

The Legacy of Progressive Thought: Decline, Not Death, by a Thousand Cuts

Richard A. Epstein*

My task in this essay is to sum up the causes of the American Illness, which by all accounts seems to engulf our nation today¹ Exactly when this illness began is a matter of genuine controversy. It seems clear that American power and prestige peaked at the end of World War II, only to follow an erratic downward course since that time. It is difficult to identify any single cause that accounts for that long-term trend in either domestic or foreign affairs. It is equally difficult to identify any one person who bears unique responsibility for the current condition. But if I had to name one constellation of ideas

* I benefited from comments on this paper made by the participants of a faculty workshop at Ohio State University. My thanks to Frank Buckley for his organization of the topic, and to Brett Davenport, Maxine Sharavsky and Christopher Tan, NYU Law School class of 2012, for their usual prompt and careful research assistance.

¹ For two recent expressions of the point, see Thomas L. Friedman, *Got To Get This Right*, N.Y. Times, Nov. 28, 2010; Frank Rich, *Still the Best Congress That Money Can Buy*, N.Y. Times, Nov. 28, 2010. For Friedman, the solution lies in lower corporate and payroll taxes, and cuts in entitlement programs—all welcome changes. Deregulation is not on his list. Frank Rich rails against *Citizens United v. Federal Election Commission*, and corporate money in politics, a clear nonstarter for structural reform.

that has exerted disproportionate influence, it would be the stunning persistence of Progressive thought in the United States, which more than any other intellectual movement has driven the overall expansion in the size of government for the past one hundred years.

Progressive ideals have been embraced at both the state and national levels, not only through taxation, but (equally critically) through direct regulation, which in turn has spawned a huge growth in follow-on litigation that has multiplied a thousand-fold in recent years. Even in the early Reagan years, no enduring reversal of that trend took place: The major government achievement of the period was to slow the rate of growth, not to shrink the size of government at the federal level. Changing the sign on the second derivative does not a political transformation make.

Whatever the precise path, all pretense of current optimism has faded: The answer to the question, “do you think your children will have a better life than you have today?” generally receives a negative answer,² and for good reason. No longer is it just a matter of slower rates of growth, which has marked the United States since the official end of the recession in the summer of 2009, and which continues unabated through the “jobless recovery” in the winter of 2011. The feeble increases in GDP during this last recovery have been insufficient to offset normal population growth, leading inexorably to the recent two-year decline in average family income.³ The explanation for this negative

² See, e.g., Peter Wallsten & Eliza Gray, Confidence Waning in Obama, U.S. Outlook, Wall St. J., June 23, 2010, available at <http://online.wsj.com/article/SB10001424052748703900004575325263274951230.html>.

³ See, e.g., **WILL GET**

trend does not rest in technological changes, for that pool of knowledge continues to grow. Rather, the explanation has to lie in some cross between our failed political philosophy and our broken political institutions. The decline is not only at the national level, either, for the expression “failed states” is routinely applied to California, Illinois and New York, along with other states that are now overrun by public debt. The financial position of the federal government has declined as well, with higher taxation, greater public expenditure, larger deficits and chronic high levels of unemployment, which just dipped below ten-percent, in part, because of all the discouraged workers who have, at least in the short run, exited the market.

The stark economic system has exacted a steep political toll. In particular, the Congress of the United States is widely held in low repute, with approval rates at under 20 percent. The recent midyear elections of 2010 marked a clear electoral repudiation of the current Democratic policies in Congress. The Republicans made major gains in governorships and state legislatures as well. Ironically, however, it would be a mistake to read into these electoral changes any stunning endorsement of the Republican Party, which when it was in power showed a rare ability to expand the size of government policy for its favored clientele and to increase deficits. Out of office, the Republican Party’s performance has been better, especially in resisting health care and financial reform. Still, the verdict is out for the time being. The current uncertainty and want of confidence in public institutions may itself count as one of the obstacles to a vigorous economic recovery. It is that much more difficult to hire and invest if the government position on such key matters as taxation, regulation and liability are left unclarified. The two questions are: What has brought this impasse about and what should be done to

reverse course before it is too late?

In dealing with these questions, I do not think that any single variable explains the ever more rapid decline in American institutions and practices, which is why the title of this Jeremiad is decline—not death—by a thousand cuts. It appears that the decline has taken place on several fronts simultaneously. To make matters worse, I do not think that there is any new philosophical movement that has driven this decline. It is not as though Marxism or socialism is all the rage, even in the outer precincts of the Democratic Party. Rather, as noted earlier, the most likely culprit of the immediate dislocations is the striking return in the Obama administration to the Progressive ideals of the New Deal, which did so much harm at the moment of its initial triumph. In some sense, the President has not taken the lead on this issue, for he has been pummeled by the left wing of the Democratic Party, which would prefer to nationalize health care through a single-payer plan and, possibly, the banks. In and of itself, a Progressive cast on matters is not alone sufficient to push the nation backward. But it is more than the label that matters. The older philosophy is now being pressed into the service of newer and ever more ambitious programs, whose combined impact can only be to deaden the economy in a thousand ways both large and small.

In this essay, I shall examine several arenas in which I think that these Progressive forces are at work in order to explain why the long-term national prognosis continues to be negative. In sorting out these causes, I do not think that the driving force has come through private litigation, although the expansion of tort liability and class actions is surely an important part of the overall story that needs a proper interpretation. Rather, I think that the chief source of difficulty in the United States lies in the expansion

of direct regulation through the administrative state at the national, state and local levels. In commenting on these issues, some features of the American experience are distinctive; others we share with the European Union, which has its own serious economic difficulties. This paper is not, however, a study of comparative institutional failures, so my purpose is not to show that we do something better or worse than it is done in Europe—or, for that matter, Asia. It is enough simply to show that the United States has done badly in many critical areas relative to any sensible standard of political prudence.

In Part I of this essay, I identify the key features of the Progressive cast of mind—the combination of public deliberation and administrative expertise—that has driven the recent government policies. In Part II, I argue that Progressive policies have led to an unwise increase in taxes and stimulus spending when the appropriate response is a consistent and stable regime of low taxes with no special stimulus program at all. In part III, I extend the analysis to cover free trade in the international arena. Part IV then turns to examine the affliction of permissiveness that affects so much of our regulatory culture at the federal and state levels. Part V takes a look at the recent developments with the Obama health care legislation. Part VI turns to the looming crisis in the entitlement world. Part VII examines employment relations in both the public and private sectors. Part VIII then rounds out the discussion by showing how the Progressive spirit has taken tort litigation far beyond its justifiable configuration. A brief conclusion follows. The clear message is that not one of these major systems works well today, and there is little likelihood of any immediate fix tomorrow. The normative critique thus leads to a pessimistic overall assessment.

I. The Progressive Mindset

The most distinctive feature of the successful Obama 2008 presidential campaign was his uncommon ability to reignite the nation's connection to older Progressive and New Deal traditions. Obama did not run, for example, on the civil rights and abortion issues that dominated American politics during the 1960s. Rather, he returned to the themes of economic security and social justice that defined the Progressive and New Deal Eras. The legislative and administrative actions of these earlier periods worked on well-articulated political philosophies that mounted a frontal assault on the once regnant classical liberal philosophy, which rested on a tradition of strong property rights, open markets, and divided and limited government powers at both the state and national levels. To the Progressives, any effort to bring America into the twentieth century started with their painful recognition that the classical liberal principles of the founding period, which might have worked in a nation of farmers and shopkeepers, could not keep up with the dynamic expansion of the industrialized age—an age in which isolated workers and consumers were pitted against large corporate interests.

