



## Episode 1,277: Private Law and Defense Are No Problem, or The Shortcomings of Public Goods Theory

Guest: Jakub Wisniewski

**WOODS:** Your name has come up on my show a couple of times in the past when I've referred to do debates that Walter Block has had with people. And you have been very patient in at least one of those debates. There's been back and forth of several papers with Walter. But here you have a book of your own that I would like to talk about, because it really is on the cutting edge of Austrian theory here, because you're exploring some, frankly, very difficult topics and challenging topics. And you're doing so in large part by using the tools of Austrian economics, and not merely with abstract theorizing, in other words, without those tools.

So I'd like to begin I think where you would expect we would begin, with an outline of the theory of public goods, why the theory exists, and what the Austrian critique of it is. So what is it? What characteristics does a good have to possess in order for neoclassical economics to classify it as a so-called public good, which, following from that is, the state has to supply it, because it will be under-supplied or inefficiently supplied on the market?

**WISNIEWSKI:** Right, so according to the neoclassical school, if a given good is to qualify as a so-called public good, it has to be non-rivalrous and non-excludable. The first part means that if someone is a consumer of a given good, he doesn't thereby reduce the ability of other potential consumers to benefit from it as well. And then the non-excludability part suggests that a given good generates positive externalities, that it thereby allows for the existence of so-called free riders who benefit from the consumption of that good without paying for it.

And that's why, according to the neoclassical economists, it is difficult or impossible to create a sufficient amount of such goods by means of market transactions, by means of voluntary entrepreneurial transactions. And here is where the normative part of the theory comes into the picture. They suggest that you need the monopolistic apparatus of coercive force in order to force all of the inhabitants of a given territory to contribute to the provision of these goods. And, of course, the most paradigmatic examples of such goods are law and defense. That's how I would characterize the neoclassical approach in a nutshell. And it really hasn't changed that much over the decades, since the '40s and '50s, when those arguments were first produced and spelled out.

**WOODS:** In your book, you give the example of a movie theater as a way to make us wonder about this model and how useful it is and how sensible it is. You give the example of a movie theater that has a certain number of seats, and on any given night, it may have empty seats. Now, it doesn't cost the theater really anything extra to show the movie to 50 people as

opposed to 48 people, so the two empty seats are viewed in this model as some kind of an inefficiency. But then the conclusion from this is so preposterous that it casts doubt on the whole model. So can you explain that?

**WISNIEWSKI:** Yes, the conclusion is preposterous insofar as it would suggest that you would have to nationalize movie theaters and force everyone to contribute to their maintenance. And I believe that intuitively we understand that the conclusion is preposterous for a number of reasons. First of all, it need not necessarily be the case that the individuals who bought their tickets do not lose in terms of subjective utility from the presence of others who have been invited for free. That's where one of the most important tools of Austrian economics comes into the picture. We have to realize that utility is of subjective magnitude. So others may be perfectly willing to pay high prices for the movie tickets in order to enjoy the movie for themselves without being in the crowded kind of situation. And besides, they might feel morally wronged by the fact that others have been admitted for free whereas they had to pay, and that again might contribute to their negative reaction to this kind of policy. And those subjective negative feelings might over time translate into very objective monetary costs for the owners of the theater. So that's one reason why the conclusion flowing from consistent application of the neoclassical theory to this case would be preposterous.

I mean, another reason would be that, even if we were to admit that within certain scope, this notion of non-rivalrous applies, we have to realize that of course the movie theater is limited space, and at some point, all of those seats will be full, and then the so-called crowd effect will kick in. I mean, we might even admit additional people and ask them to sit on the stairs or some other place. So we have to realize that we are still dealing with scarce good here.

And then one might ask oneself, as a manager or as an owner of the movie theater, whether he or she should expand the theater in order to accommodate even more people and provide even more customers the ability to benefit from the consumption of those supposedly non-rival good. But then, of course, he has to ask himself whether this is an economic rational decision, and as we know from the logic of Mises' pioneering essay, he cannot say whether expanding the movie theater would be a rational decision in the absence of monetary calculation. And he can engage in monetary calculation only by being a private owner of the theater and competing for the relevant factors of production. And if we were to think that the conclusion that follows from the neoclassical approach is that you would somehow have to finance those theaters publicly, then of course they would be insulated from monetary calculation in this context.

