

ENDOGENOUS MORALITY*

by

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Abstract: Philosophers propose a moral foundation for property rights, but a property rights foundation for morality is outlined here. It is contended that the desire to expand wealth in the face of scarcity underlies the evolution of rules, including moral norms. People "rationalize" their behavior as moral by adopting beliefs which reduce the costs (psychic or tangible) of achieving their objectives. Individuals expand their wealth through production or takings, and moral beliefs that evolve in institutions that support each process are explored. Situational morality arises for a single individual due to simultaneous involvement in numerous institutional arrangements.

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Hagar the Horrible says "Always remember one thing, Lucky Eddie... VIKINGS ARE THE CHOSEN PEOPLE!" Lucky Eddie asks "Who chose us?" and Hagar responds, "WE DID!" Hagar cartoon strip by Chris Browne, Tallahassee Democrat, January 13, 1999, page 5D.

"This reminds me, to some extent, of the hearing when Clarence Thomas and Anita Hill were both testifying under oath. Now, in some rational way, they could not have both been telling the truth, since they had directly different accounts of a shared set of facts.... [W]hen I heard both of them testify, what I believed after it was over, I believe that they both thought they were telling the truth." President of the United States, William J. Clinton, Transcript of Testimony to the Grand Jury, 1998 (CBS Worldwide Inc., <http://cbsnews.excite.com/media/excite-index.html>).

"[People] may ... picture themselves as meritorious, feeling themselves guilty of no such offenses as they see others burdened with; nor do they ever inquire whether ... they would not have practiced similar vices, had not ... circumstances of time and place ... , kept them out of the way of these vices. This dishonesty, by which we humbug ourselves and which thwarts the establishment of true moral disposition in us, extends itself outwardly also to the falsehood and deception of others." Philosopher Immanuel Kant, Religion Within the Limits of Reason Alone, T. M. Green and H. H. Hudson (trs.) (New York: Harper, 1960), p. 16.

"As someone who has spent the better part of his life behind bars, I've never run into a guilty criminal. To hear them tell it, everyone but themselves is to blame for making them commit the crime: their mother, the victim, society itself." Bank robber Gary Bornman, serving a seven year sentence in the Marianna Florida Federal Correctional Institute, letter to the editor, Tallahassee Democrat (February 24, 1995), p. 10A.

"[T]he commonest weakness of our [human] race is our ability to rationalize our most selfish purposes." Science fiction author Robert Heinlein, The Star Beast (New York: Del Ray, 1954), p. 219.

Kant's "categorical imperative" and the Golden Rule both appear to require something like unconditional cooperation (Vanberg and Congleton 1992: 420). Thus, from a moral standpoint individuals should fulfill promises and respect other peoples' rights. They also should be benevolent, generous, and in general, feel "sympathy, kindness, consideration for others" (Hazlitt 1964: 75). Even superficial observations quickly reveals that to the degree that many (all?) individuals adopt such behavior, however, they do so only under certain circumstances in their interactions with selected other individuals. And furthermore, as suggested by some of the preceding quotes, people often feel quite "moral" (ethical, honest, honorable, meritorious, righteous) even when they violate the Golden Rule and/or behave in other ways that moral philosophers would condemn as immoral. Why? The answer proposed below is that what most people (although not most moral philosophers) perceive to be moral behavior depends at least partly on the institutional setting of the relevant behavioral interaction. That is, individuals "rationalize" their own "selfish" behavior, given the "circumstances of time and place," so in their own minds they are "telling the truth", not subject to "blame", "meritorious", and perhaps even morally superior ("the chosen people"). This answer is

not new, of course. Indeed, the quotations listed above suggest that people from many walks of life recognize that perceptions of what is moral are endogenous, at least to a substantial degree. In contrast, however, Cooter (1998: 597) suggests that "Modern microeconomics trivializes moral commitment by treating it as an exogenous taste."

Recognition that what people perceive to be moral is endogenous does not mean that economists' efforts to model decision making should be jettisoned, despite the claims of so many communitarians (as well as anthropologists, sociologists, etc.) [e.g., Etzioni (1988)]. In fact, the economic model should be broadened to consider endogenous morality. If people "rationalize" their behavior as moral by adopting beliefs which reduce the costs (psychic as well as tangible) of achieving their selfish objectives, then the beliefs that evolve in different institutional environments should be predictable using an economic model. Therefore, the primary purpose of the following presentation is to provide the foundations of a positive analysis of the endogeneity of beliefs about behavior that people consider to be moral based on the fundamental assumptions of microeconomics - (1) scarcity, (2) methodological individualism, and (3) rationality - while relying on the fundamental principles of comparative advantage and opportunity costs. These assumptions are brought to bear in the context of an uncertain world with transactions costs impeding coordination and motivation, and moral beliefs evolve, at least in part, to reduce such costs. However, some individuals develop comparative advantages in violence, and therefore in predation, so cooperative norms may coordinate joint production of plunder or extortion too. When extortion is institutionalized, a set of rules regarding wealth transfers is developed by one group and imposed on another, but such organized appropriation will also affect perceptions of morality among individuals who benefit from transfers and those who lose.

After Section I's brief overview of relevant economics literature, Section II contends that the desire to expand wealth in the face of scarcity underlies the evolution of rules, including moral norms. Moral beliefs that evolve in a community with institutions that support production and exchange to expand wealth are explored in Section III. It is in this setting that beliefs consistent with the Golden Rule and Kant's categorical imperative are most likely to be adopted. Indeed, while some philosophers suggest that there is a moral foundation for private property rights, the contention here is that there is a property rights foundation for morality. Section IV focuses on moral beliefs that emerge under institutions that support coercive wealth transfer incentives. The moral beliefs implied by the preceding quotes tend to arise in this setting. Section V concludes by explaining different moral behaviors for a single individual due to simultaneous involvement in numerous institutionalized groups, some of which encourage voluntary interaction (generally within the

group), some of which facilitate involuntary wealth transfers from others (generally outside the group), and some of which support both means of wealth seeking.

