he would embark not upon an insurance business, but upon gambling. He would substitute himself for the insured. He would collect ten dollars and would get the chance either of keeping it or of losing that ten dollars and ninety dollars more.

Furthermore, "[i]nsurance, whether conducted according to business principles or according to the principle of mutuality, requires the insurance of a whole class or what can reasonably be considered as such. Its basic idea is pooling and distribution of risks, not the calculus of probability" (p. 109).

This situation describes what commonly occurs with most health or auto insurance, for example. An insurer believes (to the best of his knowledge) that, out of a particular group of people, a certain number will become ill and incur some sort of financial obligation as a result. The insurer does not know *which* of the people will become sick, only that a certain number will. The insurer can accordingly charge premiums to offset these losses (plus charge for the service), and so in effect he bears no risk. If the insurer learns that, e.g., redheads become ill at a greater rate than non-redheads, he can reclassify the people in the insured group and charge different premiums based on different anticipated losses. However, the fact remains that the insurer is always making recourse to class, not case, probability. In essence, the insurer is making a judgment about the frequency and distribution of events, not people.

The situation does not prevail in the case of natural disasters, so it is not clear that insurance is the proper provision against such events. It is not the case, e.g., that a certain number of earthquakes (events) will occur in some region, causing a certain amount of damage such that premiums can be charged to *all* (or most) of the people in that region under the assumption that only a certain number of them will be afflicted (without knowing *who* those will be). Rather, the issue is that *one* event (the earthquake) might occur, but it is simply not known entirely *when* it will happen. Also, when the event occurs, it will affect all (or least a large number) of the people in

[3]Knight (1940) also makes this distinction.

that region (but not outside it). In effect, there is no class of events and affected people. There is only a class of a single member, and the issue becomes one of judging whether a *particular* event will occur. That is, we are considering case, not class, probability. As such, it would not seem that insurance *can* be applied to such situations. In contrast, with ordinary insurance, we know (or assume to know) that the event in question *will* occur, just not *where* and *whom* it will affect.

The point is not that insurance companies do in fact take such considerations of class versus case probability into account, only that to the extent that they do not, they are not engaged in insuring against risk, but rather they are engaging in speculation regarding uncertainty. Consequently, the problem facing companies covering disaster insurance is not the fact that the risks are "correlated." Rather, the companies' problem is that they are in the position of Mises's insurer who only insures a single person; they are engaged in a speculation that may pay off most of the time, but could possibly lead to ruinous losses.

Thus Arnold's discussion of the difficulties faced by insurance companies, and the government policies that could alleviate these difficulties, seems beside the point. If insurance companies are, in essence, engaged in a form of speculation, then we should not expect such companies to be an appropriate means for people to provide against the obligations incurred by natural disasters. Unlike the case with ordinary insurance, *both* parties are in effect gambling. With ordinary insurance, only the insured is gambling; the insurer has completely accounted for the possible losses and charged appropriate premiums by assembling the insured into a suitable class. It is questionable whether such gambling is the best way for someone living, say, in Southern California, to prepare for the consequences of an earthquake, and it is equally questionable whether an insurance company which enters into such bets is to be viewed in a different light than, say, a bookie who is ruined when a major upset occurs in a sporting event. One may sympathize with such a person, but one does not typically recommend that social policy accommodate them.

What, then, *is* the appropriate provision against such calamities? In the essay "Dealing with Natural Disaster: Role of the Market," Barun S. Mitra makes a number of important points. To begin with, the fact that news media can quickly appear at the scene of a major catastrophe means that large numbers of people get to see up-close the immense physical damage and personal suffering that accompanies the event, and that it is easy for people to conclude that the situation is as bad as can be imagined. Yet, there can be no question that modern-day disasters cause much *less* death and destruction than comparable events of the past. This is especially true in the West, where the damage from such disasters is measured in dollars, not lives lost. Even in the Third World, however, such events kill far fewer people than they once did. Still, there is little doubt that the developed world weathers such storms better than the nondeveloped world, which of course leads one to ask why that is the case.

That this improvement has been accompanied by dramatic increases in the standard of living of ordinary citizens, and that disaster prevention and relief is far superior in the economically advanced West, is surely no coincidence. Mitra draws the obvious but seldom-stated conclusion from these facts: namely, that it is economic development, and the attendant advances in infrastructure, medicine, and capacity for charity that are the best tools for managing natural disasters. The equally obvious (but again rarely pointed out) conclusion is that the role of governments in addressing such disasters is to foster economic growth, which it can only do by respecting private property and the rule of law, cracking down on corruption (which invariably increases during relief efforts), and generally limiting its activities to law enforcement rather than legislating and regulating. Whether it is reasonable to expect *any* government to behave in such a way is a different matter. The main point is strong, however: it is capitalism, not government, that is needed to prepare for and reconstruct after a disaster.

The third essay, "A Fool's Errand" by John Ahrens, is in fact more of a defense of the limited State against anarchism (including, presumably, the anarcho-capitalism of Austrians such as Murray Rothbard) than it is an argument for some level of government management of natural disasters. By the author's own admission (p. 80), not much is concluded about such management except that, while some such intervention is necessary, it should be prudently limited. For the author, government-directed relief efforts are a legitimate function of the State, which for him exists to protect and secure those rights underlying a free society. Such rights are supposedly violated if some number of citizens (how many?) are permitted to languish as a result of some calamity (natural or otherwise, presumably). He invokes Hobbes's conception of man as a wolf, requiring another, stronger wolf (the State) to suppress and control those base instincts, and allowing cooperation and all its attendant benefits to flourish.