This distrust of private ordering led to an intellectual program that lauded the rise of the administrative state, backed by an expanded set of private actions, as the only effective means to curtail the operation of unfettered market forces. The grubby self-interest of the marketplace was to be displaced by a new regime that depended, for its first line of defense, on high-level public deliberation coupled with disinterested administrative expertise. Uncontroversially, the expanded set of duties created a new set of tort actions against parties whose violation of their duties created harms to others. The

truly innovative rule, however, was the decision that compliance with regulatory standards was not a defense against private rights of actions. Rather, the dominant view became one in which regulation set minimum standards, which juries could reject or accept as they saw fit with little or no judicial oversight. Two bites of the apple thus became standard operating procedure. Consistent with the Progressive mindset, this vast expansion of regulatory and private remedies was undertaken on the view that the more legal sanctions the better. This rush to greater government control over the economy downplayed the risks of faction and confiscation, and belittled the role of the traditional institutional safeguards—separation of powers, checks and balances, constitutional protection of economic interests—that had been put in place to blunt their force.

In advancing their agenda of expanded administrative and judicial oversight, the Progressives never thought to distinguish between the size of firms and the structure of the market in which they operated. The classical liberal positions that were displaced did accept the case for the regulation of natural monopolies in such key industries as communications, electricity and power, and strove mightily to devise a sensible set of rules, of no little sophistication, to implement that program in practice. In contrast, the Progressive critique of big business did not limit regulation to natural monopolies, but extended it to all large firms, even those that operated in a competitive market.

The Progressives were often upset about the decline in dickered transactions that led both parties to a contract price, but they were never able to grasp that the low transaction costs from standardized transactions worked for the benefit of consumers and producers alike by increasing the flow of voluntary transactions. Similarly, they looked askance at explicit contractual provisions that limited consequential damages, thinking

that these were a way to escape responsibility for defective products; when, properly understood, their role was to provide incentives for downstream care to avoid serious product losses.

Taken as a whole the contrast could not have been more vivid. The traditional view of markets was aimed at increasing the number of transactions for any given level of transaction costs. The Progressive view took comfort in the high level of transaction costs, which slowed down the volume of market transactions, as if there were some patriotic duty to wait in supermarket check-out lines.

This Progressive philosophy of intervention expressed itself in a wide range of markets, many of which are under siege today. Here are some of the most notable examples: free trade, drug regulation, land use regulation, mortgage and payment markets, health care, labor markets and of course private rights of action under various tort or consumer protection theories. In addition, the Progressive's aversion to competitive markets led to their insistence on a broad class of positive rights against the state, which led to the adoption of the capstone programs of Social Security and, a long generation later, Medicare and Medicaid. These social demands pushed Progressives to champion the progressive tax first as a means to pay for the positive rights that they have championed, and next to insure the redistribution of wealth thought desirable on egalitarian grounds. Their implicit assumption was that high tax rates would have at most a modest effect on productivity, so that the achievement of their distributional goals would generate little collateral damage. The extended "Socialist Calculation" debate of the late-1930s and 1940s is the most conspicuous manifestation of this trend, as many a prominent economist thought they could craft a system of taxes and subsidies that

combined optimal social production with an ideal social distribution of wealth. All problems of information and incentives were regarded as soluble.⁴

Finally, as night follows day, the effort to create powerful government monopolies at home could not take place in an environment in which free competition from overseas was encouraged or even tolerated. Hence the Progressive program featured an acceptance of the need to restrict trade and immigration from foreign nations, both of which compromised the ability of organized labor to maintain its monopoly position in domestic labor markets. At all stages of this program, a larger administrative state was needed to implement every aspect of this new political structure, which in turn could not function well if the perceived limitations on government authority crimped the administrative state.

The thesis of this article is, quite simply, that these various elements supply abundant grist to be ground into an ever-insistent expansion of government power over all aspects of the economy. Put otherwise, the key constitutional and institutional elements for a major level of government expansion were all in place as early as 1940. Most of these elements survived (relatively well) the short-term reaction to the New Deal in the immediate aftermath of World War II—which featured the passage of both the Administrative Procedure Act⁵ and the Taft-Hartley Act⁶—before the Democrats

⁴ Ludwig von Mises, *Economic Calculation in the Socialist Commonwealth*, (1920), available at <http://mises.org/econcalc.asp>; see generally F. A. Hayek, *The Road to Serfdom* (1944) (remarking on Socialist Calculation debate).

⁵ Pub.L. 79-404, 60 Stat. 237, codified at 5 U.S.C.A. §§ 501 et seq

reasserted control of the Congress in the 1948 elections. The Progressive philosophy then reasserted itself during the 1960s, leading to an additional set of reforms with long-term consequences.

The first of such lasting reforms was the entrenchment of public unions, dating to the early 1960s, both at national and state levels. This entrenchment was started by an executive order⁷ of President John F. Kennedy which authorized collective bargaining for federal employees through an unenacted expansion of the reach of labor laws, including multiple extension of the Fair Labor Standard Act⁸ and the adoption of an extensive body of employment discrimination laws, which the unions of an earlier age, with their unenviable record of racial discrimination, had stoutly resisted.⁹ The second was the rise of the environmental movement, which marks, among other things, an expansion of the systems of land use regulation used for zoning purposes. The third was the creation of the large entitlement programs of Medicare and Medicaid to complement Social Security.

I do not regard any of these major innovations as a philosophical departure from the earlier Progressive agenda. They are better understood as a delayed implementation

⁶ The Labor-Management Relations Act (Pub.L. 80-101, 61 Stat. 136, enacted June 23, 1947,

⁷ Executive Order No. 10,988, (Jan. 17, 1962), available at <http://www.presidency.ucsb.edu/ws/index.php?pid=58926>.

⁸ See National League of Cities v. Usery, 426 U.S. 833 (1976), overruled by Garcia v. San Antonio Metropolitan Transit Authority, 469 U.S. 528 (1985); see also Fair Labor Standards Act, 28 U.S.C. §§ 201–212 (1938).

⁹ Title VII of Civil Rights Act of 1964, 42 U.S.C. 2000e et seq.

of business-left-unfinished when the political tides turned sharply against the Democrats in 1938. These issues quickly came back to life after the 1964 Democratic rout of the Republicans under Barry Goldwater. In the end, the complete Progressive agenda has these key features: high levels of marginal taxation, major restrictions on international trade, extensive administrative regulation of private banks and businesses, a large menu of positive rights, strong labor laws and vigorous use of private rights of action to backstop this wide range of regulatory programs.

What is the best way to understand the periodic resurgence of the Progressive agenda? My take on this critical issue is relatively simple. The New Deal settlement was marked by two related elements. The first of these was the constitutional blessing afforded in the post-1937 period to virtually all of these legislative arenas. The second was the extent to which the Congress and the states have, over time, taken advantage of the blank check that was signed over to them by the judiciary.

There were three key elements to the constitutional permission slip granted to legislators. The first was the decision of the Supreme Court to solidify the place of independent administrative agencies.¹⁰

The second was the decision of the post-1937 Supreme Court to give a broad reading to the Commerce Clause, which essentially allowed the federal government constitutional free rein to introduce whatever program of general economic regulation that it found appropriate.¹¹ The federal government could, by virtue of its dominant

¹⁰ Humphrey's Executor v. United States, 295 U.S. 602 (1935).

¹¹ See NLRB v. Jones & Laughlin, 301 U.S. 1 (1937); Wickard v. Filburn, 317 U.S. 111 (1942).

position, block any state law program that was inconsistent with the federal government's objectives. Indeed, with the expansion of the federal commerce power, the question of federal preemption assumed greater urgency: Did the federal government mean to block state efforts, or was it quite happy to have a dual set of controls at both levels, including private lawsuits, which became a staple of the Supreme Court with the expansion of both tort law and the scope of federal power in the years after the Great Society? The recognition of a "presumption against preemption" pointed the way to the exercise of concurrent spheres of regulation over a wide range of activities,¹² where the more stringent was likely to prevail unless Congress clearly stated the opposite. The issue was of especial importance in connection with the possible federal preemption of suits involving state laws, which has been read narrowly except in those cases where the federal law contains explicit prohibitions on private rights of action. Although I shall not explore this development here, the bottom line is this: A deep fear that industry has captured regulatory authorities has unleashed a torrent of private lawsuits in industries like the FDA. But the interventions work in precisely the wrong direction. The paramount need is to find ways to prod the FDA to move forward on new drugs and new medical devices, lest innovation and development move overseas.¹³ Tort litigation only reduces the incentive to innovate further, a point that is missed in the recent implied

¹² See *Rice v. Santa Fe Elevator*, 331 U.S. 218, 230–31 (1947).

