

# Reply to Commentaries on ‘The Labour Theory of Property and Marginal Productivity Theory’

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## Abstract

Jamie Morgan’s commentary (Morgan, 2016) on my paper ‘The Labour Theory of Property and Marginal Productivity Theory’ (Ellerman, 2016) and Ted Burczak’s later comments (Burczak, 2016) raise a number of issues that surely will occur to other readers and that need to be addressed. I take the occasion to expand upon the arguments and to explore some related issues. In the narrative that unfolds, Frank H. Knight plays the role of the sophisticated defender of the system of renting, hiring and employing human beings. He was quite clear that the social role of economics is to develop an idealised model, the competitive free enterprise model, and then to frame the normative discussion in terms of that model. Knight would agree with the whole thread of heterodox ‘criticism’ that the actual economy falls far short of the ideal – which is why I largely eschewed the descriptive shortcomings of ideal model as a purported model of the actual economy. Instead my paper focused on developing a critique of the key part of the *idealised* model, the marginal productivity theory of distribution under competitive conditions. That critique is based on the usual juridical principle of imputing legal responsibility in accordance with factual responsibility – the principle whose property-theoretic application is the modern treatment of the labour theory of property.

Historically, heterodox economics faced a fork in the road in the 19<sup>th</sup> century: whether to criticise ‘the system’ by developing the inchoate ‘labour theory’ as a theory of value or a theory of property. Marx and much of left-wing economics took the labour-theory-of-value road, whereas my paper is part of a modern attempt – Thomas Hodgskin (1832) being an earlier attempt – to take the labour-theory-of-property road. As we will see, much of the debate still revolves around these two roads.

**Keywords:** labour theory of property, power relations, employment system of renting persons, Marxism, theories of exploitation, the corporate legal form

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## 1. Introduction

I am grateful to both Jamie Morgan and Ted Burczak<sup>1</sup> who made substantive comments on and raised good questions about my paper, ‘The Labour Theory of Property and Marginal

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<sup>1</sup> Full disclosure: Ted Burczak is a long-time supporter of the modern treatment of the labour theory of property as expressed in his book *Socialism after Hayek* (2006). The late dean of American institutional economics (whose specialty was theories of property), Warren Samuels, read the book and supplied the dust-jacket blurb that read in part: ‘Burczakian socialism = (Hayek + Nussbaum + Sen + Ackerman + Resnick and Wolff) = Ellerman = legal-economic democracy. Brilliant!...’ I credit Burczak’s book with helping Samuels to fully understand that treatment of the labour theory of property. When he died, Samuels was at work on the second draft of a paper entitled: ‘On Precursors in the History of Economic Ideas: Is Karl Marx a Precursor of David Ellerman?’ (2007). We were in disagreement about the paper since I was in favour of the ‘fork-in-the-road’ imagery and argued that a whole lot of misunderstanding would result from presenting Marx’s labour theory of value as a ‘precursor’ along the same road as the modern labour theory of property. Some quotes from Samuels’ unpublished paper are in Ellerman (2014). My objections were summarised in my later paper on Marx (Ellerman, 2010).

Productivity Theory' (Ellerman, 2016) on the *Economic Thought* Open Peer Discussion forum. Many of the points they raise will surely occur to others and really need to be addressed.

## 2. Power Relations and the Maldistribution of Wealth

One general point of Morgan's commentary was that my treatment of the labour theory of property (LTP) did not address power relations (typically resulting from the maldistribution of wealth). In this case, my reluctance to go charging into the swamp of discussions about economic, political, sociological and psychological 'power relations' was deliberate. The fact that most real-world contractual relations involve inequalities of power and wealth is surely a truism. The real point is that power relations are irrelevant to the critique provided by LTP since it is *not* a critique based on unequal power relations and thus the critique would not be resolved by, say, wealth redistributions or more countervailing power to collectively bargain the human rental contract.

There is a logical or methodological point at stake here. The point is that if one is going to criticise a practice or a whole system *because of X* (e.g., unequal power relations or the maldistribution of wealth), then one is implicitly accepting the framing that this X-critique of the practice or system would be resolved if X was removed. If a defender of the system posits a version without X and the critic says, 'It's still wrong,' then the defender is well justified in asking: 'Why don't you tell me the real reason why you think the system is wrong, and stop engaging in apparently ancillary discussions about X?'. Morgan says the presentation of LTP is perhaps 'incomplete' because it lacks this sort of ancillary discussion about X = unequal power relations.

In contrast, neoclassical theory does have a theory about power relations expressed in the juxtaposition between the ideal of competitive markets on the one hand and monopolistic/monopsonistic markets on the other. There is also a neoclassical theory of exploitation which applies to the non-competitive case which would fall short of the ideal since input suppliers would be paid less than the value of the marginal product of their inputs and output buyers would pay more than the marginal cost of the outputs. Thus neoclassical theory does have a theory based on power relations, the power of a monopsonistic buyer of inputs or a monopolistic seller of outputs.

The neoclassical apologists for the employment system would like nothing better than to have an excuse to avoid the main point about the inalienability of responsible agency in favour of engaging with critics in endless discussions about the economic, political, sociological and psychological nuances of power relations – in addition to the usual discourse about making markets more competitive. I made it quite clear the LTP critique was *not* based on such power relations and such resulting 'exploitation', and I take that to be a virtue of the theory, not a vice.

Ted Burczak raises a related point about the causal relationship between the maldistribution of wealth and the employment relation.