So all of those decisions would then become completely arbitrary and meaningless. So we see that, to apply and the neoclassical public good theory to such cases, which think are pretty intuitively understandable, yields some highly absurd and economically counterproductive conclusions.

**WOODS:** Let's move on now to the challenging cases of defense and law. You begin with defense, and I think here, people would think that the major issue is the non-excludability, because that leads to the so-called free rider problem. If there is some form of defense in place, then why wouldn't I just enjoy that product and not contribute to its production? And it's hard for people to understand that on some level. Now, you divide up conceptually the idea of defense into different kinds. So for instance, you might have a small-scale example, where you're just talking about maybe some kind of a security guard or something. But then

when you get up to, let's say, larger scale defense, you're talking about ballistic missiles and so on, again, there it becomes more difficult for people to understand how this could work. So first of all, does military defense qualify as a public good under the neoclassical criteria? And secondly, how can we think of its provision, regardless of how you give that answer?

**WISNIEWSKI:** Right, so it would seem that a good such as national defense is, conceptually speaking, the one that fits most closely and most fully within this standard neoclassical framework, because regardless – for example, if we are speaking about anti-missile defense or goods of that kind, it seems that regardless of how many people inhabit a given territory, they are covered by that defense, and they can enjoy this defense regardless of their ability or willingness to pay. So I believe that it's particularly useful to focus on those kinds of goods because, conceptually speaking, they seem to be the perfect examples of what a new classicist means when he's talking about public goods.

But of course, one general problem with classifying any good supposedly enjoyed by free riders as a public good is that this enjoyment is, by definition, divorced from what Murray Rothbard called demonstrated preferences. If someone isn't willing to pay for the maintenance of, let's say, national defense, then in fact we are engaged in vain psychologizing, if we are trying to determine whether it's such a person benefits or not. I mean, such a person might be a pacifist or an anarchist and believe that, actually, the existence of this so-called national defense makes living in a given territory morally dangerous, because it's a tool that continually provokes international conflicts, or at least it has the potential to provoke such conflicts.

And that is why my general line of argumentation throughout the whole book is that this notion of so-called public goods shouldn't be thought of as an economic notion, but rather as a psychological notion, which is not completely empty of meaning or value, but in fact, it should be thought of in terms of something that entrepreneurs have to take into account if they want to maximize their revenue. They cannot be sure whether this or that particular potential consumer is a free rider or not. But if they do believe that he is a free rider, then they have to devise some methods of internalizing the relevant externalities. And of course, whether such externalities exists or not cannot be determined objectively. But again, this is something that entrepreneurs have to take into account as part of their management strategies.

And again, I believe that this applies to this case of national defense, as well. If an entrepreneur working in the business of large-scale defense, anti-missile defense, were to believe that there are certain individuals inhabiting a given territory who do not contribute even though they benefit, then such an entrepreneur might engage in a range of strategies. For example, he might encourage ostracizing such individuals, encouraging others to cut off all business ties with such individuals, since it is unbecoming of them to enjoy the safety of a given community without contributing to its safety.

Another factor that might help in financing the existence of such goods would be voluntary contributions of other entrepreneurs, those who do not work in the defense industry but in some other industry. For example, hospitality or other sectors. In order to boost their reputation, in order to boost the recognizability and the value of the brands, they might engage in voluntary contributions to the maintenance of such large-scale defense goods. And that's another strategy of financing them on the basis of purely voluntary and contractual methods.

And one other strategy that I also mention in my book is that whenever contributions are being collected voluntarily, for the maintenance of such goods, the relevant contracts may include assurance clauses, in other words, the kinds of clauses that assure all of the contributors that, in the event that not sufficient funds are collected, all of the money that they contributed will be reimbursed to them. So that, again, makes all of the contributors aware of the fact that it is not that likely that there might be any free riders who might jeopardize the viability of the whole enterprise.