¹³ See, for one manifestation, Andrew Pollack, *Medical Device Makers Shun U.S.*, N.Y. Times, Feb. 9, 2011, available at <http://www.nytimes.com/2011/02/10/business/10device.html>.

preemption cases.¹⁴

The third piece of this constitutional settlement was that claims of property rights¹⁵ and economic liberties had relatively little traction outside the area of rate regulation, which was subject to more stringent rules.¹⁶ In the case of property rates, strong property protection was only offered to the right to possess land and exclude others—clearly not a trivial safeguard. But the ability to use, develop, or alienate property was subject to extensive restrictions, blocking easy access to courts and forcing the adoption of a narrow vision of property rights. The result was that it took longer to get to court than ever before, and once the landowner got there, the prospects of relief were in general slim.¹⁷ With respect to economic liberties, an aggressive version of the rational basis test (which imposed a burden on those objecting to a regulation to show that it

¹⁴ Contrast *Wyeth Co. v. Levine*, 552 U.S. 312 (2008) (virtually no implied preemption), with *Riegel v. Medtronic, Inc.*, 129 S. Ct. 1187 (2009); see also Richard A. Epstein, *What Tort Theory Tells Us about Federal Preemption: The Tragic Saga of Wyeth v. Levine*, 65 N.Y.U. Ann. Surv. Am. L. 485 (2010); David A. Kessler & David C. Vladeck, *A Critical Examination of the FDA's Failure to Preempt Failure-To-Warn Claims*, 96 Geo. L. J. 461 (2008).

¹⁵ The truncation began earlier. See *Block v. Hirsh*, 256 U.S. 135 (1921); *Euclid v. Ambler Realty*, 272 U.S. 365 (1926).

¹⁶ *Hope Nat'l Gas Co. v. Fed. Power Comm'n*, 320 U.S. 591 (1944); *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989).

¹⁷ See *Williamson County Reg'l Planning Comm'n v. Hamilton Bank*, 473 U.S. 172 (1985).

lacked a rational basis) made it difficult to attack on constitutional grounds widespread government regulation of all manner of voluntary transactions.

In one sense, therefore, all the necessary pieces for an expanded state were in place by the end of the New Deal. But however necessary constitutional approval is to the expansion of state power, it is surely not a sufficient condition to presage some persistent level of economic decline.

Of greater importance is the extent to which the Congress and the states have, over time, taken advantage of the powers given to them by the judiciary. On that score, it is possible to see where the generational shifts have taken place. There is no question that the interventions of the latter New Deal have exerted, and continue to exert, a powerful influence on the current state of affairs in this country. Even if the various spending and public works of the New Deal withered and died with the onset of the Second World War, the legislative agenda dealing with key matters of labor, agriculture, banking, securities and social security are still very much with us today, in the form of the National Labor Relations Act, the Fair Labor Standards Act, and the Agricultural Adjustment Acts.¹⁸ These trends jumped into high gear, with the aggressive promotion

¹⁸ With time, the ability of an economy to adapt to these shocks improves. The most conspicuous illustration of this transformation is the decline of non-public employee union membership, which grew rapidly after the passage of the National Labor Relations Act of 1935, only to shrink from a peak of about 35 percent of the private labor force in 1954 to a little more than seven percent of the work force by 2009. The relatively stable body of labor law has allowed most employers to develop coherent strategies to control the level of union penetration.

of a legislative agenda that seeks in many ways to exploit the full range of constitutional powers, many of which had not been pushed to their extremes in earlier times. The election of a Republican House of Representatives in 2010 reverses this calculation to a degree, and the current legislative expansion might perhaps proceed at a slower rate or even be cut back, if only through a slowdown in the appropriations needed to secure the timely implementation of the two centerpieces of the first two years of the Obama Administration: the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010¹⁹ on financial reform and the Patient Protection and Affordable Health Care Act,²⁰ or ObamaCare. But, in and of itself, this will not be sufficient to undo the status quo, which has in it the potential for many further general dislocations.

In evaluating the burden of the excessive regulation, liability, or taxation—I treat all three as close substitutes for each other²¹—the relevant comparison is with the outcomes that would be dictated by a pure competitive system. In making this claim, I am well aware that there are many complex industries in which competitive solutions are just not possible. With respect to these, the test of legislative error has to be modified in order to measure the more elusive gap between the current and ideal forms of regulation—which became enormous under the 1996 Telecommunications Act,²² as

¹⁹ Pub. L. 111–203 (2010) (codified at 7 U.S.C. § 1 et seq.).

²⁰ Patient Protection and Affordable Care Act (“ObamaCare”), Pub. L. No. 111-148, 124 Stat. 119 (2010).

²¹ See generally Richard A. Epstein, *Takings: Private Property and the Power of Eminent Domain* (1985).

²² Telecommunications Act of 1996, Pub. LA. No. 104-104, 110 Stat. 56.

construed by the FCC. But in this grand project the details do not matter. What matters is the extent of the deviation from competitive solutions. In dealing with these issues, moreover, I think that it is important not only to consider the initiatives that have been enacted into law, but also those which have been high on the agenda, for even though these initiatives may have failed, the mere fact that they have been proposed skews the universe of legislative opportunities in ways that lead to the prospect of more regulation.

Let us now look at particular cases to see how matters are moving.

II. Taxation and Stimulation

One of the key questions every society has to face is how to allocate scarce resources between public and private expenditures. On that question, the presumption should be set in favor of the private control of investment capital, on the ground that owners of the capital will have the strongest incentives to seek the highest rate of return commensurate with the risk they bear. Capital markets can thus segment in a variety of ways into risky ventures and stable firms. For both types of groups, specialists can emerge on both the equity and debt side of the market, and into equity and debt on the other, with ever higher degrees of specialization. With the proper pricing of these various instruments, investors can then assemble portfolios that fit their own personal circumstances. The decentralized system of control insures that competitive markets can operate at every stage of the process.

This system of course is not self-sustaining, so that no one could think that governments have no claim on scarce resources. The tasks of insuring social order to

protect against violence, to secure property rights, and to enforce contracts requires a monopoly of force that ideally should be in the hands of a government subject to constitutional constraints on the way in which it uses its power. In addition, the creation of infrastructure, which often requires the use of an eminent domain power to overcome holdout problems, also requires a measure of government control, which in part may be contracted out to private operators under various business arrangements. For certain essential facilities—i.e., those with monopoly power—one might need some negotiated limitation on rates. Yet even here, the strong preference should be for private ownership of regulated firms, not for government operation of these facilities.

The underlying issue remains what it always has been, in both good times and bad: What is the sensible role for major government involvement? The ideal mix of public and private roles should in general incline toward low (and broad) taxation coupled with high levels of private investment. One key question is whether this formula works only in times of relative prosperity, or whether it works in bad times as well. In my view, the clear answer to that question is: Stick to your guns. Keep this formula in place regardless of the state of the macroeconomic world. The appropriate way to even out the ups and downs is for private individuals to equalize their wealth across different periods by some combination of two strategies: If cash-poor, borrow in bad times and repay debts in good times; if cash-rich, save during good times in order to cover losses in bad times. Most people and most firms adopt some combination of both strategies, individually and in families.²³ It is yet another version of the Milton Friedman's permanent income hypothesis, by which ordinary individuals, ever-cognizant of their

²³ And it is not without Biblical support. Genesis 41:29-37.

personal diminishing marginal utility of wealth, seek to equalize their income across all time periods and all states of the world.