'Is the employer-employee relationship really the cause of income and wealth inequality (as the outcome of labour leveraging) or is the employer-employee relationship the result of unequal distribution of productive assets?' (Burczak, 2016).

Surely the answer is that the causal relationship is one of circular causation (as Gunnar Myrdal called it) in a case of self-reinforcing 'positive' feedback.

This raises a second methodological point. When asking a question about our system of renting people, it may be very helpful to transpose the question to one about the earlier system of owning other people, i.e., slavery.

For the question in hand, there was also a relationship of circular causality between unequal power relations (e.g., between victor and vanquished in battle) and slavery (e.g., enslaved prisoners of war). Greater power created more enslavement, and more slaves (as soldiers and workers) created greater inequalities of power. Surely one can recognise that circular self-reinforcing dynamics in either the case of owning or renting other people without therefore concluding that the problem lies in the unequal distribution of power. Would voluntarily owning or renting other people be acceptable if it arose, for whatever reason, out of essentially equal power relations? The analysis based on the labour theory of property and inalienable rights would apply just as well in that case of essentially equal power relations so I did not engage in such an ancillary discussion – although the commentators have good grounds to raise those questions explicitly.

### 3. The Consequences of Abolition

Burczak raises a related question about the consequences of abolishing the system of renting people (e.g., by a constitutional amendment) while leaving intact 'given the current distribution of wealth'.

The first point to make is that while the maldistribution of wealth is not 'the problem' *per se* in the institution of renting people, the critique of the misappropriation of the whole product (whose value is the profits) in the employment system is, *by the same token*, a critique of the past maldistribution of wealth *resulting* from that 'institutional robbery' (there are, of course, other unjust sources of wealth such as conquest, violence and ordinary uninstitutionalised fraud and robbery). Hence the abolition of renting people in the future would not, by itself, address the even trickier question of rectifying past robberies. It would be like abolishing slavery while leaving the whole *ante-bellum* system of wealth intact, e.g., not supplying '40 acres and a mule' to the freed slaves, which is exactly what happened historically.

This reaches to second part of Burczak's point:

'Could it be possible that many of us would be better off (in terms of material standard of living) to allow the rich to hire the non-rich into employment relationships, thus mitigating the desirability of abolishing wage-labor?' (Burczak, 2016).

Using my second methodological point, we can transpose the question back to slavery to see a similar problem for the freed slaves.

'But the sanctity of personal freedom in Western legal systems, the doctrine of inalienable rights, makes it impossible for a person effectively to pledge his future earning power in exchange for present resources' (Knight, 1947, p. 152).

The freed slaves, lacking the freedom to sell or mortgage themselves by the doctrine of inalienable rights, lacking the necessary capital due to the Radical Republican proposal of '40 acres and a mule' failing in Congress, and possibly lacking some of the knowledge and skills

to operate as independent farmers, resulted in many becoming sharecroppers and debt peons (often to their former masters) – a milder ‘slavery by another name’.

Burczak considers a concrete example.

‘For instance, if the law prevented my relatively richer (in capital and talent) local roofing contractor from hiring employees and if, as a result, that contractor only accepted self-directed tasks that s/he could complete alone, leaving the potential employees even poorer in an absolute material sense, why would we want to embrace such a legal regime?’ (Burczak, 2016).

Firstly, it should be noted that in the Yugoslav socialist version of ‘self-management’, the small family/craft businesses were allowed on simple pragmatic grounds to have a few (e.g., up to five) non-member workers.

Secondly, even with a universal requirement of, say, the worker cooperative form of business, there is always a tendency to reproduce the employment relation by having a semi-permanent class of temporary or probationary workers who are not members – as is happening around the edges of the Mondragon cooperatives. That may well be the outcome of the roofing contractor if the cooperative requirement was imposed without other changes.

In the US today, we still have the legacy of slavery over a century-and-a-half after the abolition of slavery (without the broader changes) and where the freed slaves were only a small portion of the population. It is difficult to imagine the changes that should be made after centuries of the human rental system and where the ‘unrented’ workers would constitute ‘the great mass of the population’ (Knight, 1965, p. 271). The relatively smaller changes to go from subjects in a monarchy or other autocratic government, to citizens in a political democracy is still a work in progress in the industrialised countries and still has a long way to go in much of the world.

#### **4. Basic Neoclassical Apologia Based on Voluntariness, not Absence of Power Relations**

Furthermore, the *basic* neoclassical-Austrian-classical-liberal defence of the system of renting, hiring or ‘employing’ people is not that markets are ideally competitive (when they really aren’t) but that the market contractual relations are *voluntary*. Unfortunately, most of the left-wing criticism argues that wage labour is  $X =$  ‘not really voluntary’ – which is superficial because it accepts the classical liberal framing that human rentals would be acceptable if they were ‘truly’ voluntary. And then defenders and critics of the system can again charge off with swords waving into the bog of arguments about whether or not unequal power relations prevent market contracts from being ‘really’ voluntary.

One way to better understand the neo-abolitionist critique of a truly voluntary contract to rent persons (Ellerman, 2015), is (using the second methodological point) to transpose the arguments back to a hypothetical economy based on civilised voluntary slavery contracts. The most sophisticated defenders of slavery argued in favour of an idealised system of implicitly or explicitly voluntary self-enslavement contracts in which the employer could buy labour by the working-lifetime instead of just for specified periods of time. They recognised that the existing system of slavery often fell far short of that and they wanted to reduce those abuses.