II. The Economics Literature on Moral Behavior

While most of microeconomics assumes that moral norms simply do not matter, there is a growing recognition among economists that this is not the case (Hausman and McPherson 1993). Goldfarb and Griffith (1991) explain that the expanding economics literature dealing with morality includes models that treat moral values as part of preference functions, and models that treat moral norms as constraints [Dowell, et al. (1998) model morality as affecting both preferences and constraints]. If morality is endogenous, however, then the assumption that preferences are given and stable must be questioned (Cooter 1998: 597-598). Similarly, the assumption that morals are constraints is inadequate if different moral beliefs arise in different institution environments.

Goldfarb and Griffith (1991) also explain that the recent economics literature dealing with morality includes models that treat norms as rational strategic decision rules in games. In certain types of games (e.g., repeated games, reputation games), rational strategies can involve behavior that is often described as ethical or moral: e.g., cooperating, living up to promises, being trustworthy.¹ The endogeneity of morality is becoming increasingly explicit in this and related literatures.² However, the types of cooperative behavior implied by such modeling does not explain the beliefs suggested by the quotes listed above. Non-cooperative behavior can also arise in games [e.g., one period or finite repeated prisoner's dilemma games], of course, and the "moral hazard" problem has been recognized in the literature on insurance, principal-agent, and other asymmetric-information situations [e.g., see Hart and Holmstrom (1987)]. The property rights literature also concludes that different types of behavior arise under different institutional arrangements. It is widely recognized, for instance, that secure private property rights encourage voluntary cooperation such as division of labor and exchange. Private property rights also encourage long time horizons which create incentives to conserve, maintain assets, invest and innovate [e.g., see Libecap (1989) or Umbeck (1981a)]. Insecure private property rights or common pools, on the other hand, create conflict and encourage short time horizons [e.g., see Libecap (1989) or Benson (1994a)]. But efforts to insure that others will respect private property also create incentives to provide assistance to those who find themselves in distress and therefore feel compelled to violate property rights [e.g., see Johnsen (1986)]. Finally, the literature exploring the conflicting incentives to cooperate or appropriate [e.g., Skaperdas (1992); Rider (1993); Anderson and McChesney (1994); Hirshleifer (1991); Benson (1994b, 1999)] also implicitly, and at times explicitly, suggests that moral behavior at least is

endogenous. In fact, much of what is suggested below can be found, at least implicitly, somewhere in these economics literatures, although the argument is packaged in a fashion which hopefully will yield some additional useful insights.

Microeconomics tells us that, at the margin, relative prices influence consumption choices. This may be true with moral decisions as well, given differential payoffs arising from and/or costs accruing to moral behavior in different institutional environments. If this is the case, then the question an individual faces in the context of a particular interaction is not simply, "What is the moral thing to do?" At a minimum, it also includes the follow-up: "Can I afford to behave morally in this situation?" The Golden Rule may be recognized, for instance, but rationally ignored if the expected price of morality is too high. In other words, moral behavior may be endogenous while moral beliefs themselves are exogenous. But Frank (1988) argues that it is difficult (i.e., costly) for humans to pretend beliefs that are not actually adopted, so if acting as if such beliefs are real is desirable then it is rational to adopt them. In this light, the argument made here is that norms are rationally internalized as part of the belief system that individuals in a particular institutional environment have found to be beneficial, in order to reduce the psychological costs of taking actions that otherwise would violate their conscience. This is not the only reason to expect people to rationalize their behavior by adopting beliefs that support it, however. Adopting beliefs can also reduce decision-making costs (Holcombe 1992). After all, rational individuals are not able to use conscious reason to evaluate every option in the array of available alternatives, because there are significant limits on abilities to reason and absorb knowledge (O'Driscoll and Rizzo 1985: 119-122). This means that rational individuals often find it beneficial to voluntarily develop and conform to rules (including norms reflecting beliefs about what is moral) to guide their actions.

II. Scarcity, Wealth Seeking, Property Rights, and the Evolution of Rules

Norms. "Rules" are behavioral patterns that other individuals expect a person to adopt and follow in the context of various interdependent activities and actions. The rules one individual is expected to follow influence the choices made by other individuals: like prices, rules coordinate and motivate interdependent behavior. While the most obvious rules to many people may be "positive laws" created by states, there are many other types of rules that guide behavior (e.g., habits, conventions, traditions, customs, norms). This is relevant because even though beliefs regarding what is moral may be codified as "law," they need not be. In fact, such beliefs tend to arise, particularly initially, as "norms" which do not require explicit codification or backing by coercive threats to induce recognition. Norms are widely "shared values" (Voight and Kiwit 1998)

adopted by individuals in their interactions with an identifiable group of other individuals. As such interactions evolve and change, norms also spontaneously evolve. Indeed, as Nee (1998: 87) suggests, "Norms are implicit or explicit rules or expected behavior that embody the interests and preferences of members of a close-knit group or community."

Rules are generally not necessary if there are no conflicts to avoid or resolve, and as Hume (1751) emphasizes, the primary source of conflict between individuals is scarcity. Thus, the incentives created by scarcity underlie the evolution of rules and institutions (Benson 1994b, 1999). Rules to coordinate competition over the allocation of scarce resources and the wealth produced by them (e.g., to create incentives to compete through markets or through political institutions rather than through violence) establish the obligations that underlie the property rights to those resource and their products, as well as the procedures through which such property rights can be created, attenuated, and transferred. Wealth can expand through cooperative interaction, including team production (e.g., of goods, protection, mutual insurance), as well as the division of labor and voluntary exchange (of goods, but also of support, friendship, loyalty, etc.). Such voluntary cooperation requires trust, of course, so as explained below, rules that encourage ethical behavior tend to evolve in order to encourage participation in such positive-sum games. A second method of wealth enhancement for an individual involves taking wealth produced by others through the use of force and/or guile. Rules to facilitate extortion of involuntary transfers can also be institutionalized. Indeed, some rules are not shared values, but instead, they discriminate in favor of targeted individuals and are imposed on others by using coercive threats. That is, they are intended to transfer wealth. Their design and enforcement typically involves cooperative efforts by those with power, of course, and these cooperative processes are often governed by group norms.³ Importantly, such rules are rarely able to completely dictate the targeted behavior because knowledge is incomplete for the rule makers and policing is imperfect (Hayek 1973). Nonetheless, such designed rules do influence behavior. Deliberate efforts to impose rules create incentives to find and exploit uncontrolled margins in order to avoid the full consequences of those rules [e.g., see Cheung (1974)], and in this context, the search for ways to avoid the rules also can significantly alter the path of the spontaneous evolution of norms (Benson 1996a; Nee 1998). Therefore, a positive analysis of the evolution of beliefs regarding what is moral must account for the influence of the rules and institutions which facilitate cooperation and wealth expansion as well as those that are part of a wealth transfer process.