So long as these private devices of income equalization are in place, the worst possible strategy is one that combines high taxation with public investments that are not directly tied to the maintenance of social order and the creation of needed public infrastructure. The decision to keep taxes high necessarily takes money out of private hands, thereby forcing the government to make its own investment choices so that capital constriction does not destroy the economy. The benefits of decentralized decision-making are lost and the dangers of perverse political intervention become rife, with the government subsidizing just about every silly investment under the sun as “needed infrastructure improvements” or “green friendly” investment. As the huge influx of cash reduces the level of needed quality control on projects that can be exerted from the center, the line between essential facilities and political pork becomes ever harder to police.

The net effect is that job creation will suffer as capital is diverted from sensible to wasteful projects. It is therefore no surprise that the constant succession of stimulus programs done at a grand level has done nothing to improve overall social output on the one hand, or to increase employment levels on the other hand. The constant delusion that the stimulus program will spark consumption that will then create jobs overestimates the ability of central planners to predict how ordinary individuals will respond to infusions of cash. The result is an overall decline in the return from these investments, which is one big reason why the economy is in its current rut and is likely to remain there for the foreseeable future.

The low tax/high private investment strategy thus dominates any stimulus program. The emphasis on higher levels of taxation, of course, is not only tied to the stimulus but also to questions of income distribution. As noted in connection with the permanent income hypothesis, the diminishing marginal utility of wealth surely applies to the way in which people allocate their wealth over time. It also could be used as a basis to allocate wealth across individuals at any given time, which is the heart of the case for the progressive income tax, under which marginal dollars are taxed at ever higher rates. The real hardships at the bottom of the income distribution are hard to gainsay, especially in hard times with jobless recoveries. But it hardly follows that the direct remedy of progressive taxation is the appropriate way to respond to the problem.

The problems with progressive taxation are manifold, starting with how to determine the optimal level of progressivity. Even if we assumed (which is decidedly not the case today) that all tax expenditures were directed toward the creation and maintenance of public goods—social order and infrastructure—the following question still remains: How progressive ought the tax to be in order to achieve the optimal rate of income distribution?

On the one side, low levels of progression generate relatively little income shifting, so that they are not worth the administrative costs that are needed to put them into place. On the other side, high levels of progressivity run the real risk of dulling incentives to produce, which in turn will shrink the overall size of the social pie. However, just because we can identify the two extremes does not mean that it is possible to identify abstractly, or implement politically, some ideal progressive tax that falls between these two extremes. On this issue, the public choice dynamics—“tax the

rich!”—run the real risk that the largest burdens will fall on the most productive members of society. The result is a heavily skewed system where a tiny fraction of the population pays the lion’s share of the income tax, which it then seeks to minimize by a set of socially counterproductive ways to shield their wealth from taxation. Right now the approximate numbers are that about 20 percent of the income is concentrated in the top one percent of the population, which in turn pays 40 percent of the total tax burden. The skewed nature of that distribution indicates that the wealthy are not able to resist the popular pressures for massive income redistribution, which in turn promises a reduction in the overall level of wealth creation going forward.

The sober lesson here is that no form of income redistribution can offset the unambiguous gains from growth. The miracles of compound interest are much with us, and a one-percent increase in growth rates would in the course of a generation lead to nearly a doubling of income.

The pressures in favor of government redistribution would soften noticeably if people paid more attention to the vast gulf between patterns of income and consumption. What happens to the 20 percent of the wealth that one percent of the population earns? Expanding—some would say gorging—on self-indulgent individual consumption is one part of the picture, but it is by no means the only part that matters. First, the highest earners also tend to be the highest savers, and hence the highest investors in new firms and businesses that can create jobs for others. Regimes of high taxation leave less to invest at the outset, and promise a lower rate of return on investment down the road. The net effect is to encourage a shift toward the conspicuous consumption that it is so easy to decry. Second, high income earners do more than just consume or invest. They also

engage in major efforts of redistribution of their own, both to their families and through various charitable activities. The reduced rate of return also dampens these activities, which can easily sap the support that major cultural institutions receive from the largest of donors.

In light of these general considerations, the ideal system would feature a flat tax imposed on a broad base of taxpayers. That system produces a level of rate stabilization that can eliminate the constant class struggles. It simplifies the overall administration of the tax system by removing all incentive to shift income over time and across individuals in order to reduce the tax burden. It makes it easier to calculate the return on investments, which are calculated to increase the size of the social pie. It places no artificial dollar limitation on the amount of cash that can be allocated to the public sphere. It cannot limit the level of subsidies that can be funneled through public transfer programs. But it does place one important constraint on the perils of factional politics: So long as everyone knows that he or she cannot escape his share of those payments, it reduces the temptation of people with low incomes to petition adamantly for high levels of taxation that could increase, in one form or another, the transfer payments to themselves. Thus, if this requirement were put in place in the health care, the desire to subsidize those with preexisting conditions would have to be funded through general payroll or income taxes and not the individual mandate to purchase health care, which lies at the heart of the constitutional challenges to the Affordable Care Act.²⁴ The solution will necessarily be imperfect unless independent constraints can be imposed on

²⁴ Virginia v. Sebelius, 702 F.Supp.2d 598 (E.D. Va. 2010); Florida v. U.S. Dep't Health & Human Serv., Case No. 3:10-cv-00091-RV/EMT (2010).

the spending side, a major challenge of institutional change that I cannot address here.

In light of these considerations, the current unstable system of taxation has to count as a serious cause of the American Illness. Far from creating a stable economic basis over time, the tendency to change short-term tax policies produces an unhappy succession of peaks and valleys that only increase overall levels of social insecurity. Just that result was all too evident from the cash-for-clunkers program that produced an orgy of new car purchases (and old car destruction) followed by a real trough in the industry. The government subsidies for new home purchases had the same result: a short-term burst followed by a long-term decline in the sales of new and existing homes that persists to this day. Stability of expectations is the chief task of any sound tax or regulatory regime, which these programs violated.

The same can be said of the constant tax pressures to impose heavy estate taxes and high levels of progressivity on income tax, which now are determined by short term political compromises with a two year time fuse.²⁵ Whatever income is raised by the estate tax is likely dissipated by the constant efforts to arrange private transactions in ways that minimize its impact—even at the cost of the overall efficiency in the operation of small businesses. The strong effort to impose tax increases on the most productive citizens will just replicate the pattern of short bursts of public revenues coupled with long-term decline, which reduces state revenues even if taxation rates are increased.

One of the key tasks of any sound system of taxation is to develop a stable

²⁵ Nicholas Johnston, Obama Wants Upper Income Tax Cuts Ended in 2012, BusinessWeek, Jan. 06, 2011, available at <http://www.businessweek.com/news/-2011-01-06/obama-wants-upper-income-tax-cuts-ended-in-2012-jarrett-says.html>.

platform that eases the uncertainty in the general marketplace. The stimulus and tax programs which have luxuriated in the past several years, and which can be laid at the feet of the Progressive mindset, count as a major cause of the American Illness. It remains to be seen whether steps will be taken—and if so which ones—to remove the gimmicks, flatten the tax rates, and cut out the stimulus. Such changes are long overdue.

III. International Free Trade

One of the low points of the Great Depression was the passage of the Smoot-Hawley Tariff, which placed a major dent in international trade relationships and hampered economic recovery world-wide during the 1930s. It is, of course, difficult to calculate the exact economic losses of this legislation, but there is no mistake about the negative social consequences it produced, as all tariff regulation adds high administrative costs while simultaneously reducing the gains from trade.

International markets should be informed by the ideal of fostering competition across national borders, just as domestic markets should seek to foster competition within borders. Moreover, the argument for free trade is stronger now than it was during the Great Depression. The effectiveness of competitive markets depends in large measure upon their geographical reach. As communications and transportation become more inexpensive, it makes ever more sense for firms to mount global campaigns to find the most efficient trading partners in order to exploit new possibilities for gains from trade.