Who were some of those sophisticated defenders of voluntary slavery contracts? The most sophisticated modern defender of the human rental system was Frank H. Knight who

pointed out that Adam Smith's classical liberal defence of competitive markets was built on a foundation provided by the three pillars of classical liberal thought.

'The classical exposition of the new doctrine in its positive aspect was Adam Smith's *Wealth of Nations*, published in 1776. Interestingly enough, the political and legal theory had been stated in a series of classics, well in advance of the formulation of the economic theory by Smith. The leading names are, of course, Locke, Montesquieu, and Blackstone' (Knight, 1947, p. 27, fn. 4).

As I have pointed out elsewhere (e.g., Ellerman, 2010a, 2015b), all three of these founders of classical liberal thought *accepted* a civilised voluntary slavery contract. Locke's defence of such a contract, which he renamed 'drudgery' (*Second Treatise*, §24), is too well known to quote, but the passages from Montesquieu and Blackstone are little known.

'This is the true and rational origin of that mild law of slavery which obtains in some countries; and mild it ought to be, as founded on the free choice a man makes of a master, for his own benefit; which forms a mutual convention between two parties' (Montesquieu, 1912 [1748], Vol. I, Bk. XV, Chap. V).

Like Locke and Montesquieu, Blackstone would reject an uncivilised 'contract' where the master had the power to legally kill the slave and such a slave would be free 'the instant he lands in England'.

'Yet, with regard to any right which the master may have lawfully acquired to the perpetual service of John or Thomas, this will remain exactly in the same state as before: for this is no more than the same state of subjection for life, which every apprentice submits to for the space of seven years, or sometimes for a longer term' (Blackstone, 1959 [1765], section on 'Master and Servant').

In spite of being defended by Knight's 'great names' in classical liberal thought (not to mention modern libertarians such as Harvard's late Robert Nozick (1974)), the voluntary master-slave contract is today recognised as being invalid in the advanced democracies. What are the reasons why it is outlawed?

- Was it because the real wages (paid in food, clothing, and shelter) of the slaves were below the value of their marginal product (or contained less labour-time than was expended by the slaves) – which would only imply higher real wages?
- Was it because of the hugely unequal power relations between the prospective masters and slaves – which would only argue for some countervailing power on behalf of the slaves?
- Was it because of the obscenely unequal distribution of wealth and income between masters and slaves – which would argue for redistributive policies like the more progressive income taxes, larger estate taxes, and perhaps a guaranteed minimum income suggested by today's progressive reformers to address today's human rental system?

No, these were not the reasons why that voluntary contract was *abolished* (as opposed to being modified or reformed in the above indicated ways). The self-sale contract, like today's self-rental contract, is invalid for reasons inherent in the contract itself, not because of the inevitable inequalities in power relations used to get people to consent to it. I have elsewhere (1992, 2010a, 2015a) outlined the intellectual history of the inalienable rights doctrine that descends to modern times from the Reformation (inalienability of conscience) and the Enlightenment through the abolitionist and democratic movements. That critique also applies to the voluntary human rental contract that is the basis for today's employment system. This neo-abolitionist critique is not grounded on the X of power relations (or non-competitive markets in the neoclassic proffered self-critique) – or for that matter on the whole train of X, Y, and Z abuses so well described by Marx the economic sociologist/historian in his volumes of moral invective<sup>2</sup> that covered up for the lack of a sound theoretical critique based on the labour theory of value and exploitation.

Frank Knight was annoyed with, and suspicious of, the whole idea of inalienable rights; if there was something inherently wrong with buying labour on a long-term basis, then he might have correctly sensed that the same sort of argument would apply to the short-term rentals of persons – for as James Mill put it:

'The only difference is, in the mode of purchasing. The owner of the slave purchases, at once, the whole of the labour, which the man can ever perform: he, who pays wages, purchases only so much of a man's labour as he can perform in a day, or any other stipulated time' (Mill, 1826, Chapter I, section II).

Hence Knight was quick to offer a different rationale for the abolition of slavery.

'The abolition of slavery or property in human beings rests on the fact that slaves do not work as effectively as free men, and it turns out to be cheaper to pay men for their services and leave their private lives under their own control than it is to maintain them and force them to labor' (Knight, 1965, p. 320).

## **5. The Fundamental Myth and the *Laissez-Faire* Imputation Mechanism**

Morgan's treatment of the fundamental myth was somewhat confused with the way the assets and liabilities created in production are imputed in the absence of any legal trial (the *laissez-faire* mechanism of imputation).

Firstly, the fundamental myth is not part of the legal system (since capital is perfectly rentable); it is part of the standard ideology accepted by *both* the left and right concerning the 'rights of capital'. It is the idea that the right to the product (and discretionary management rights over production) are part and parcel of the 'ownership of the means of production'. The idea is easily defeated by pointing out that in our present system, capital goods are just as rentable as persons, and the legal party that ends up owning the product and managing the process of production is determined by who rents what or whom. In short, 'being the firm' is a contractual role determined by the pattern of contracts (e.g., capital hiring labour rather than the reverse – which of course depends in part on power relations). It is not a prior property

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<sup>2</sup> As Albert O. Hirschman put it, Marx's 'works exhibit a simple juxtaposition of scientific apparatus and moralistic invective, wholly *unversöhnt*' [unresolved] (Adelman, 2013, p. 570).

right – as seems to be indicated by the common phrase ‘ownership of the firm’ as if residual claimancy is already ‘owned’ prior to market contracts being made one way or the other.<sup>3</sup>

The fundamental myth is not a part of the legal system but it *is* part of neoclassical capital theory and corporate finance theory (see Ellerman, 1992) and is apparently accepted, or perhaps not even noticed, by the purported heterodox Cambridge critics of capital theory (Harcourt, 1972) who only criticise orthodox capital theory because of  $X =$  aggregate notions of capital, reswitching, and all that.