State of Nature. In order to analyze the process of moral evolution and consider some of its consequences, let us begin with the thought experiment so common in political philosophy (Hobbes 1651,

Locke 1690, Rawls 1971) and constitutional economics (Buchanan 1975). Imagine the Hobbesian "state of nature" wherein no cooperative interaction occurs (Hobbes 1651). Further assume, as in Benson (1994b), that while there is considerable uncertainty, and therefore high transactions costs, decisions are not made behind the Rawlsian "veil of ignorance."⁴ Thus, this analysis focuses on the rules and institutions that emerge assuming that rational individuals recognize their alternatives and anticipate potential but uncertain outcomes.

Competition over the use of scarce property can take different forms depending on the rules that exist, but in the absence of rules, unilateral efforts to capture exclusive benefits of an asset (turn a property claim into actual ownership) require that an individual back a claim with a sufficiently strong threat of violence to induce others to abandon their conflicting claims.⁵ Since several individuals are likely to have similar incentives with regard to any particular scarce resource, competition through violence could consume vast amounts of resources as each invests in an effort to exclude others. The competition for scarce resources is multi-sided, however, and any group of individuals may reduce the costs of conflict by voluntarily recognizing some subset of each others' claims (Vanberg and Buchanan 1990: 18). In fact, anthropological evidence rejects Hobbes' (1651) "war of all-against-all" at the individual level, as cooperative orders characterize relationships within small close-knit groups (Ellickson 1993; Ridley 1996; Rubin 1998).⁶ While cooperation dominates within primitive groups, inter-group conflict also appears to be a dominant characteristic of human history (Ridley 1996: 152-169, 189-193; Rubin 1998). Therefore, even though the norms of a spontaneously evolving cooperative order are considered before turning to the beliefs that arise under institutionalized extortion, it must be emphasized that these two developments often are simultaneous, and each can influence the evolution of the other.

III. Cooperation, Property Rights, and the Evolution of Morality

Moral behavior as a rational strategy. It is widely recognized that game theory and experimentation demonstrates that cooperation can arise through repeated interactions which create both a willingness to cooperate and a potential to punish non-cooperative behavior through strategies like tit-for-tat [and others discussed by Ridley (1996: 53-84)].⁷ A threatened sanction such as tit-for-tat is relevant because of the recognition of positive long-term benefits of remaining on good terms with the other party. Such reciprocity has implications for moral behavior because it means that an individual can face an immediate choice of bearing costs (e.g., by living up to a promise or recognizing another person's property rights) without an immediate gain, in expectation of future reciprocal behavior by someone else. As Taylor (1982: 28) suggests,

Each individual act in a system of reciprocity is usually characterized by a combination of what one

might call short-term altruism and long-term self-interest: I help you out now in the (possibly vague, uncertain and uncalculating) expectation that you will help me out in the future. Reciprocity is made up of a series of acts each of which is short-run altruism (benefiting others at a cost to the altruist) but which together typically make every participant better off.

Because the long-term reciprocal response is uncertain, a repeated-game situation does not guarantee unconditional cooperation in the form of "short-term altruism." The dominant strategy still depends on expected payoffs, frequency of interaction, time horizons, and other considerations (Ridley 1996: 74-75). Additional incentives for cooperation and for short-term altruistic behavior arise, however.

Vanberg and Congleton (1992: 420) explain that most forms of interaction are not actually characterized by the typical game-theoretic models because they assume that the individuals must play. In reality, however, people often have an "exit" option (Vanberg and Congleton 1992), and the exit threat can be more powerful than strategies like tit-for-tat under some circumstances. Specifically, Vanberg and Congleton (1992: 420) explain that "In practice, the net benefits of exit depend on the availability of alternatives (or more specifically, on the expected payoffs from those alternatives), whether such alternatives exist in the form of potential interactions with other players or in solitary activity." Thus, the exit threat becomes credible when each individual is involved in several different games with different players, in part because the same benefits of cooperation may be available from alternative (competitive) sources. And of course, even in a very primitive setting (i.e., not far from a state of nature), individuals are generally involved in at least one "community" as described by Taylor (1982: 26-30), wherein "the relations between members are direct and ... many-sided" [also see Bailey (1992), Ellickson (1993) and Rubin (1998)].

Vanberg and Congleton (1992: 421) suggest that one strategy that can be adopted, given a credible exit option, is unconditional cooperation until or unless noncooperative behavior is confronted, and some form of explicit punishment of the non-cooperative player as exit occurs. They label this strategy "retributive morality," and the "blood-feuds" of primitive and medieval societies provide examples. However, the fact is that retributive morality or the blood feud played a much less significant role in primitive and medieval societies than is popularly perceived (Benson 1991, 1994a). After all, such violence is risky, and there is an even better strategy. Given the availability of competitive alternatives, all members of the community have a refuse-to-play option, and therefore they may cut off all relationships with someone that they know has been untrustworthy in dealings with anyone else in the group. Thus, to the extent that information, or "truthful negative gossip" (Ellickson 1991: 180-182), can travel from one game to another, the negative consequences

on reputation can limit the non-cooperative player's ability to enter into other games. This means that there is a low cost option to retributive morality: unconditional cooperation whenever an individual chooses to enter into some form of interaction, along with the spread of information about any noncooperative behavior. Vanberg and Congleton (1992) refer to this response as "prudent morality," and given that reputation information spreads quickly within a group, the consequences of retributive and prudent morality become quite similar.⁸ If everyone spontaneously responds to information, the noncooperative individual is excluded from all interaction with any member of the community. Such spontaneous social ostracism can be a very significant punishment.