So as I said, I believe that this is a perfect area for entrepreneurs to exercise their managerial and business skills by devising various strategies, various revenue-maximizing strategies, and internalizing the relevant externalities, understood not so much in economic terms, but in psychological and managerial and entrepreneurial terms.

**WOODS:** What do you think of the approach that Hans Hoppe takes to this question, where he imagines that the solution to this problem comes essentially in the form of insurance companies? That in the same way that, on a small scale, they have an interest in preventing break-ins into your house, and so they give you reduced premiums if you have, let's say, a guard dog or an alarm system or things like that in place, likewise, they would want to prevent the kinds of payouts they would need to engage in if there were a large-scale attack on a lot of people, and therefore they would put in place various defense systems? Is that what you think would happen, or do you think there would be a more varied approach?

**WISNIEWSKI:** I believe that this approach is quite probable. It sounds plausible enough, but I don't know whether this would be the only approach utilized in this context. Again, I believe that the greatest strength of applying this kind of voluntary, entrepreneurial, contractual, and polycentric take on this issue is that you can have a variety of approaches. Insurance companies might be one kind of company interested in providing those kinds of defense services or tying insurance services together with defense services. But I also believe that there might exist communities where specialization and the division of labor is more widespread or more far-going and you have separate entrepreneurial agencies engaged in defense and insurance services.

**WOODS:** Obviously, there's a lot that we can talk about in all these chapters of your book, but just given the constraints of time, I want to give people a sampling of what your arguments are. So let's say a little something then about the other major problem that needs to be dealt with, which is the idea of law. How could law be – we think of law is something that must be provided monopolistically, in large part because we can't even conceive of what society would look like if there weren't one monopoly lawgiver. So what are some ways we can help improve our imaginations on this, first of all, so that it's possible for us to conceive of this the correct way? Because you're saying that it's better to think of law as something that ought to be polycentric as opposed to the plaything of a single monopoly. Are there any kinds of thought experiments or real-life examples that can help us to see why that's the better way to look at it?

**WISNIEWSKI:** It seems to me that if we think of how law developed over the centuries, over thousands of years, then we can come to the conclusion that the so-called civil law or positive law, which is essentially the law understood as a certain set of commands or injunctions imposed on a given society or community by a monopolistic apparatus of violence that controls it, is a pretty recent invention. The way I think about the law is that it's essentially a combination of what has been called the natural law and what has been called common law.

In other words, law consists of a number of objective moral rules and constraints that have to be followed if any kind of peaceful social interaction or cooperation is to emerge, and you do not need any monopolistic lawgiver in order to have that kind of law in place. You have to discover it. You have to deduce it. You have to come to its intuitive understanding. I believe that those kinds of theories are quite prevalent in all kinds of philosophical and religious systems which constitute the foundations of our civilizations. And then you have the common law, which is also very important insofar as it provides the principles of the natural law with the requisite kind of precision and the requisite kind of attunement or correspondence with the specific circumstances of time and place. And again, if a given society or if a given community is to enjoy peaceful and productive social interactions, then it is the members of this community that have to determine what are the specific, detailed rules of conduct that satisfy them and allow them to settle their conflicts in a satisfactory manner.

And the way I conceive of this voluntary, entrepreneurial, polycentric system of law provision is that various competing agencies have to take into account, first of all, those principles of natural law, without which there cannot be any peaceful social cooperation whatsoever. But then also, they have to make the kinds of decisions and they have to publish the kinds of legal codes that aim at discovering the kinds of specific and detailed principles that are simply acceptable by the community in which they operate, which tap into the social norms and traditions and expectations of the members of this community. So on both of these fronts, I do not see any necessary role for a monopolistic lawgiver who simply imposes his arbitrary will within a given territory.

**WOODS:** All right, I hear the logic behind that. And incidentally, we might note that even today, people sometimes interact with each other who are themselves living under a different legal system from themselves, and we have mostly compatible and similar, but nevertheless somewhat distinct legal systems in the 50 states of the United States. But although I can understand how the natural law is always present in the background in the sense that it's impossible to imagine people saying that a legal system that says murder is acceptable is one that anyone would want to live under. Certainly I understand that there are certain things that we would expect everyone to understand. But at the same time, you do have very contentious issues like abortion, like the desirability or necessity of wealth redistribution. How could people who have such different views on these sorts of questions — okay, I see how they have trouble living under one system, because they're constantly fighting about it, but then what's the alternative?