The second point is about how the property system works – how it imputes the liabilities for the used-up inputs and the ownership of the produced outputs in the normal operation of *any* private property market economy (such as a labour-managed market economy with the human rental contract abolished). Somehow in Morgan’s treatment of this mechanism, there was no mention of the input liabilities (the negative product) which together with the produced outputs (the positive product) comprise the ‘whole product’.

The algebraic symmetry in the concept of the whole product (what neoclassicals just call the ‘production vector’) seems to be a particularly difficult point for anyone to understand. One does not have to be a mathematician to know about negative numbers in addition to positive numbers. One does not have to be an accountant to know about expenses in addition to revenues. And one does not have to be a neoclassical economist to understand that inputs are used up in addition to outputs being produced in production. Why is it so difficult to think in an algebraically symmetric manner about production?

The *laissez-faire* imputation mechanism is *not* a system where someone grabs the produced outputs and the Law says, ‘Let it be’. It is the system where one party has already paid all the costs (i.e., appropriated the negative product) and then the Law says, ‘Let it be’ when that same party sells the produced outputs. Thus the Law or ‘Invisible Judge’ imputes the whole product to that one party who got into the contractual position (thanks to the human rental contract) of being the last owner of the input services used up in production (treating the productive activity of the people working in the firm as one of those used-up inputs) and thus was in the defensible position to claim and sell the produced outputs.

The market imputation mechanism has nothing to do with the fundamental myth. But there is something ‘fundamental’ associated with that market mechanism of imputation, namely the Fundamental Theorem (unmentioned by Morgan) which gives the conditions such that *laissez-faire* imputation would be in accordance with the basic juridical principle of imputing legal responsibility according to *de facto* responsibility, i.e., would be in accord with the modern treatment of the labour theory of property. Those conditions and the theorem are outlined in the paper (see Ellerman, 2014 for more details). The final part of the paper shows how the renting of persons inherently violates those conditions due to the *de facto* inalienability of responsible agency. Thus the ‘natural system of private property and free contracts’ is in fact based on the inherently invalid human rental contract (whose longer-term version is already abolished) which allows ‘an institutional robbery – a legally established violation of the principle on which property is supposed to rest’. This quote is from John Bates Clark (in the paper) when Clark confidently thought that marginal productivity theory would ‘seal the deal’ for the idealised competitive human rental system and show it was not an institutional robbery.

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<sup>3</sup> As a personal aside, I am embarrassed to note that I was in the thrall of the fundamental myth when I first published on this topic in the pink of youth (Ellerman, 1973) and it took a couple of years to work my way out of it. To understand the market mechanism of appropriation, one needs to first understand that product rights are not already part of the ‘ownership of the means of production’ – which is why the whole question of appropriation in production rarely comes up in the conventional literature. The whole question is supposedly already settled by the ‘ownership of the means of production’ or in the equivalent non-Marxist phrase, the ‘ownership of the firm’.

Morgan also argued that by focusing on the institutional robbery at the root of the human rental system, I was somehow neglecting the grotesque mal-distribution of wealth, that:

‘... is a source of power, which in turn is rooted in socio-economic relations and is manifested in influence. This, for example, is basic to Piketty and many others’ argument regarding the institutional problems of wealth and income inequality...’ (Morgan, 2016, p. 41).

In terms of the historical analogy, by focusing on the underlying master-slave relation, one is ‘neglecting’ the mal-distribution of wealth between masters and slaves (and the resulting power/socio-economic relations) which could be addressed by more progressive taxes and social redistributive programs. One should differentiate the root of the problem from the symptoms. Just as one can have financial leverage by renting other people’s money and getting its returns, so one can have human leverage by renting other people themselves and thereby appropriating the (positive and negative) fruits of their labour. The grotesque mal-distribution of wealth and income today results from (i.e., is the accumulated symptoms of) centuries of institutional robbery by thus ‘leveraging’ human beings, first in the system of owning other people, and more recently by the current system of renting other people. And in the aforementioned circular causation, that maldistribution of wealth and power will ensure that the human rental system survives to include the next generation.

Yes, the maldistribution of wealth and income is ‘basic to Piketty’ and to similar progressive and even left-leaning Nobel-prize-winning economists. But that is a focus on the accumulated symptoms or effects, not on the root cause, and their various redistributive palliatives do not reach to the root – which is the whole institution of the renting of human beings. In terms of the historical analogy, a redistribution of *antebellum* wealth in favour of the slaves (surely, a good thing), while keeping the institution of ownership of other persons intact, would not get to the root of the problem. Morgan is correct that my neo-abolitionist focus on the root cause may seem to some as being ‘incomplete’ without some fashionable hand-wringing about all the accumulated symptoms.

## 6. Personhood

On the basic issue about the inalienability of responsible agency, Morgan notes that this is:

‘... at root an argument concerning the nature of personhood, the nature of what it means to be human. It is an ontological claim. So one might also note that Ellerman’s case – in at least its normative dynamic – requires a clear ontological argument regarding the nature of personhood (and species-hood), and the possible consequences of personhood for socio-economic forms, including the case for economic democracy’ (Morgan, 2016, pp. 41-2).