Ridley (1996: 132) notes that "Moral sentiments ... are problem-solving devices [that evolve] ... to make highly social creatures effective at using social relations [by] ... settling the conflict between short-term expediency and long-term prudence in favor of the latter." Many widely shared moral sentiments are simply commonly adopted behavioral strategies that apply for all interactions. Others are expected to be followed by all members of a group because obeying these norms produce positive externalities within the group (Vanberg and Buchanan 1990: 115). One example, the ostracism sanction, is suggested above. Investments in communication mechanisms can substitute for investments in the tools of personal violence, and since communication is cheap, resources will be left over to devote to wealth production. Norms like "inform your neighbors about individuals who violate trust rules" evolve and as individuals begin avoiding interactions with noncooperative players such behavior comes to be expected, so norms like "do not cooperate with individuals who behave in a non-cooperative fashion with someone else" arise. As members of the community conform with such norms, expectations of automatic expulsion for a breach of a community norm develops. Thus, the production of information and automatic boycott create benefits for everyone in the group by deterring non-cooperative behavior, even though they arise out of individual self interest. Ostracism has always been a primary obligation in primitive societies (Benson 1991) and in other cooperative groups [e.g., commercial societies (Benson 1989, 1992, 1995)].

Property Rights and Morality. Since the primary source of conflict is scarcity (Hume 1751), group-wide norms will focus on property allocation issues. No one really knows how cooperation norms and property rights actually emerged for the first time, of course, since both predate recorded history (Rubin 1998). A number of possible theoretical scenarios can be imagined, but let us focus on one that has an empirical basis,⁹ in order to illustrate some of the types of moral behavior that can arise as property rights are established within an evolving community. Assume that initially, productive resources are abundant relative

to potential claimants. Also assume that individuals do not have a comparative advantage in violence (a reasonable assumption in most primitive settings before technological advances in violence have occurred). Therefore, individuals are likely to prefer to avoid conflict by claiming resources that are not yet claimed, as long as unclaimed productive parcels exist (note that they do not have to be equally productive since the expected benefits of a less productive but undisputed asset may be greater than the expected benefits of more productive but disputed property, given the probability of losing in a violent confrontation). Thus, each party tacitly recognizes previously existing claims. This suggests that neighbors are not necessarily hostile towards one another from the outset, so various repeated-game social and economic relationships may also develop relatively easily. A multilateral web of such relationships may evolve and a "community" may form before scarcity of productive resources becomes a problem and conflicting claims arise. Indeed, it is likely that people will be members of a community before many claims are made (e.g., with discovery of technologies for agriculture, the individuals in an already-cooperative nomadic hunter-gatherer community may claim adjoining parcels of land in the same area and explicitly recognize each other's claims). As more people make claims in the area, however, resources ultimately become scarce and new entrants may attempt to institute conflicting claims (i.e., take property already claimed). Existing claimants now have a strong common interest in maintaining first-possession claims, and some experience with at least tacit, and probably explicit, recognition of those claims. At a minimum, they have already tacitly agreed not to attack one another, and by building upon that cooperative relationship they may join together in a protection association in order to exclude new entrants from taking any of their possessions. We can only speculate about prehistoric events of this kind, but as Ellickson (1993: 1366) notes [also see Bailey (1992)],

There is abundant evidence that a ... group need not make a conscious decision to establish private property rights in land [and other resources]. People who repeatedly interact can generate institutions through communication, monitoring, and sanctioning.... Contrary to Hobbes and Locke, a property system can get going without an initial conclave.

After all, as Hayek (1973: 107) explains, "The understanding that 'good fences make good neighbors', that is, that man can use their own knowledge in the pursuit of their own ends without colliding with each other only if clear boundaries can be drawn between their respective domains of free action, is the basis on which all known civilization has grown. Property, in the wide sense in which it is used to include not only material things ... is the only solution men have yet discovered to the problem of reconciling individual freedom with the absence of conflict." Indeed, the primary goal of such agreements may be to obtain non-material wealth

in the form of "peace" or security, but of course, material wealth is also likely to be enhanced for everyone involved in such trust relationships. If property rights are made relatively more secure and relatively more private, time horizons lengthen and incentives to use the property for production increase. Private property means that the individual's use of the owned asset is unhindered as the owner pursues his interests, as long as that pursuit does not impinge on someone else's rights. That is, an individual's freedom to act is coupled with a norm establishing an obligation or a responsibility to respect other people's right to do the same thing. And in order to make all community members' claims more secure, additional norms like "watch out for your neighbors and their property" and "inform everyone when a rights violation occurs" arise. After all, transaction costs of possessing property include the devotion of resources to theft prevention, and high transactions costs for an individual imply that protection will not be completely effective. The empirical fact is that one joint product of cooperative clusters often involves the policing functions of watching to prevent theft, and cooperation in pursuit and prosecution when a theft occurs (Benson 1991, 1994a). Other norms also arise in order to make property rights more secure.

Sharing Norms, Mutual Insurance and Benevolence. The earliest forms of cooperation probably did not involve individualized private property, of course. Group ownership of things like hunting territories (Bailey 1992) and of the proceeds from a successful hunt (Ridley 1996: 105-117) were common. Consider Ridley's (1996: 108) interesting conjectures about the development of the dart thrower and the incentives to cooperate in mammoth hunting. Since an individual was unlikely to kill a mammoth without help or defend it once killed, there were incentives to form "partnerships" for joint production of hunting and exclusion. Several hunters could surround the animal, preventing escape and inflicting multiple wounds. Furthermore, once an animal was killed, it could be "owned" by the killer(s) only if outsiders (and other animals) could be excluded. The dart thrower made killing a large animal much less dangerous, thereby lowering the cost of cooperation in hunting (prior to this, promises to cooperate were less credible because an individual might flee rather than put himself at extreme risk for the uncertain shared benefit of the cooperative effort). This reduction in incentives to shirk lead to more success in production and increased the ability to withdraw the asset from the commons. The dart thrower also lowered the cost of exclusion. The result was not individualized private property even when a particular hunter clearly inflicted the fatal wound, since the carcass was shared with everyone in the community. It was private property in the same sense that partners jointly own a business and share profits, however, and "sharing norms" or "equality norms" were very common in primitive communities. These norms were quite rational, enhancing the incentives to cooperate in

joint production and serving as a form of insurance (Posner 1980; Rubin 1998). While one individual or hunting party might not be successful another was likely to be, so sharing was a mutual insurance arrangement that reduced everyone's risk of going hungry. Essentially, sharing norms are examples of short-term altruism motivated by repeated-dealing reciprocities. Such "insurance" also gives rise to moral hazard, of course, and there were incentives to free ride, as Ridley (1996) explains, so cooperation might not materialize without rules that undermine such incentives. Such rules also arose. The strong norms regarding sharing were reinforced by taboos against free riding and other activities (e.g., hoarding) that might create incentives for hunters in the group to shirk. Thus, an understanding of such cooperation requires more than a recognition of potential benefits. The development of such norms, and of the institutions that instill incentives to recognize them, must also be considered.