**WISNIEWSKI:** Well, it seems to me that, again, this is one of the greatest selling points of a genuinely polycentric and voluntary system of social organization, which is composed of a multitude of independent economic zones, charter cities, private neighborhood associations, and other property-based living arrangements or institutional arrangements of this kind. It seems to me that the greater the number of such communities serviced by particular competing law or arbitration agencies, the more scope there is for peacefully settling those kinds of disagreements by simply settling in a kind of community which conforms to your very specific, detailed expectations of what a proper solution to settling a given highly contentious issue which might be unresolvable on the basis of natural law.

And it seems to me that — I mean, it would be particularly advisable to have as many decentralized and fully independent communities sharing the same culture, because then the transaction costs of leaving one community and resettling in another community would be quite small. The costs of exiting a given community will be quite small, and also the benefits

associated with being able to influence the policy of that community would be quite high. So what is sometimes called in the literature as the "voice option," as well as something that is called in the literature the "exit option," would be quite easily exercisable in this kind of arrangement. And I believe that's the best solution that we can have on offer when it comes to dealing with those highly detailed moral issues which seem to be irresolvable on the basis of the general principles of natural law, which can't be deducible on the basis of pure logic.

**WOODS:** All right, two more things here. Number one, how would you deal with the concern people would have that, at least in a monopoly system, there's one final arbiter? If there's a dispute, you may not like the way it's resolved, but there is one source that everybody respects. 99.9% of the public acknowledges the legitimacy of the state courts and state adjudication. And so at least you have the benefit of peace being reintroduced, that now, for better or worse, the matter is resolved and the parties just go on about their lives, and they don't perpetually continue fighting it with my company and your company and seemingly perpetually.

**WISNIEWSKI:** I believe that it's a mistake to treat the existence of a monopolistic law provider as being able to impose its will and ending the whole issue definitively. In this context, I like to refer to the distinction which was formulated by our mutual friend, Roderick Long, who makes a distinction between so-called platonic finality and realistic finality. And this notion of platonic finality is precisely that the state is some kind of superhuman, omnipotent organization, which can say, "This or that is my final decision. All of you have to conform," and then everyone conforms.

I don't believe that this is the case, especially in the context of democratic systems of governance, which are internally fragmented and whose constituent elements have to negotiate with each other, have to bargain with each other. I mean, the judiciary, the executive branch, and the legislative branch have to engage in negotiations if they are to maintain some kind of stability within the whole system of governance. And besides, we also live under a system of international anarchy. Various countries also have to and for the most part they settle their disputes on the basis of negotiations and diplomacy. They resort to violent conflicts only in the most extreme cases. So I believe that this notion that the state constitutes this kind of entity capable of ensuring what I referred to as platonic finality is mistaken. Besides, I mean, there exist civil wars, there exist revolutions. So more often than not, the decisions of the state are being conducted in a variety of ways, both internally and externally. So it is not the case that the existence of a monopolistic lawgiver and law enforcer settles this issue.

What we need to focus on is what are the optimal conditions for the emergence of an entity or entities capable of passing the kinds of verdicts that can constitute what I call realistic finality, the kind of finality that, even if it is not entirely acceptable to all of the aggrieved parties, is nonetheless accepted, because this is the kind of solution or the kind of verdict that everyone is willing to abide by in order to maintain some peaceful living relations. And I believe that, again, this kind of voluntary, polycentric system is much more suitable and much more effective in the context of ensuring this kind of realistic finality, first of all, because it's a competitive system. All of those institutions in order to survive in monetary terms have to pass the kinds of verdicts that are really attuned to the expectations of their customers. And secondly, if you have a polycentric system of this kind, then it can utilize what Hayek referred to as the specific circumstances of time and place in a much more effective manner. So they have to be more attuned to the expectations and norms of various

local communities. And that, again, in my opinion, contributes to their ability to arrive at the kinds of verdicts and judgments that constitute not this hypothetical utopian, platonic finality, but the kind of realistic finality that all of the involved parties are willing to accept and to live by, even if they are not perfectly satisfied by its contents.