Morgan is certainly correct as a matter of moral philosophy and I have written extensively about this elsewhere (1988, 1992). But the social scientist can take a more modest stand by not arguing the moral philosophical question of whether or not a certain principle is right or wrong, but by arguing the analytical/factual question of whether or not a given system violates a certain principle (regardless of what one thinks about the principle).



Consider the case of Milton Friedman who was a great advocate of 'positive economics' and who at the same time argued that the idealised competitive system involving human rentals satisfied 'the ethical proposition that an individual deserves what is produced by the resources he owns' (Friedman, 1976, p. 199). Friedman did not try to philosophically argue for the supposed principle, which he called the 'capitalist ethic' (Friedman, 2002, p. 164); he only argued that the competitive system in fact satisfied the principle. Or consider Frank Knight who argued that the competitive system satisfies:

'... justice by the principle of equality in relations of reciprocity, giving each the product contributed to the total by its own performance ("what a man soweth that shall he also reap")' (Knight, 1956, p. 292).

One can argue against their assertions, as I do in the paper, without indulging in a moral argument over the principle 'what a man soweth that shall he also reap'.

In fact, I think it is largely a waste of time to dive into moral philosophy and argue with the intellectual hirelings of the employment system over the moral principle of 'what a man soweth that shall he also reap' or the moral status of institutionally treating persons as things. Nor is that necessary. One only has to show that the system of renting persons violates that principle and treats persons as things since the employees (*qua* employees) in an employment firm owe zero percent of the negative fruits of their joint labour (the input-liabilities) and own zero percent of the positive fruits of their joint labour (the output-assets) – exactly the legal role of rented things.

The defenders of the faith in the 'science of economics' are perfectly free to disagree with the moral principles at stake by saying, 'Yes, employees have the institutional role of rented things, but that is OK' or 'Yes, employees appropriate zero percent of the (positive and negative) fruits of their labour, but that is OK'. However, I think the defenders of the faith will wisely choose to just avoid this whole set of arguments. When they want to prove their value to their social masters by doing intellectual battle with critics of the system, they will search for some member of the dwindling band of Marxian economists to serve as their foil (Ellerman, 2008, 2010c) in arguments about whether or not 'wages are too damn low' due to power relations in non-competitive markets, about the labour theory of value, or about abolishing the 'private ownership of the means of production'.

Furthermore, one of the dogs that didn't bark in Morgan's commentary was my whole discussion of marginal productivity theory (MPT) which was one of the main points of the paper since I have written about the LTP extensively elsewhere (Ellerman, 1992; 2014). In particular, there was no commentary on the stunning success of neoclassical theory to get liberal-progressive thinkers to implicitly accept the *metaphorical* application of the responsibility principle in MPT as correct in theory, since 'critics' such as Lester Thurow (1975), John Rawls (1971), and Steve Keen (Chapter 6, 2011) only attack such things as X = measurement difficulties in practice, X = non-competitiveness of labour markets, and X = the background mal-distribution of wealth – all of which were long ago acknowledged by sophisticated defenders of the system of human rentals such as Frank Knight.

This raises a more general point. Many heterodox economists, and progressive thinkers in general, take it as given that the social role of economic theory is to be a descriptive science, and then they castigate orthodox economics for being so unrealistic, e.g., the above mentioned 'criticisms' of marginal productivity theory. But to understand the social role of economic theory, one has to consult a thinker of the depth and forthrightness of Frank Knight who openly acknowledges that 'economic theory is not a descriptive ... science'. There you have it; the secret is out. As Knight explains:

'Economic theory is not a descriptive, or an explanatory, science of reality. Within wide limits, it can be said that historical changes do not affect economic theory at all. It deals with ideal concepts which are probably as universal for rational thought as those of ordinary geometry' (Knight 1969, p. 277).

The point of orthodox economics is:

1. to outline an idealised system, i.e., the free enterprise, free market, competitive private property system (including human rentals of course), and then
2. to frame the whole normative discussion in terms how to get the real-world economy to better approximate that idealised model.

Heterodox economists who think they developing a 'critique' of the system by showing how the 'ideal concepts' so poorly describe the actual economy are, in fact, working well within the orthodox paradigm. In fact, 'everyone' (including orthodox economists) knows that the ideal concepts are poor descriptors; that was never their purpose.

In order to critique the system, one needs a critique of the *ideal* model, not simply another banal recital of how the actual economy falls short of the ideal model. Marginal productivity theory plays a key role in showing how the idealised model would allegedly satisfy the demands of justice in distribution. The point of my paper was to use the labour theory of property (the property-theoretic version of the juridical principle of imputation) to show that the idealised model of the free enterprise, free market, competitive human rental system does not satisfy the principles of justice *even in theory*. Hence the paper did not discuss difficulties in actually measuring marginal productivity or imperfections in the labour market. It did not discuss the fact that almost all actual markets are not competitive or that the given prior distribution of property can hardly be assumed to be just, or all the other points that are easily acknowledged by sophisticated defenders of the human rental system such as Frank Knight.

## 7. Kirzner's Entrepreneurship Theory

Burczak's third point is that:

'There is an argument, made for instance by Israel Kirzner (1974), that the hiring party is the responsible agent of production and, thus, the rightful appropriator of the entire product (i.e., the output assets and input liabilities)' (Burczak, 2016).