As the benefits of individualizing property rights arose, such rights also were recognized. Hunters tended to own hunting tools, for example, and with domestication of animals for hunting (dogs, horses), individual private property rights were recognized for them as well (Benson 1991). With advances in agricultural technology, individualized private property rights to land also evolved (Ellickson 1993; Bailey 1992). Future events can lead to predictable changes in the opportunity cost of cooperation that can reduce incentives to respect such private property, however. This means that members of a cooperative group have incentives to attempt to insure against the consequences of such changes. One way to encourage people to continue to recognize the cooperatively-produced property rights system even when circumstances change is to develop mutual insurance arrangements that provide aid to individuals who find themselves to be at significant risk as a consequence of mistakes, unanticipated natural disasters, or general bad luck. That is, apparent altruistic behavior in the form of voluntary wealth transfers can be made by rational self-interested individuals in order to induce others who find themselves in distress to continue to behave in predictable ways over the long term. Johnsen's (1986) analysis of the potlatch system of the Southern Kwakiutl Indians provides an insightful example. Johnsen (1986: 42) explains that "In order to provide the incentives of would-be encroachers to recognize exclusive property rights, and thus to prevent violence, those Kwakiutl kinship groups whose fishing seasons were relatively successful transferred wealth through the potlatch system to those groups whose seasons were not successful.... Although potlatching thereby served as a form of insurance, the relevant constraint in its adoption and survival was the cost of enforcing exclusive property rights rather than simple risk aversion." If the flow of payments is always in the same direction this could be analogous to a tax induced by the threat of violence, of course, but such transfers can arise due to expected

reciprocities. Members of one Kwakiutl kinship group may have a poor harvest of salmon in one year, and therefore receive a transfer, but the next year members of the other group could have the poor harvest so the transfer goes in the opposite direction. Thus, voluntary mutual insurance may be a more appropriate description.¹⁰ Not surprisingly, "gift exchanges" and "potlatching" have been common practices in societies all over the world, and they naturally evolve from the food-sharing norms that characterize hunter-gatherer communities (Ridley 1996: 114-124).

Actually, individuals need not anticipate reciprocal treatment in the future to voluntarily establish a transfer arrangement. As a cooperative group develops and property rights are increasingly privatized, for instance, everyone may recognize that some individuals are likely to gain considerable wealth while others may not enjoy the same kinds of gains. Thus, a class of relatively poor people can be expected to develop, and their opportunity cost of living up to promises to respect others' property rights will be low. Indeed, without help, they could be forced into thievery to survive. Recognition of this possibility implies that the transactions cost of property rights protection can be expected to rise in the future. An arrangement that pays the destitute before they violate others' rights may therefore be a low cost alternative to reacting after a violation through retributive or prudent morality. Solvason (1991: 72) discusses such an arrangement in medieval Iceland, for instance, which provided for those who suffered due to uncontrollable events. The members of neighborhood groups helped rebuild and restore property destroyed by fire, orphans or individuals who were destitute were taken in by others who were able to provide for them, those without property but able to work were given work by those wealthy enough to employ others' labor, and revenues were even collected and pooled to provide for the poor directly. This kind of arrangement might be based on bilateral reciprocities as in potlatching, but as a group evolves and expands they may become group-wide norms as the broader community takes on several functions that traditionally had been performed by more narrowly focused groups [e.g., by families under kinship-based norms, neighboring clans, etc. (Solvason 1991: 34-35)]. Thus, while free-rider incentives often are countered with ostracism threats, a private property rights system creates long time horizons and incentives to adopt moral behavior that emphasizes benevolence. Indeed, Hazlitt (1964: 354) suggests that "The conduct we call moral is the conduct we consider likely to lead to the most satisfactory situation *in the long run*." Such insurance arrangements mean that even those who may find themselves in desperate situations know that recovery is possible, so they have relatively strong incentives to adopt longer time horizons, respect property rights and behave cooperatively within the community that supports them in times of distress.

Generosity on the part of the wealthy, which reduces threats to their property, is not unique to primitive societies. Commercial societies have, throughout history, generated considerable wealth, for instance, relative to other less commercial societies (Wesson 1978), and as noted above and explained below, close knit commercial communities have much in common with the primitive communities discussed here. Indeed, "For all the protestations of Karl Marx and Max Weber, the simple idea of gains from trade lies at the heart of both the modern and the ancient economy" and therefore, "the origin of the market, with all its capacity to exchange goods of different kinds, exploit the division of labour and provide a hedge against dependence on one good, may lie in the reciprocal food-sharing arrangements of a hunter-gatherer band" (Ridley 1996: 199, 114). For instance, from his study of the social, legal and economic relationships among the Yurok, Hupa, and other Northern California Indians before European influence, Goldsmidt (1951: 506) concludes that these Indians had "a culture which reflects in surprising degree certain structural and ethical characteristics of emergent capitalistic Europe", and as a consequence, they were "a busy and creative people . . . [and] poverty was not found here" (Goldsmidt 1951: 513-514). Furthermore, an examination of the emergence of commerce in the medieval period (Benson 1989), as well as the relationships in modern international commercial communities (Benson 1992) and within domestic trade associations (Benson 1995) reveals that they are ruled by modern versions of the same kinds of norms (ethics, morality) and institutions that develop in primitive societies.¹¹ And in this context, Wesson (1978: 173) explains that in Holland of the seventeenth century,

The Dutch liked to consider their material prosperity as proof of their virtue. Perhaps it was, for the Dutch were credited with such traits as cleanliness, stolidity, patriotism, modesty and straightforwardness ... They seemed particularly immune to bribery. Honesty was one secret of their commercial success. Incidentally, no other people provided so amply for their poor as the mercantile Dutch. (Wesson 1978: 173).