In these circumstances, government should seek to facilitate seamless connections between domestic and foreign firms. This objective does not require that all foreign

firms be exempt from domestic regulation, a practice that would give them an unfair trading advantage over domestic firms producing the same product. Thus labeling and purity requirements for foreign goods imported into the United States should be the same as the restrictions that are imposed on domestic firms, and it is perfectly appropriate for the FDA to exercise powers to stop adulterated or misbranded goods at the border. The goal, then, is a nondiscrimination rule which does not distinguish between foreign and domestic firms, and which allows firms that are incorporated in different jurisdictions to compete on equal terms.

The nondiscrimination rule only applies to the regulation of the products and services themselves, not to their inputs used to make them. Thus, if the host nation has a minimum wage law for its workers, it should not restrict imports from nations that do not follow the same policy (which, of course, is not to say that one should be indifferent to egregious rights abuses, such as the use of slave labor). Similarly, the decision of poorer nations to accept less attractive environmental conditions is generally a matter of local concern only. Those conditions will improve without foreign intervention, once the income levels rise, which they will do more rapidly when trade barriers are removed. The simple proposition is that, in any well-governed society, people desire at the margin to achieve the highest possible living standard by a correct apportionment of wealth between public and private amenities, so that the last dollar spent on each yields the same social return as the last spent on the other.

To be sure, many nations do not follow nondiscrimination policies consistently—including the United States. But it is a mug's game to apply unilateral trade sanctions in the fruitless effort to improve the domestic policies of foreign nations, who will most

likely ignore our entreaties and shift their business elsewhere. Once these collateral matters are put to one side, what matters in the end is only the condition of the goods and services rendered, not the mode of their production. Indeed, the entire purpose of the free trade regime is to use a constant and nonselective external check to limit the ability of any group, be it management or labor, to gain a monopoly footing in its own land.

Once this logic of free trade is accepted, then the loss of jobs or customers through foreign competition in any particular instance does not justify any form of legal protection any more than it does when all domestic competition displaces other domestic workers. It is therefore a large mistake to adopt worker retraining programs that drain public resources by subsidizing skills that may well not be marketable in their own right. The better approach by far is to husband the human and physical resources from failed firms, so that they can be recombined into new packages that could prove more successful in domestic and foreign competition. Any effort to forestall this mechanism, whether by trade barriers or currency manipulation, is therefore counterproductive. It is, for example, not feasible to enter into international trade negotiations on the static assumption that any gain in jobs overseas translates into a loss of jobs in the U.S. To do so, as President Obama did in his failed negotiations with South Korea in late 2010, is to engage in false advertising by making it appear as though all international negotiations should be treated as zero-sum gains in which the successes of the United States in creating jobs is exactly offset by the loss of jobs in other nations. “Exporting our Way to

Stability,”²⁶ sends exactly the wrong message because it diverts everyone’s attention from the main focus, mutual gains through trade, which necessarily depends on a willingness to import as well export.

By the same token, it is unwise to seek to weaken one’s own currency in order to spur exports abroad. The strategy can never have any long-term success, even if other nations do nothing to counter the trend. The ability to create competitive exports depends on the ability to secure inputs from firms located all around the world. Let those inputs become more expensive because of a cheap monetary policy and the price of domestic goods will increase in both the domestic and the export markets, reflecting the high component prices. And if the decision is made to shift to a cheaper source for American components, the social loss will manifest itself in a decline in product quality, not in increased price.

Against this backdrop, it is possible to see why the failure in recent trade policy has done much to contribute to the current national malaise. One of the more misguided initiatives in the early Obama years was the Buy-American initiative,²⁷ which was

²⁶ Barack Obama, Exporting Our Way to Stability, N.Y. Times, Nov. 6, 2010, available at http://www.nytimes.com/2010/11/06/opinion/06obama.html?_r=4&partner=rssnyt&emc=rss.

²⁷ American Recovery and Reinvestment Act, Pub. L. 111–5 (2009). Its key provision states subject to exceptions, “no Recovery Act funds may be used for a project for the construction, alteration, maintenance or repair of a public building or public work unless all of the iron, steel, and manufactured goods used in the project are produced or manufactured in the United States.” Dep’t of Energy, Frequently Asked Questions about

imposed in early 2009 and had the nasty effect of adding paperwork at home in order to achieve a less efficient product mix for domestic and foreign markets. That initial mistake has been compounded by the general reluctance of the Obama administration to expand its bilateral trade agreements with Colombia, Panama, and South Korea, in response to opposition from environmental and labor groups. It is surely aggravated by the step-up in efforts to use antidumping laws to keep out subsidized goods from other nations. The revival of American protectionism stands in sharp contrast to the way in which America's competitors embrace free trade agreements, and illustrates how, in this respect, our economic malaise is fairly labeled the American Illness.

The real losers from American protectionism are the American taxpayers who have to bear the brunt of these efforts. The dislocation in the position of some domestic U.S. firms is real, but equally real are the gains the American importers can reap from cheaper imports under free trade. In the end, the case for free trade shows once again the wisdom of the late Robert Nozick in his insistence that “patterned principles”—whereby individuals seek to find the justice in certain institutional arrangements by making some assessment of the end-state distribution of goods, services, and income—are always a delusion.²⁸

In sum, the economic logic of voluntary exchange is not limited to national

the Buy American Provisions, http://www1.eere.energy.gov/recovery/buy_american_faq.html#q1 (last visited Feb. 28, 2011). The Steelworkers are perhaps the most insistent protectionist union in the United States.

²⁸ Robert Nozick, *Anarchy, State, and Utopia* (1974).

borders. The purpose of international agreements is to allow the same principle of comparative advantage that works at home to work in a larger arena. Any efforts to turn the clock back on free trade, in the name of a Progressive ideology, will, in the aggregate, have negative consequences on the efficiency of domestic markets in a way that will contribute to overall domestic decline.

IV. Permittitis

Turning to more national-level issues, one feature of the American decline that bears notice is the rise of the permit culture. I coined the term “permittitis” in connection with the actions of the Food and Drug Administration, which has institutionalized an exceedingly risk averse attitude about allowing new drugs and medical devices onto the market.²⁹ Alas, that regulatory disease is by no means confined to this one federal agency, but has become a staple feature of federal regulation with respect to all dangerous substances—fungicides and toxins—and a wide range of land regulation programs dealing with both environmental and urban growth issues. Although the application varies across subject areas, the consistent pattern represents a misunderstanding as to the proper way of dealing with uncertainty in both public and private disputes.

In all legal settings, the law has to make key decisions on the incidence and sweep of regulation. First, it has to decide whether to stop actions that might cause harm before

²⁹ Richard A. Epstein, *Against Permittitis: Why Voluntary Organizations Should Regulate the Use of Cancer Drugs*, 94 *Minn. L. Rev.* 1 (2009).

they begin, or allow the harm to take place, after which it punishes the activities. Second, it has to decide whether these control functions are best administered by public or private actors.

In dealing with these questions, the first issue is what counts as a harm against which government action should be applied. That question received a relatively narrow definition in traditional legal analysis. The harms that were redressible in the tort system were confined to physical injuries to person and property, and to interference with advantageous relationships by the use of force or fraud. Outside this calculation lie various kinds of social harms, such as the want of green space in the middle of a community or the public offense that one group of individuals takes against the activities undertaken by others. The narrower definition of harms thus limited the potential scope of government action to activities in which the private harm of the plaintiff corresponded with some overall social loss.

Side by side with this definition was the realization that any determination on when and how to use force had to contend with two forms of error. The first involves intervention that is too late, so that the harm actually occurs. The second involves the intervention that is too soon, so that gainful activities that would have otherwise taken place were not allowed to go forward. The traditional private law solution was to call for a mix of injunctive remedies before the fact and damages after the fact, with the balance tilted against early intervention by injunction.