Yet surely this is backwards. To begin with, as Hoppe (2001) has pointed out, governments are composed of *men*, and even if we agree that man is in fact wolf-like, his nature is not changed simply by placing him in an organization and calling it "government." Such an "explanation" could not explain why governments, consisting always of a minority ruling over a majority, can persist. The answer to *this* paradox, as Hoppe (following Rothbard and de la Boétie) notes, is that States, however unpopular particular policies of theirs may be, are always considered legitimate by the ruled. In other words, if a significant number of people refuse to cooperate with the State (or indeed actively resist it), then that State will collapse, and there are many examples even in recent history of just this sort of phenomenon. Thus, cooperation must *precede* the establishment of any social organization (including the State) or, put differently, people must have some recognition of, acceptance of, and respect for property rights in order for cooperation between them to occur. People may have flawed ideas about what constitutes valid property rights (and these misunderstandings are precisely what the State exploits to remain in power), but that is a different issue. If the State is in fact an aggressor and a violator of (property) rights, then it can in no way be considered a protector of such rights, and any case on that basis for government involvement in disaster relief must be rejected. Governments can only assist victims of such disasters by appropriating the property of nonvictims (that is, by violating the rights of *others*).

In other words, governments do not exist to "protect our freedom and thereby facilitate cooperation" (p. 80). Even dictatorships must seek some sort of approval from their subjects, and people must *first* accept *some* form of cooperation as useful or just before they engage in it, such that dissenters from that order may be justifiably punished. Inasmuch as it is man's rationality that permits him to recognize the benefits from peaceful cooperation and specialization under the division of labor,[4] it is

[4]See Mises (1998, chap. 8) and Hülsmann (1999). Hülsmann (p. 716) quotes Mariam Thalos:

also man's mistaken (but correctible) conceptions of justice that permits exploitative institutions like the State to flourish. However, just as man can be disabused of false notions, there is also no reason to suppose that natural disasters "may lead to an escalation of violations of individual rights: assault, fraud, looting" as Ahrens (p. 69) claims. Even if true, that does not justify the government coercing others into assisting the victims of such disasters, and Ahrens has not made the case that this is so. It is not even clear where Ahrens himself draws the line with such interventions, as he views (p. 72) the massive role of the State in welfare and medical care as not "particularly worrisome," and he is not terribly worried about prospective "relaxing [of] requirements of due process" during disaster relief efforts. Ultimately, his essay rests on the contradictory notion that in order to protect individual rights, government must violate individual rights.

The final essay, "Liberty, Policy, and Natural Disasters" by Aeon J. Skoble, is the best one in the collection. To begin with, he is the only contributor who recognizes (though only implicitly) Mises's distinction between case and class probability. Skoble writes (p. 98):

> Insurance companies base their premiums on the information they can gather about similar things, "similar" because although each case is different, one can extrapolate statistically from trends and probabilities. For example, health insurance premiums may be more expensive for a smoker, not because the insurance company knows that *this person* will incur greater medical expenses but because smokers tend to. Auto insurance premiums are higher if you own a late-model car and live in New York City, not because they know that *your car* will be stolen but because there is a demonstrable rate of thefts of certain models.

This superb passage aptly summarizes the issue at hand. And of course, Skoble's point that people who live in South Florida *should* expect to pay higher insurance premiums, and that myriad government programs have encouraged people to engage in riskier behavior than they otherwise would, is correct, although, as has been already argued, it is debatable whether such people should even expect that insurance *can* address the *uncertainty* (as contrasted with risk) they face.

Other parts of the essay deal very nicely with a number of issues already considered: moral hazard and erosion of individual responsibility, media proliferation and propaganda regarding government efficiency, and unwelcome escalations of government power during such emergencies. While his final recommendations for dealing with disasters (restricting agencies such as FEMA to coordinating rather than providing relief, and limiting government activities to "truly unexpected" events [i.e., residents of South Florida should not be terribly shocked that hurricanes strike their area, and should thus not be expectant of benefits obtained by the coercion of others]) consist largely of tinkering, he is fully aware of this limitation and leaves room for more "libertarian-oriented" solutions. In all, his essay is very nicely written and the most forcefully argued and philosophically sound in the book.

> [T]he existence of such a system [the State] presupposes prior collaboration, for how could such a system arise except as a result of very significant collaborative efforts? . . . Prior to anything resembling a legal system that can inflict penalties for breach of contract, what can serve the function of bringing potential collaborators together to erect such a system?

Governments *always* attempt to exploit a crisis, and disasters provide a natural (no pun intended) excuse for them to do so. Their proffered "solutions" to problems (which they often create) invariably worsen those problems. As is the case with general standards of living, economic growth and development—in short, capitalism—has dramatically lessened the impact of Mother Nature. This collection of essays makes these points very clear, and is worth reading for that reason alone. In the end, however, the authors cannot really extricate themselves from the notion that the State simply *must* have some role to play in the mediation of such calamities, and so their case is weakened as a result. By assuming that the State (i.e., institutionalized compulsion) has at least some legitimate function in this case, prospective "privatized" solutions take the form of a square peg in a round hole. In such cases there can be no substitute for private charity efforts, motivated by a true concern for the members of one's group, and tempered by an understanding that it is each individual's responsibility to exercise prudent judgment and to be prepared to bear the consequences.

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