The same was true of England of the eighteenth century, where "commerce in open markets" required dealings on the basis of "equality, according to recognized rules and by mutual consent" so the merchants were "famed for honesty;" but in "seeking security for property and person, freedom to produce and enjoy wealth," they were also characterized as "generous, sober, and charitable" (Wesson 1978: 197, 199).

Entrepreneurship and Honor: Additional Reasons for Benevolence Norms. Tribal and clan organizations generally have strong norms regarding loyalty and respect for leaders but only if the person aspiring to a leadership position had specific characteristics. Consider a leader ("big man") among the

Kapauku Papuans of West New Guinea, who essentially acted as a nexus of the voluntary relationships that dominated Kapauku life. The first important characteristic was that he had to be a tonowi (Pospisil 1971: 67): "an individual who has a great amount of cowrie-shell money, extensive credit, several wives, approximately twenty pigs, a reasonably large house, and many cultivated fields." The wealth accumulated by an individual within a Kapauku community almost always depended on that individual's work effort and skill, and his ability to cooperate with others. Therefore, anyone who acquired sufficient property to be a tonowi was likely to be a mature, skilled individual with considerable physical ability and intellectual experience, and perhaps more important, someone who had a history of cooperative behavior. He deserved respect. This was not unique to the Kapauku Papuans, as those who gain wealth in close-knit communities are generally held in very high regard (Benson 1991, Pospisil 1971).

Not all tonowi achieved respect that would attract substantial numbers of others outside his own family to regularly rely upon him as leader (Pospisil 1971: 67). Long-term leadership required that gains from entrepreneurial activities and innovations be dispersed. Thus, a self-interested entrepreneur within a close-knit community rationally choose to pursue activities that benefited others in the group and generously spread the wealth. Innovations that may generate relatively large returns for the entrepreneur can also be accepted by the group if the entrepreneur generously disperses the benefits in the form of gifts. Indeed, in primitive societies, the honor of being recognized as a leader is often "purchased" through public displays of generosity demonstrated at occasions such as marriages and in connection with disputes, in the form of "gifts" on behalf of the leader's followers in order to secure good marriages or buy peace among disputants. For instance, among the Kapauku, "The way in which capital is acquired and how it is used make a great difference; the natives favor rich candidates who are generous and honest. These two attributes are greatly valued by the culture" (Pospisil 1971: 67). The honor of being recognized as a maagodo tonowi (a "really rich man") and therefore a leader was "purchased" through such displays of generosity, since such a leader could expect to benefit in the future through greater opportunities for exchanges and reciprocal obligations of loyalty.

Another source of prestige for entrepreneurial leaders can be skill and bravery in battles against external enemies (Benson 1991; Ridley 1996: 166), as emphasized in the next section, since one potential source of wealth, for both leaders and followers, is the productive efforts of individuals in other groups. However, even these leaders typically had to display generosity within their own communities. Among the Comanche of nineteenth century America, for instance, disputes were generally resolved through negotiation,

but in situations where an imbalance of bargaining power existed, there was an alternative: "Men whose status was so low that on the personal and kinship basis they were, in effect, without status were still guaranteed protection under the Comanche law . . . There was the institution of champion-at-law" (Hoebel 1967: 198). The champion-at-law was generally a "war chief" who served to represent a damage claim in the bargaining process and, if need be, in physical combat. There were no payments to convince a warrior to act as a champion. The prestige purchased by giving such support to others seems to have provided sufficient incentives, however. Hoebel (1967: 200) concludes that the "The institutional capitalization of these factors is an amazing piece of social engineering", but norms associated with obtaining and maintaining honor are common among close-knit groups, and one way to do so is in the context of dispute resolution. Third party mediation or arbitration often develops in close-knit groups, for instance, and entrepreneurs such as Tonowi typically offer to help resolve disputes and provide advice free of charge (Pospisil 1971; Benson 1991). "Fair" non-violent dispute resolution is attractive to community members because it avoids the spillover costs associated with violence dispute resolution, and it is attractive to the "suppliers" of such dispute resolution even when they are not explicitly paid, because it enhances their prestige. In other words, both generous gift and advice giving (e.g., dispute resolution) serve as signals that the individual is successful, cooperative and trustworthy, and therefore an attractive partner for joint ventures and trade. As Ridley (1996: 138) puts it, such acts "scream out 'I am an altruist; trust me.'" And in fact, while such behavior can be explained as purely self-interested, leaders probably believe that their motivations are altruistic.

Natural Law, Natural Altruism, or Endogenous Conformance to Norms? Vanberg and Congleton (1992: 429) conclude that perceptions "of what is moral vary with relevant differences in exit costs. At the high-cost end of the spectrum, moral justification for tit-for-tat and retributive behavior seems to be fairly common, whereas Prudent Morality gains in importance as we move to the low-cost end." In other words, morality evolves when the benefits of adopting a different norm exceeds the costs. Actually, however, the discussion up to this point, based on game theory [including the analysis in Vanberg and Congleton (1992)] and property rights literatures, simply suggests that much of the behavior often seen as moral (e.g., trustworthiness, cooperation, sharing, charity) can be quite rational for self-interested individuals under particular circumstances. Perhaps moral norms do not exist at all, as clever calculating people consider their strategies and behave accordingly? "Conformist" behavior within groups is a widely observed phenomenon (Ridley 1996: 181-193), however, and such conformist behavior need not reflect the ongoing (case-by-case) rational calculation implied by game theory. In particular, the internalization of norms by adopting them as

"beliefs" allows individuals to avoid the high cost of calculating expected outcomes in every situation.¹²

As noted above, significant limits on abilities to reason and to absorb knowledge means that individuals are not able to use conscious reason to evaluate every particular option in the array of alternatives that are available, so rational individuals will often find it beneficial to voluntarily conform to rules, including norms, in an almost unthinking way. For instance, religion and mythology about ancestors or a combination of the two play important roles in some (although certainly not all) systems of group-specific norms, and in a world of uncertainty and high transactions costs, this is a rational development (Holcombe 1992). Religion and/or mythology can be a low cost means of communicating and conforming to behavioral rules without having to actually invest time and effort in learning precisely what the costs and benefits of such behavior are.