The hiring party is, of course, the *legally* responsible party who, by bearing the legal liabilities involved in production, has the *legally* rightful claim on the outputs. That is a correct description of how the market system of appropriation works. The question, however, is about the *factual* responsibility.

Kirzner's theory is built on the image of the entrepreneur as arbitrageur. The entrepreneur in production is seizing an opportunity to arbitrage between input and output markets, which is seen as being more complicated than, but not differing in kind from, an arbitrageur in commodity markets. There is no questioning of the contracts involved (e.g., the

human rental contract) as if the contracts were no more problematic than buying and selling wheat or crude oil in commodity markets. There is no argument that *de facto* responsible agency has somehow been actually alienated by the employees; the whole question is not even raised.

Frank Knight was a more sophisticated defender of the human rental system in addition to anticipating the essentials of Kirzner's theory.

'Under the enterprise system, a special social class, the business men, direct economic activity; they are in the strict sense the producers, while the great mass of the population merely furnish them with productive services, placing their persons and their property at the disposal of this class; the entrepreneurs also guarantee to those who furnish productive services a fixed remuneration' (Knight, 1965 [1921], p. 271).

And Knight faces up to the point that the rented workers have the legal role of rented instruments by arguing that this is essentially the factual situation.

'It is characteristic of the enterprise organization that labor is directed by its employer, not its owner, in a way analogous to material equipment. Certainly there is in this respect no sharp difference between a free laborer and a horse, not to mention a slave, who would, of course, be property' (Knight 1965, p. 126).

Kirzner may approach this perspective when he, like much of the popular business press, treats the entrepreneur as some sort of *ubermensch* who has such powerful creative agency that everyone else involved in the enterprise is, in comparison, a drone-like piece of material equipment. I take that aspect of Knight's and Kirzner's apologia – that the other humans working in an enterprise are factually like employed material equipment – to be beneath criticism like the slavery apologists' view that the slave was factually a beast of burden like Knight's horse.

## **8. Marx and the Wage System**

I pointed out that Marx's exploitation theory, even if successful, only concluded that 'wages are too damn low' which is not a critique of the wage system *per se*. However, Burczak comments:

'Finally, Marx was pretty clear about seeking to abolish the wages system, rather than advocating higher wages in an employment system' (Burczak, 2016).

Yes, Marx was clear on seeking to abolish the wage system. The first point is that Marx was also clear on seeking to abolish 'private ownership of the means of production' and the result has been that every revolution made in Marx's name has resulted not in abolishing wage labour, but only in nationalising it. Secondly, I was not talking about Marx's views but his theories. Marx only brought a value theory (plus a lot of non-theoretical moral invective) to a property-theoretic fight – so it would not do the job, even if successful as a theory of value and exploitation.

A similar example is John Rawls (Ellerman, 2010a). Aside from spending a lifetime writing about justice without once considering the human rental contract as being inherently problematic, Rawls also shared the Harvard Philosophy Department with Robert Nozick who advocated that a 'free system' should allow a person to voluntarily sell himself into slavery (1974, p. 331). No one would doubt that Rawls' personal view was against allowing such a civilised slavery contract, but the remarkable thing is that Rawls' theory of inalienable rights (such as it was) does not rule it out. Rawls refers to Montesquieu's argument that one cannot alienate *all* one's rights as they are 'beyond all price'. But as noted above, Montesquieu goes on to approve alienating some basic rights in a mild form of voluntary slavery. And Rawls similarly goes to hold:

'This explanation of why the basic liberties are inalienable does not exclude the possibility that even in a well-ordered society some citizens may want to circumscribe or alienate one or more of their basic liberties' (Rawls, 1996, p. 366).

'Unless these possibilities affect the agreement of the parties in the original position (and I hold that they do not), they are irrelevant to the inalienability of the basic liberties' (Rawls, 1996, p. 367, fn. 82).

So while Rawls' personal views were no doubt against such a contract, his *theory*, like Montesquieu's, left plenty of room for Nozick.

Burczak's last point is that:

'Perhaps contemporary Marxists are a dwindling group, but a large subset of them supports cooperative production relationships, very much like David Ellerman (e.g., Jossa 2014, Wolff 2012)' (Burczak, 2016).

It should first be noted that Marx and Marxists have always supported cooperative production – as the Bolsheviks 'supported' the worker soviets – as a transitional institution to full socialism. In the whole sorry history of Marxian socialism in the 20th century, there was not a single Marxist revolution that established a market economy of worker cooperatives (although Yugoslav eventually tried out a muddled hybrid) or even a multi-party political democracy (not even Yugoslavia). Real-existing Marxist socialism was always a system of near-universal state employment as, for instance, in Cuba which only in the last few years has started to 'allow' non-state worker cooperatives.

In today's world, it seems that many heterodox thinkers have bonded with the word 'socialism' in the pink of youth, e.g., Bernie Sanders who self-sabotaged his U.S. presidential campaign by trying to validate his youthful bonding with the word by redefining Scandinavian social democracy as 'democratic socialism' (which in the U.S. is considered an oxymoron). But Marxian socialism has always had the *sine qua non* of 'government' or, excuse me, 'social' ownership of the means of production. Marxists such as Richard Wolff and Bruno Jossa interpret 'cooperative production' as meaning 'worker self-management' at least on the shopfloor coupled with 'social ownership of the means of production' (in some muddled remix of the Yugoslav socialist system). What could go wrong with that?