The principle behind this rule is that major financial actors would take appropriate steps to avoid harm, making it appropriate to let them seek independent gain without premature legal interference. These parties would still be pinioned in place by the

realization that an injunction before harm could be imposed when harm became imminent, and that damages would follow if the harm itself materialized.

That rule tended to work well for many years for such key issues as drug development and land development. With regard to the former, the downstream protection afforded by physicians and hospitals made rapid deployment the preferred strategy with drugs, which allowed for the seizure of impure or misbranded products before they reached the market. And with land use, the absence of an extensive permit process allowed the construction of major landmarks, which are far more difficult to build under the current approval process.

No one claimed that this presumption against public permits or licensing was or should be universal. Driver's licenses for new drivers issued after the routine tests is a perfectly sensible form of public regulation that gains salience precisely because no individual driver could ever have the knowledge or incentive to keep anonymous bad drivers off the road. In similar fashion, the condition of public roads and rivers matters as well. Where these are threatened by activities that amount to traditional public nuisances—blocking a right of way, or polluting a river—public administrative action is the best way to attack the issue, up front, leaving injured persons with “special damages” the right to bring individual law suit—a solution that in its modern essentials has been in place since the early sixteenth century.³⁰

The rise of the Progressive era challenged all parts of this synthesis. First, the definition of harm became far more expansive, which in turn led to greater scrutiny of medicines for their adverse side effects, land use regulation for its effect on the character

³⁰ Anon., Y.B. Mich. 27 Hen. 8, f. 27, pl. 10 (1535).

of a community, and indeed for ordinary competition in all sorts of markets. In the land use area, the judicial decisions meant that federal and state governments could prevent most of these newly defined harms without paying compensation to the persons injured therein, which only stoked the demand for further regulation and the political intrigue that went with it. The situation was made even worse as liberalized standing requirements allowed all citizens to move to block various kinds of action with which they had no connection.

That kind of broad-based standing is, I believe, appropriate in those cases where there is a serious question of whether certain government action is ultra vires of its various administrative agencies. But when the activity in question is clearly within the power of the government branch—issuing permits or taking the initiative on public projects—then it is wholly inappropriate. At the same time, the relative balance between the remedies ex ante and the remedies ex post shifted, so that the errors of commission loomed large, while those of keeping new products off the market and new projects off the ground were treated as far less serious.

The explosion in regulation has led to a massive slow-down in the introduction and approval of new drugs. The permit culture with respect to real estate has grown by leaps and bounds at both the federal³¹ and the state levels,³² which in turn mobilizes

³¹ See, for federal intervention, the inconclusive decision in *Rapanos v. United States*, 547 U.S. 715 (2006).

³² On which, see the elaborate procedures for land use approval in New York City, under its Uniform Land Use Review Process, or ULURP,

political opposition, delays new development, cuts down on the local tax base, and generally reduces the level of economic activity in ways that contribute to the overall decline of economic efficiency. Reversing this strong trend is hard to do, to say the least, but undoing the preference for early legal intervention is critical to any program that seeks to reverse the worst effects of the American Illness.

V. Health Care

ObamaCare also represents an expression—but not the only expression—of Progressive sentiments on health care issues. My few brief remarks about this legislation touch on a several key features of the legislation, some of which represent a marked extension of government power.

The first of these features, and the one that has attracted the most attention, is the so-called “individual mandate,” which requires all individuals to acquire private health care insurance or pay the government \$750 per year for the privilege of remaining uninsured. The ostensible justification for this program is to offset a free-rider problem that is created when certain individuals decide to forgo health care coverage, by relying instead on free emergency room coverage in their time of need. In this instance, however, the free rider question does not follow from the public goods character of health care, but from the peculiar set of government regulations that operates on an embedded system of cross-subsidies.

<http://www.nyc.gov/html/dcp/html/luproc/ulpro.shtml>, whose multiple layers of approval have little to do with prevention of abuse.

A public good represents a type of service, like police power or public amenities of all sorts, which can be supplied to one individual only if it is supplied on equal terms, with equal benefits, to all others.³³ The non-excludable nature of the good leaves people with an incentive to sit back and pay nothing toward an amenity that they can enjoy just as much as someone else who pays for it. The problem with this strategy is that virtually everyone can opt for the passive approach, at which point the amenity does not get constructed at all. A set of taxes that matches benefits with burdens is one way to deal with this version of the Prisoner's Dilemma game, by securing the needed funds for projects, which leaves all members of the public better off with the tax-plus-improvement than without either.

Health care does not meet the definition of a public good because it is possible, indeed inevitable, to supply the care to some without supplying it to all. The free-rider problem in question only arises because of the insistence that the cost of health care to some, including elder patients and those with preexisting conditions, be cross-subsidized by others—a provision enjoying virtually unanimous support on both sides of the aisle. The reason, therefore, that many people decline health care is to avoid the cross subsidy.

The individual mandate to purchase health care insurance is just a mandate to participate in the program of cross-subsidies. The supposed free-riding is in part an effort to resist transfer payments to others. It is also part of an effort to get the subsidized care from other means, at least in some cases. Given this pattern, the way to avoid both the subsidy and free-riding problem is to do away with both the individual mandate and the

³³ For the classic account, see Mancur Olson, *The Logic of Collective Action* (1965).

expanded cross-subsidy program that lies at the heart of ObamaCare.

The constitutional challenge that is based on the proposition that Congress has no power to force people to engage in any activity, even if it has plenary power to regulate all economic activities in which people engage, is an odd but effective way to make the point. There is a difference between requiring people to become insured if they drive and requiring people to get insurance irrespective of whether they actually drive. But the real claim here is one of individual autonomy, which has nothing to do with enumerated powers. The police powers of the state would not extend that far either. The case is really a substantive due process case ingeniously packaged as a Commerce Clause challenge when brought against the federal government.

Beside the points expressed above, the current unpopularity of the health care measure could well lead to acceptance of this argument, which gained traction in the Florida litigation of *McCollum v. HHS*³⁴ and the subsequent Virginia suit in *X v. Y*.³⁵ But what happens if the mandate is struck down? It is, in short, a crisis of major proportions. Under current constitutional law, the costs now attributable to the individual mandate could be collected as general taxes from all individuals. The object of the coercion shifts, but the level of coercion remains high. Alternatively, Congress could refuse to find new taxes for the mandate, which is sure to leave the program in limbo. Stay tuned.

As this battle goes on, the larger administrative fight is over the implicit price

³⁴ Florida v. U.S. Dep't Health & Human Serv., Case No. 3:10-cv-00091-RV/EMT (2010).

³⁵ Virginia v. Sebelius, 702 F.Supp.2d 598 (E.D. Va. 2010).

control system that applies to all private plans that seek to gain access to the health care exchanges. These institutions are not involved in the usual kind of exchange, where parties are allowed to list their wares for sale so long as they can make good on their contractual obligations. Instead, these health care plans impose by statute, but fleshed out by regulation, a rich set of obligations that are beyond the means of the people of limited income for whom they are intended. The government thus has to pick up the slack, although (with shades of Hayek³⁶) the government cannot figure out how to set the prices for these services when its own contribution is so large in individual cases, while the private market to which it might otherwise make reference is overheated by excessive government regulation of every element of the pricing system.

It is an open question as to how this will play out, but the one government feature that seems wholly dubious is the requirement of the so-called “medical loss ratio,” which requires individual health care plans to cap their administrative expenses at 20 percent and group plans at 15 percent—figures that are well below current market rates, even before their compliance costs rise sharply under ObamaCare. A huge set of government regulations is now in the process of review as to how this is best to be achieved, but no variation can hit the fundamental point that the price controls cannot bleed out waste in health care any more than rent control can bleed out waste in rental housing markets.

It is therefore no surprise that the government has been inundated with requests for waivers by hard-hit plans, most of which have been granted.³⁷ But government by

³⁶ The Use of Knowledge in Society, 35 Am. Econ. Rev. 519 (1945).