In a primitive society, where knowledge is very scarce and uncertainty is very significant, the adjudication of disputes tends to be highly ritualized or regularized, for instance, as North (1990: 23) observes [also see Pospisil (1971) and Benson (1991)], so that individual choices are structured in ways that mitigate the effects of uncertainty. In this context, Burkett (1996) explains that one of the benefits of religion in primitive (and medieval) societies was to reduce the cost of delineating property rights and enforcing contracts through the belief in oaths. Violation of oaths was expected to result in retribution from the gods, so believers had strong incentives to live up to their promises. The same can be said for the general belief in the validity of trial by ordeal in medieval Europe where strong religious beliefs that the righteous would be saved while the immoral would be punished created incentives to behave honestly.¹³ Holcombe (1992: 1) suggests that: "The people who accept fictions could see with little trouble to are in fact not true, but people still behave as if they are true because such behavior serves a larger social purpose." But recall Frank's (1988) argument that it is difficult for humans to pretend that they believe something that they actually do not, so if acting as if such beliefs are real is desirable then it is rational to actually adopt the belief and not question them. As McCloskey (1994: 182) concludes from a telling anecdote related by a woman at a cocktail party whose roofer, at his own instigation, had redone a bad roof for free: "A reputation for fair dealing is necessary for roofer whose trade is limited to a town with a population of fifty thousand. One bad roof and he is finished in Iowa City, and so he practices virtue with care. By now he would not put on a bad roof even if he could get away with it, and *he behaves like a growing child internalizing virtues once forced upon him*" (emphasis added). Norms and the beliefs that support them, are rationally internalized as part of the belief system that individuals in a particular institutional environment have found to be beneficial.

The contention that moral norms are rationalizations of behavior that supports the accumulation of

wealth does not imply that such norms are irrelevant. It does not imply, for instance, that individuals never violate norms because they simply adopt new ones to justify such violations. Indeed, norms are not likely to be as flexible or as readily changeable as game-theory models based on rational calculations might imply. Once beliefs are established and used to dictate behavior in an uncalculating way, they may be quite inflexible even in the face of conflicting conditions. Conditions may have to change quite dramatically before an individual will reevaluate established beliefs, since the costs of such a reevaluation and establishment of new norms might be quite high.¹⁴ This relative inflexibility implies that individuals may resist changes in institutions that would be desirable if they were fully informed, because the behavior required under the institution changes conflicts with established beliefs. Once it becomes apparent that existing norms are in significant conflict with an individual's interests, however, so that the individual must either violate the norm or act very irrationally (e.g., repeatedly forgo obvious benefits or incur obvious costs), an individual will face a moral dilemma as she/he is forced to question the validity of existing beliefs. The impetus for rationalizing new norms arises. Thus, the rationalization of norms does not imply that all norms are always "rational" when considered in the light of full information or immediate circumstances.¹⁵ Rather, the argument is that when they evolve, the direction of evolution can be predicted with the economic model of rational decision making.

The discussion up to this point suggests that as groups form, incentives exist for members of these close-knit communities to follow the Golden Rule in their dealings with other members of the community; that is, to establish, internalize, and conform to norms of cooperation, honesty, and generosity. There are other potential explanations for such beliefs, of course. If some natural law, or natural morality, is universally recognized because of reason, the dictates of a god, or genetic "hard-wiring" through natural selection of cooperative behavioral traits,¹⁶ people could fulfill promises, respect other peoples' rights, and in general, feel sympathy, kindness, consideration for others, without the rational self-interested preferences suggested above. Similarly, much of the behavior predicted above might also be predicted by assuming altruistic motives rather than narrow self-interest. If the same institutions can be explained by assuming natural law, unrestricted altruism, or personal self-interest, does it really matter what the true motivation is? Yes. After all, if self interest in preserving a private property arrangement is even a significant part of the motivation for various moral norms, then it follows that preventing the evolution of or undermining the stability of private property rights will also prevent the evolution of or undermine the development of such norms. A theory of moral behavior based on an assumption of altruism alone, or of some sort of hard-wired natural law, implies

that the institutional environment does not matter. But there are reasons to expect that institutions do matter. For instance, much more voluntary "charity" appears to be targeted at individuals in identifiable communities than at other communities, and while a pure altruist would not require recognition for his gifts, the fact is that many gifts are "repaid" by public recognition, enhancing an individual's prestige. More significantly, even superficial observations quickly reveals that to the degree that many (all?) individuals adopt cooperative behavior consistent with the Golden Rule and philosophers' concepts of morality, they do so only under certain circumstances in their interactions with only selected other individuals. Wesson (1978: 161) points out, for instance, that the Renaissance Italian merchants were reliable in commerce and generous to their communities, but that they also practiced in the "intrigue and faithlessness recommended by Machiavelli" when it came to political matters. In order to understand such apparently immoral behavior on the part of individuals who apparently adopted moral behavior in many non-political activities, we must consider the conflicting incentives that arise when an individual's wealth can be expanded through voluntary cooperation or through involuntary transfer.

IV. Coercion, Redistribution, and the Evolution of Inter-Group "Morality"

No community evolves in complete isolation. Even with the development of agricultural technology, close-knit groups tend to remain relatively small, and all humans distinguish between group members and outsiders (Brown 1991: 136). Krebs and Denton (1997) explain that humans quickly classify others as members or non-members of their own group, and that all non-members tend to be viewed as being alike. They are perceived as enemies. And in this light, anthropological and historical evidence suggests that intra-group conflict has been an almost ubiquitous characteristic of human history.