In terms of characterising different systems, Marxist socialists, like Jossa, take the 'ownership of the means of production' as the key differentiator, not the renting of persons (wage labour). If wage labour were the criterion, then Jossa and Cuomo see a *reduction ad absurdum* since:

'If this definition is accepted, the system with publicly-owned production means and centralized planning is a form of capitalism' (Jossa and Cuomo, 1997, p. 113).

Imagine that; Soviet or Chinese communism being seen as essentially a form of state capitalism! They continue:

'This classification contradicts a long tradition of thought; and it is also for this reason that it can barely be assumed to be the most acceptable one. The other possibility is to adhere to the classical distinction between firms with privately-owned production means and firms with publicly-owned production means. In this case one will have capitalism on the one hand and two or more forms of socialism on the other: and provided the Soviet socialist model is not viewed as an 'ideal type' ..., these forms of socialism are reduced to no more than three...: (i) the Lange-Taylor model, (ii) socialism with autonomous firms run by managers, and (iii) socialism with labour-managed firms' (Jossa and Cuomo, 1997, p. 113).

The last version (iii) is the Marxist socialist version of 'cooperative production'. In contrast, genuine worker cooperatives, like the Mondragon cooperatives, are *private* democratic organisations.

Marx's notion of the 'ownership of the means of production' (as including the right of management and ownership of the product) played the key role (not wage labour) in his thought as Jossa and Cuomo explain. And it is perhaps Marx's greatest blunder (as explained in the whole previous discussion of the fundamental myth). In Medieval times, the ownership of land was seen as including the ownership of the product of the land and the governance of the people living on and working the land. The landlord was the Lord of the land. Marx's blunder was to carry over that feudal notion of 'ownership' from land to capital, the 'ownership of the means of production.'

'It is not because he is a leader of industry that a man is a capitalist; on the contrary, he is a leader of industry because he is a capitalist. The leadership of industry is an attribute of capital, just as in feudal times the functions of general and judge were attributes of landed property' (Marx 1977, pp. 450-451).

But in the human rental system, the right to govern people in production is legally based on the employment contract, and the right to the (positive) product goes to the party who has already appropriated the negative product (i.e., paid the costs of production including the wages) so those rights are attached to the contractual role of being the hiring party and are not part and parcel of the 'ownership of the means of production' (which is why that view is a myth, the fundamental myth). Marx's view that the management and product rights are part of capital also accounts for the misnomer of 'capitalism' to denote the human rental system.<sup>4</sup>

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<sup>4</sup> I no longer use the word 'capitalism' to denote the human rental system for the second reason that a critic of 'capitalism' is automatically assumed to be a critic of private property. Quite the opposite, the critique of 'capitalism' on the basis of the labour theory of property is a critique in the name of a just private property system based on the most legitimate reason for property appropriation, namely people getting the fruits of their labour. To paraphrase Gandhi, 'I think private property *would* be a good idea' –

As one might expect, Frank Knight, was quite clear on ‘capitalism’ being a misnomer and that the employer-entrepreneur may not be the owner of the capital, i.e., may not have the ‘ownership of the means of production’.

‘Karl Marx, who in so many respects is more classical than the classical themselves, had abundant historical justification for calling, i.e., miscalling – the modern economic order “capitalism”. Ricardo and his followers certainly thought of the system as centering around the employment and control of labor by the capitalist. In theory, this is of course diametrically wrong. The entrepreneur employs and directs both labor and capital (the latter including land), and laborer and capitalist play the same passive role, over against the active one of the entrepreneur. It is true that entrepreneurship is not completely separable from the function of the capitalist, but neither is it completely separable from that of labor. The superficial observer is typically confused by the ambiguity of the concept of ownership’ (Knight, 1956, p. 68, fn. 40).

Thinkers who, in their mature thought, have not managed to fight their way out of the paper bag of the simplistic Marxist notion of the ‘ownership of the means of production’ (as including product and management rights) are hardly in a position to understand the restructuring of property and personal rights in a *private* worker cooperative (Ellerman, 1984). In a worker cooperative or democratic firm, the worker’s membership rights are personal rights (not property rights that, for instance, could be sold or bequeathed) based on their inalienable rights to the joint private ownership of the fruits of their labour and on their own inalienable rights of self-governance – not on product and ‘self-management’ rights delegated from the benevolent ‘social’ owners of the means of production.

## **9. The Corporation as a ‘Deeply Problematic’ Legal Entity**

The last major point raised by Morgan is about the corporation as a ‘deeply problematic’ (Morgan, 2016, p. 39) legal entity and the whole corporate governance debate. I did not directly address these issues in the paper but I am glad to briefly comment on them. I am afraid that much of the progressive commentary attacking the very idea of a corporation as a separate legal party (i.e., separate assets and liabilities from the individual members) is largely superficial and the policy recommendations that follow from the arguments would be quite counterproductive.

Here in the United States, these arguments are often focused on the *Citizens United* case which many critics think was based on the argument that corporations are legal ‘persons’ and thus should have the same constitutional rights as natural persons – even though the judge writing the dissenting opinion noted specifically that this was *not* the argument (Ellerman, 2010b). The policy recommendation drawn from this ‘criticism’ is that only *natural* persons should have the rights of free speech by way of making political campaign contributions. No policy would be better for the super-rich 1% than this silly idea wherein, to echo Anatole France’s sarcasm, the average person on the street and one of the Koch brothers would each have an equal right to as much public voice as they could individually afford. Any legal organisation which might amplify the public voice of ordinary

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as opposed to the property-is-theft system (Proudhon) based on renting human beings so as to appropriate the fruits of their labour.

citizens by joining them together in a labour union or a non-profit NGO would also *not* be a natural person and thus would also be forbidden, along with conventional corporations, from constitutionally protected associational speech in the form of campaign contributions.