³⁷ For a more extensive discussion, see Richard A. Epstein, *Government by Waiver*, The National Interest (2011) (forthcoming).

waiver is a precarious business because it is never clear who gets these waivers, why they are awarded, or whether they will be renewed. The clear message is that additional employees create additional uncertainties, which in turn puts greater pressure on entitlement programs, an area to which I shall now turn.

VI. Entitlements

The difficulties with the health care system offer a nice bridge to the entitlement question. On this point, the basic structural flaw of Medicare and Medicaid is built-in on the ground floor. The founders of the system have never explained how the consumption of medical services could be constrained when they were offered at a marginal cost of close to zero. The low marginal costs lead to all sorts of overconsumption by people acting in good faith. Whatever the moral case for some “positive” right to health care is, the descriptive consequences are clear. The positive right at zero (or some nominal price) generates an acute over-demand. But at the same time, the want of cash into the system from its customers leads to budget shortfalls, which require an increase in fixed fees (a small part of the current solution) and most critically a massive expansion in taxation to fund the shortfall.

All of this was apparent in principle in 1966, but the politics of denial have pushed us to the point where the budget sleights-of-hand in the initial ObamaCare regulation cannot paper over the systematic shortfalls in the fund. The issue has become so bad that Richard Foster, the fund’s actuary, issued a personal disclaimer to the report he had signed in his institutional role. Foster could not ignore the simple fact that the

harsh reductions in government reimbursements to physicians would have to be lifted for Medicare to continue in operation. It is yet another instance of how disguised price controls necessarily fail.

The entitlement difficulties extend to Medicaid, which in fact becomes a more expensive program under ObamaCare. But here, too, the entire structure is coming apart at the seams. The current proposals require the states to fund much of these costs as of 2014, without supplying the revenue to allow the states to do this. The only way to meet these mandates is to cut other programs that are under stress, given the difficulty of dealing with pensions of unionized public workers, on which more in a moment. Opting out is, however, hard to do because it comes with two strings attached. First, the opt-out requires that the state assume the cost—using its own revenues—of Medicaid payments for the large and costly group of individuals in the 100-133% of poverty range. Second, the opt-out does nothing to allow the state citizens to hold back their Medicaid dollars from the federal program, where they can then be funneled to other states. The whole scheme has the whiff of federal commandeering of state activities, which since *New York v. The United States*³⁸ raises a credible claim that state sovereignty has been curtailed by overzealous federal oversight—an argument which may have some constitutional legs.

VII. Labor Markets

The next piece of the puzzle involves employment markets. Left to their own devices, employment markets are competitive, so that direct regulation is hardly needed.

³⁸ 505 U.S. 144 (1992).

But by the same token, there are powerful institutional pressures that could easily make these markets a hotbed for government regulation, to be enforced by some combination of direct control and private litigation. One clear reform is to undo this whole regulatory structure, which is more easily said than done. But any analysis of the American Illness requires at least some consideration of these issues, both for public and private unions.

A. Public Unions

It is quite clear that President Obama and many of the Democratic members of Congress owe their political lives to the strong intervention of American labor unions, which are active in both the public and the private spheres. It is equally clear that the same level of political dependence is found at the state level as well. At present, the most conspicuous feature of most state budgets is that their balance sheets are in desperate shape because of the tens, if not hundreds of billions of dollars, in deferred pension obligations that cannot be met from current sources of public revenue. The situation has boiled over as of late as governors of many Republican states are pushing hard not only for union concessions but for a more fundamental reorganization of bargaining in the public sector that puts a hold on union monopoly power—a proposal that is fiercely resisted by Democratic legislative walkouts, including both Wisconsin and Ohio (as this is written), with more likely to follow.

The short-term impasse is so acute that the absolute priority of these pension obligations over other state budget items have led to a sharp contraction in funding for education at all levels—from K-12 on the one hand to university support on the other.

Moreover, other social welfare services have been cut back as well. Until recently, the dominant strategy has been to try to negotiate some givebacks with respect to future pension obligations, both for current workers and for those who have yet to be hired. These two-tier systems (which are also invoked in private labor negotiations with unions in declining markets) offer powerful testimony to the enduring monopoly power of labor unions in many key service industries. No such price discrimination is possible in competitive markets.

The overall disparities between public and private wages have been often noted and much deplored. Yet now that these wages are entrenched, it will take a powerful antiunion coalition to undo these vested rights. By the same token, however, it often takes only the signature of the governor to extend certain key privileges—the card check is one—to government employees, with a consequent increase in union power.

One specific approach, which has gone from the improbable to the highly possible in a matter of months, is to engage in massive decertification of public unions at all levels, coupled with a major revision of union wages and especially pension benefits until these budgets are brought into balance. The current law treats union contracts as vested constitutional rights that cannot be reversed by legislative action. I believe that this conclusion is premature, at least before it is attacked in concerted litigation. The level of political influence that led to the expansion of pensions for union members shows a degree of political self-dealing. There is little doubt that any corporate officers who sought to create these sweetheart deals for their employees (in exchange for political support) would be set aside as a breach of fiduciary duty. It is hard to achieve that result in the public context. Indeed, at the federal level there is some question as to whether

taxpayers or citizens even have standing. But it is surely worth the effort to mount those challenges in light of the evident size of the stakes. In addition, any ability to subcontract work to nongovernment employees should be strongly supported as yet another way to undo union power in this area.

In dealing with these issues, it is probably a mistake to think that only unionized systems are vulnerable to expropriation. The problems go deeper because other nonunion parties can obtain similar benefits. One sensible way to deal with the system is to monetize all future pension obligations by simply switching, as private firms have done, from a defined benefit plan (where the shortfall lies with the state) to a defined contribution plan that liquidates all future liabilities at the moment of payment, and forces workers to decide the best pattern for asset allocation with their portfolios. For these purposes, the key point is that the dollar figure allows for prudent cash management at the state level, and for greater public oversight of the entire process. That system is compatible, moreover, with any independent rules that limit the amount of money that recipients can allocate to equities or other risky ventures. What is desperately needed is a way to stop the excesses.

B. Private Unions

The situation with private unions is more complex. As noted earlier, union membership has been in steep decline, and it seems clear that the best union strategy for organization under current laws is likely to fall short when confronted with the best management defense. That result does not occur because management has received some

hidden bonus from a change in the substantive law in recent years; labor law has been very steady for at least the last fifty years.

It is far more likely that the result derives from the ability of most employers to avoid the silly mistakes in employee relationships that could easily turn their workers against them. Unions have constantly attacked employers for their all-out resistance to organization campaigns. But while unions have been quick to denounce the effectiveness of such resistance, they have been much more hard-pressed to prove that labor's organizational setbacks are attributable to employer unfair labor practices that have either gone undetected or been punished with only a mild slap on the wrist. The signs of unionized failure in major industries—automobiles, steel, and construction, for starters—are known everywhere. The expected gains to workers from staying out of unions are greater than those of joining unions, once the risks of lost wages and benefits to layoffs, strikes and bankruptcy are taken into account. Employers may not be allowed to make threats of what they will do to respond to unions, but they are surely allowed to make predictions, usually painfully accurate, as to the likely outcome of union membership. The drive from within is just not there.

In response to this decline, unions have resorted to a variety of other tactics that do not require their success at the bargaining table, and on these unions have been far more successful. They have pressed the Obama administration and state governments to make unilateral changes through executive order whenever this is possible. The Obama administration has put through recess appointment Craig Becker on the National Labor Relations Board, knowing full well that he was not confirmable by an up-or-down Senate vote. More recently, the White House's Middle Class Task Force, headed by Vice

President Biden, has announced an initiative whereby the American Bar Association and the Department of Labor will pair up to bolster the enforcement of the Fair Labor Standards Act (“FLSA”).³⁹ The “Middle Class Task Force” should be understood as a term of art for organized labor’s drive to secure the passage of labor reform, including the Employee Free Choice Act.⁴⁰ At present, there are about 6,000 class action lawsuits under FLSA, each of which can be initiated by a complaint from a single employee.⁴¹

Unions have also been active in opposing free trade by filing antidumping cases under current law and pushing hard to slow down the rate of bilateral trade agreements with places like Colombia and South Korea. At the local level, unions have pushed hard to use zoning ordinances as a way to keep big-box stores out of urban areas where they stand a good chance of underselling their more established unionized rivals, which have, on average, expanded at a far lower rate than the nonunionized firms. Unions also have fought for increases in the minimum wage law, an effort that has had more bite than

³⁹

<http://www.whitehouse.gov/blog/2010/11/19/helping-middle-class-families-pursue-justice>.