**WOODS:** All right, one other thing. Let's say you could answer all these kinds of questions satisfactorily and you could lay out why it is that we would expect that, in fact, the market, which produces goods and services of all kinds in ways that are highly satisfactory, would also do so in these areas. You would still have to face the question about what would happen with people who could not afford these services. These are the most — I suppose, second only to food itself, these are the most important goods of all. And so, if the poor can't afford them, then what kind of society is this, where basically the rich would dominate, both in terms of how much protection they'd have and they would dominate the courts, so the law would be skewed to their direction. What kind of safeguards can you offer, at least on a theoretical level?

**WISNIEWSKI:** Well, first of all, I believe that it's a mistake to believe that the law would be secured in the direction of the rich, because again, unlike the monopolistic institution of law provision that we are living under today, which are funded coercively, the institutions that would constitute the kind of polycentric, entrepreneurial system that I'm referring to would simply go bankrupt if it came to pass or if it became public knowledge that they are willing to make their judgments partial to their richest customers. I mean, we have to be aware of the fact that the institutions that operate on the basis of free enterprise are not supposed to — the ones that are the most effective, the most stable ones, the most longeval ones are not the ones that cater to the whims and wishes of a small, rich elite, but are the ones that cater to the needs of the masses and provide the masses with the kinds of goods that they are willing to accept and tolerate. That's one issue.

But with respect to this issue of safeguarding the well-being of the poorest, the ones who cannot afford buying any legal goods or services, again, I believe that it would be highly favorable to the reputation of competing legal and defense agencies to accept various so-called pro bono cases, to agree to represent various poor individuals once in a while in order to boost their reputations, in order to demonstrate to a given society or to a given community that they are willing to engage in charitable activities. We have to be aware of the fact that it is precisely a system which respects the principles of voluntariness and contractuality that is likely to be particularly conducive to the development of a charitable mindset among the population inhabiting such a community.

Because on the other hand, in such a community, various enterprises which provide various goods and services and receive monetary remuneration for their services are able to keep the entirety of the money that they earn. So, on the one hand, they have more resources than the enterprises in a statist community to engage in various kinds of charitable endeavors. But they also have far more incentive to engage in charitable endeavors, because they feel that they are dignified, that they are treated in a dignified manner, that they are not treated as hosts for a monopolistic parasite controlling a given territory, and they are not treated as milk cows that are capable of providing resources for the politicians who would want to distribute them or redistributed them in a populist manner.

So again, it seems to me that one important conclusion that this vision of a polycentric legal and defense system that I sketch in my book offers us is that there is no essential tradeoff

between efficiency and equity. There is no tradeoff between — economics and ethics enrich society, and I believe that society organized along those lines would be far richer than any existing society and would also be an unprecedented moral society, the kind of society where charitable activities engaged both by individuals and by enterprises would be much more widespread, and much more intuitively praiseworthy.

**WOODS:** The book is *The Economics of Law, Order and Action: The Logic of Public Goods*. I'll link to it at [TomWoods.com/1277](http://TomWoods.com/1277). Do you have a website, Jakub?

**WISNIEWSKI:** I have a personal website, a personal blog, [JakubW.com](http://JakubW.com). You might find my blog entries there, you might find links to my online lectures there, and you can also find links to all of my books there.

**WOODS:** Excellent, all right, so I'll also link to that at [TomWoods.com/1277](http://TomWoods.com/1277). This is a book we could discuss for hours, but I thought, you know, given the normal number of minutes I devote to an episode, we could at least give people a taste of the kind of approach you're taking to a problem that obviously needs more work in our area. So I was delighted to hear that you had worked on it and done it and with obviously a complete inside-and-out knowledge of the Austrian literature. So this is an important work, and it's an advanced for sure, and I'm glad that you did it and that you were able to spend some time with us today. Thanks so much.

**WISNIEWSKI:** Thank you. It has been a pleasure to be on your show.