Far from being 'deeply problematic', the basic idea of a corporation as a separate legal party from its members is an important social invention (e.g. to foster risk-taking innovation). It should not be attacked simply because it is the most common legal shell for institutional robbery of the whole system of renting persons (which is just as 'problematic' when the employers are natural persons or partnerships). The corporate form should be preserved for the democratic, labour-managed firms of the future after the abolition of the human rental contract, and it is the form for the fledgling worker cooperative corporations of today, e.g., those incorporated under cooperative *corporation* law such as the law I co-drafted for Massachusetts back in the early 80s (Ellerman and Pitegoff, 1982).

The long quote by John Kay (Morgan 2016, p. 40) from the *Financial Times* is also typical of the superficial analysis and criticism of the corporate form. Kay makes the point that shareholders are not really 'owners' since they can't just walk into 'their' corporation and grab something as their personal property and use it to pay off a personal debt. But that is a banality – true in a worker cooperative or in any other organisation (e.g., any club, association, or NGO) that is a separate legal party from the individual member – so it has little to do with corporate governance debate.

Kay also makes the point that the shareholders' right to appoint the directors who select the managers is only 'theoretical'. This is the common lament about the separation of ownership and control in the large, publicly-traded corporations so that the 'shareholders' democracy' exists only in theory, not in practice. But the nontrivial point that one will not find in the *FT* is that 'shareholders' democracy' would not be democratic even if it did exist in practice.

The simple reason is that democracy is the collective form of *self*-government, and the people being managed by the directors and their managers are the people working in the corporation, not the far-flung shareholders. The so-called 'shareholders' democracy' if it existed in practice, not just in theory, would be like the people of Russia going through a whole set of vigorous discussions, deliberations, and debates and then voting to elect the government of Poland. But, alas, as liberal critics would lament, such a 'democracy' would only be 'theoretical' in Kay's words if the voting rights of the Russian people to elect the government of Poland were usurped by the unaccountable nomenklatura of the Communist Party. Unfortunately, the real critique of the corporate governance debate about 'shareholders' democracy' will not be found in the writings of liberal critics like John Kay or printed in the pages of the *FT*.

I have written at length over the decades about how differently a democratic corporation would be structured (Ellerman, 1984; 1990). But contrary to the apparent policy recommendation of the book (Tombs and Whyte, 2015) referenced by Morgan and subtitled 'Why corporations must be abolished' – I would never suggest that the corporate form should be abolished so that the worker-members would have unlimited personal liability for their cooperative's economic liabilities. Again, this policy recommendation would only be favourable to the rich since only they could then afford to undertake the risks of enterprise on any scale.

Apparently the real concern of Tombs and Whyte, and much of the other 'anti-corporate' literature cited by Morgan, is that crimes of commission and negligence committed by corporate managers might go unpunished – which is a very real fear given the extent to which the present-day legal and legislative system is suborned to the corporate employers – which is reminiscent of the way the judges, state legislatures, and politicians of the ante-

bellum South were suborned to the economic masters of that time. The underlying normative principle of that critique is that corporate managers, like other people, should be held legally responsible for their *de facto* responsible actions – a legal principle that in its application to questions of property appropriation is called ‘the labour theory of property’, the topic of my paper.

## 10. Concluding Remarks

I have tried to address the points raised by Morgan and Burczak, taking some occasions to expand upon the arguments and touch on broader issues. I took Frank H. Knight as my adversary-helper since he was surely one of the most sophisticated and forthright of the apologists for the human rental system and its economic theory.

One of Knight’s points was particularly relevant to the discussion, namely that economic theory aims to build an idealised model and then to frame the normative discussion in terms of that ideal. So much of the heterodox criticism focuses on the fact that the actual economy falls far short of that competitive free market ideal – instead of being focused on the ideal itself. The case in point is the crucial role of the marginal productivity theory of distribution that is so key to the claim that the ideal model obeys the principle of justice (e.g., ‘what a man soweth that shall he also reap’) – even if the reality falls short of that ideal.

The point of the paper was to change the framing from that sort of a price-theoretic argument (marginal productivity pricing of inputs) to the property-theoretic framing of: who is to appropriate the liabilities and assets created in a productive enterprise? Then applying the normal juridical principle of imputing legal responsibility in accordance with factual responsibility coupled with the non-metaphorical fact that only humans and not things can be morally or legally responsible – all leads to the rather different conclusion that all the people who work in a productive enterprise constitute the legal party who should appropriate the positive and negative fruits of their joint labour.

Some practical people, even conservatives, who have looked at the matter objectively without all the filters, blinders, and misconceptions of economic theory have come to the same conclusions.

‘Here is the most urgent challenge to political invention ever offered to the jurist and the statesman. The human association which in fact produces and distributes wealth, the association of workmen, managers, technicians and directors, is not an association recognised by the law. The association which the law does recognise – the association of shareholders, creditors and directors – is incapable of production and is not expected by the law to perform these functions. We have to give law to the real association, and to withdraw meaningless privilege from the imaginary one’ (Percy, 1944, p. 38).

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