⁴⁰ See, e.g., the Congressional Hearings that have used that title. Strengthening America’s Middle Class Through the Employee Free Choice Act: Hearing on H.R. 800 before the H. Subcomm. Health, Employment, Labor, and Pensions, 110th Cong. 4 (2007).

⁴¹ See 1-800-Trial Bar, Wall St. J., Nov. 27, 2010, available at http://online.wsj.com/article/SB10001424052748704369304575633482885808438.html?mod=WSJ_Opinion_AboveLEFTTopWall.

anyone expected given the collapse in demand for labor after the market meltdown in September 2008.

For the moment, at least, unions have failed to gain traction for their most powerful reform, the Employee Free Choice Act (“EFCA”), which goes far beyond the National Labor Relations Act of 1935. The earlier statute had two features which, with time, have become bulwarks for the employer. The first was the requirement of the secret ballot at the close of any organization campaign, which does much to eliminate the risks of coercion from either side. The second was the ability of the employer to bargain to impasse, on the ground that the requirement of bargaining in good faith did not require either side to make any particular concession, which meant that employers could not just stonewall employees at the outset—but the employers could hold firm.

EFCA promised to work a transformation in both of these key features. The card check of eligible workers allows a union to force the election if fifty-percent of the members of a relevant bargaining union sign up. Once that is done, a form of binding interest arbitration awaits the firm that cannot enter into a binding first contract with a union within 130 days of the official recognition of the union. The arbitrations are chosen by unspecified processes by a political employee in the Department of Labor, the most politicized of the cabinet positions. These provisions have rightly provoked a fierce and unified managerial opposition, and their defeat will surely help to loosen labor markets in the short-run. But the adverse effect that the provision had on job formation during the first year or so of the Obama administration is hard to calculate.

VIII. Tort Liability

The last portion of the Progressive synthesis that I want to touch upon has to do with the radical expansion of tort liability through the common law system. Anyone who took a snapshot of tort law in 1850 would have seen a field that was dominated by private liability of landowners and others for harms committed against the person or property or strangers. At this point, a tough legal system that deals with these “boundary crossings” has a strong libertarian feel to it, given that the law’s major function is to reinforce the separation between neighbors. The rules in these cases tend, imperfectly, to gravitate to a strict liability system that does not allow parties to escape liability by showing that they exercise due care or had no intention to harm. Indeed the most conspicuous expansion of liability in this period was through the doctrine of vicarious liability under which employers, including the newly minted corporations, could be held responsible to strangers for harms that arose in the course of their employment. Meshing limited with vicarious liability was a great achievement, insofar as it expanded the pool of assets available to protect strangers, by encouraging unconnected strangers to contribute fixed and bounded sums to a common venture.

The changes in the twentieth century, which are now seeping into the twenty-first century, require a more subtle analysis. The vaunted expansion of product liability law through the first 60 years of the twentieth century was largely sound and fury signifying nothing. On the medical malpractice front, tort liability was universally limited to cases of physicians who deviated from the customary standard of care, where the notion of custom gave the physician the benefit of choosing what school of practice to join. In effect, non-contractual standards were not superimposed on private behavior. The newly

minted system of strict liability for defective products was likewise hedged in with sensible limitations that prevented its undue expansion. Thus, after a prolonged oration of how it was “to the public interest” to run a risk sharing program through the tort system, Judge Roger Traynor concluded his remarks with the observation that the new strict liability system (which was in any event not very different from the system that put the burden of disproving negligence on the defendant) only applied when the product was still in its original condition when the defect manifested itself, and that, even then, recovery was only permissible when it was used in the normal and proper way.⁴²

In effect, the better production techniques meant that tort liability rules were but a ripple on the pond until one key development: the inability to vary the rules of the game by voluntary contract, which arose in 1960 in the first product liability cases⁴³ and shortly thereafter in medical malpractice cases.⁴⁴ The hostility toward freedom of contract that had worked itself through so many other parts of the legal system finally crept into the tort law. The key feature of this new approach was that it made it impossible for private parties to correct allocation mistakes made by judges in setting out what they thought were the correct rules of the system.

It was only a matter of time until the expansionist tendencies that were part of Progressive thought worked themselves into the fabric of the law. On the malpractice side, the standards of care became more exacting, the proof of causation more pliable and the level of damages more expansive. Similarly, on the product side, the definition of

⁴² See, e.g., *Escola v. Coca-Cola*, 150 P.2d 436 (1944).

⁴³ *Henningsen v. Bloomfield Motors*, 161 A.2d 69 (N.J. 1960).

⁴⁴ *Tunkl v. Regents of Univ. of California*, 60 Cal. 2d 92 (Cal. 1963).

defects expanded, and the normal and proper use defense quickly eroded until the presumption was that upstream providers had to take care of downstream users even against conditions that were fully disclosed and thus remediable by a user, or (in workplace situations) a user's employer. All of these changes were multiplicative, at which point it is easy to see how the overall system can start to overload, with the usual negative effects on innovation.

Conclusion

The basic thesis of this article is that the combined impact of bad government policies has taken its toll on the fabric of American institutions. We speak now of the American Illness, and the once familiar talk of American Exceptionalism becomes an ever more distant memory, invoked today only with a sense of irony that it does not remotely describe our current situation.

The implications of this great transformation in the American economy and psyche are not easy to predict. As a general matter, the weaknesses at home will lead to systematic weaknesses abroad. God favors the big battalions in international affairs. The decline in American production leads to constant calls to weaken the military presence overseas, which in turn allows nations like China (who have thus far avoided some of our structural mistakes in their youthful capitalist phase) greater sway in international affairs, which in turn will make it more difficult to succeed in a variety of international commercial ventures.

Domestically, the want of one single national cause is what makes it so difficult to

reverse a pattern of behaviors and laws that have become so entrenched in the American psyche. But the effort has to be made. The fact that major declines come from multiple causes does not mean that they do not have long-term corrosive effects. Unless and until we embrace the classical liberal provisions that allowed for innovation and growth, we can expect more of the same: a grim stagflation in which technological improvements cannot quite offset the major dislocations in the regulatory state, for which we have the Progressive movement to thank.

The final inquiry is what lesson do we learn from this set of disparate elements. The major lesson is that it is not so disparate at all. The changes all come with distinct doctrinal labels in what appear to be unrelated substantive areas of law. Each of these changes is made on the implicit assumption that the rest of the system remains constant, so that the interactive effects of different maneuvers are never made part of the law. The inability to trace long-term adverse consequences to earlier political maneuvers lends the entire operation political cover. Since we are no longer dealing with push-pull relationships, it is easier to argue that there is always something, indeed anything, else that accounts for the brake that is seen on development. But the dangers here lie in the compounding of these errors over long periods of time. No one can say that any of these changes itself is that “big,” but assume modestly that if all these errors are put in the right position for a period of many years, and lo, one comes up with the conclusion that Robert Cooter develops in his excellent essay in this book. Think growth over the long run, and you will not do too badly in the short run. As a general matter, the gains from long-term overall improvements will swamp the supposed gains from short-term ameliorative programs. This leads to the final irony. The Progressive movement is an intellectual

failure because it stifles the long-term systematic growth and social welfare that its supposedly “scientific” foundation was intended to promote.