Group Loyalty and Intergroup Relationships. Since a key function of cooperative clusters is to establish and secure private property rights, and such rights are insecure if outsiders are able to "invade" and take the property, one joint product of a cooperative group is likely to be mutual defense. In fact, an external enemy can strengthen group cohesion (Wesson 1978: 184, Ridley 1996: 174), leading some to actually suggest that moral norms are important because they enable groups to be sufficiently united to deter their enemies, not because they allow people to create order (coordination) within their groups (Alexander 1987). Clearly, norms that support the production of mutual defense against enemies evolve, and an important part of an individual's belief system will be "a concept of them and us" (e.g., tribalism, patriotism) where individuals are expected to aid in the defense of the "community." A more plausible scenario than Alexander's (1987), however, is that these mutual-defense norms simply evolve along with intra-group norms of cooperation (e.g.,

prudent morality, generosity, mutual insurance) as part of the overall objective of securing property rights. And as suggested above, one source of prestige for entrepreneurial leaders is skill and bravery in community defense **or** in aggression against enemies. After all, a potential source of wealth, for both leaders and followers, is wealth created by individuals in other groups, if it can be taken.¹⁷

In order to consider the consequences of this method of wealth enhancement, note that as wealth accumulates and some individuals prove to be less productive than others, these individuals may perceive that they have significant comparative advantage in violence. One group may rely on hunting, for instance, and while the improvements in technologies for hunting resulting from specialization (e.g., the dart thrower) can enhance wealth in the short run, the long-run effect can be quite different. Many migratory animal populations were hunted into extinction by primitive groups (Ridley 1996: 227-247) because ownership could not be established until an animal was killed. As scarce huntable resources are depleted the group's members might accumulate relatively less wealth compared to members of another group claiming relatively fertile land and settling into agricultural production. However, because the members of the group relying more on hunting than on agriculture also develop new weapons and other inputs to hunting (e.g., horses, ships) that can also be superior technology for warfare, and become skilled in the use of those inputs, they develop a comparative advantage in violence. Therefore, an entrepreneurial leader skilled in violence and especially in organizing joint production of violence, may expect that an attractive way to gain property rights and wealth is through organized aggression against another community. He may persuade members of his community to act as a "firm" for the joint production of plunder. Not surprisingly, many historical examples of organized plunder involve cooperative communities with established internal trust relationships such as those described above (e.g., Apache, Vikings).¹⁸ Such raiding was probably legitimized in the minds of the raiders by the "us-against-them" views that arise in the context of the morality of group loyalty discussed above. After all, given the belief that some other group is made up of enemies, such aggression can easily be rationalized - "the best defense is a good offense" - particularly when the expected gains in wealth exceed the expected costs. Indeed, members of a group are likely to rationalize such raiding through beliefs in the moral superiority of their group, as implied by the first quote at the beginning of this paper. Rosenberg and Birdzell (1986: 94) note, for instance, that during and after the middle ages, in the Mediterranean "Differences of religion between the Moslems and Christian furnished a pretext for mutual depredations.... It legitimized the pirates by renaming them privateers."

Many other examples exist as well. The internal order of the commercial communities that

dominated many of the cities in ancient Greece and late-medieval/early-modern Europe depended on cooperation created through trust, for instance (Fox 1971: 37-39, 65-66; Benson 1989), but one of the most important "commodities" traded in both periods was slaves (Fox 1971: 35-36, 62-63). The Greeks often sent their own ships on raids to capture slaves, while the Dutch and British created markets for slaves that encouraged others to actually capture them. No doubt, many slave traders felt morally superior to those who were being enslaved, perhaps even rationalizing their behavior because they were "improving the lot of the savages" by civilizing them and giving them an opportunity to improve their living conditions (whether true or not).

Extortion. Raiding for plunder and slaves may produce relatively small returns compared to the wealth that might be extorted over time if productive people are allowed to continue to combine their productive efforts with the resources they control in exchange for continuous payments of "protection money" (tribute, taxes). Therefore, an entrepreneurial leader (e.g., war chief) may advocate invasion and occupation of the territory of another community, intending to tax those who are conquered as they continue to create wealth. The most successful examples of protection rackets by modern organized crime typically involve kinship or ethnic "communities" that have strong internal trust relationships supported by recognized norms of behavior [e.g., see Gambetta (1993: 57-58)], for instance, although the territories controlled by such efforts are often relatively small (e.g., a few blocks of a city, part of the Island of Sicily). Much larger scale protection rackets exist, however. Oppenheimer (1908) contends that the origins of the earliest states trace to precisely this situation, for example, as nomadic hunting and/or herding communities from the relatively unfertile mountains, deserts, or sea coasts, invaded and subjugated those who had settled in fertile valleys, setting up "protection rackets." Many historians and political theorists also characterize the earliest states (e.g., in Egypt, Mesopotamia, and China) in this fashion (Levi 1988: 11). Carneiro (1970) adds that successful creation of relatively permanent states of this type occurred where exit by those being subjugated was very difficult due to the surrounding hostile environment (e.g., deserts, mountains, other hostile communities). Indeed, a vital institutional objective of an entrepreneurial extortionist must be to erect barriers to exit from the extortionist game [i.e., establish a "monopoly in violence" over the subjugated territory]: "For the real tyrant, hardly any measure of security is more pressing than to raise barriers, psychological and political, to fence in his realm" (Wesson 1978: 190). After all, if a potential target for extortion can turn to another "firm" specialized in the sale of true protection, to an alliance of cooperative groups that jointly produces defense, or to another protection racket which will fight for control (Gambetta 1993: 31), then the

extortionist's ability to extract tribute is significantly limited. The regimes of many dictatorships of the twentieth century clearly fall into the same classification as these early states [and even the institutions of modern democracies can be traced to such initial conditions (Levi 1988; Benson 1999)]. The strongest evidence of the endogeneity of morality arises when one group successfully achieves dominance over another. As a result of such dominance, the moral norms that apply in both groups are likely to change.

When a group that uses cooperative procedures to maintain internal order also acts as an organized protection racket, there is "honor among thieves," but the same moral rules clearly do not apply in interactions between the conquerors and their subjects. Indeed, as a "class system" is created and maintained through coercion, "law" in the form of discriminatory rules mandated by the extortionist at the "top" and imposed downward becomes necessary (Benson 1994b). The entrepreneur in extortion is no longer simply a "leader" who achieves his position through persuasion. He must become a "ruler" (rule maker and enforcer) who continues to persuade supporters to work within the extortionist organization while also coercing tribute from those who have been conquered. Such discriminatory rules are likely to be rationalized by the conquerors, however, as natural extensions of their community norms and the view that those who are conquered are morally inferior.

Resistance to discriminatory rules can be quite strong. Indeed, organized revolt is possible as numerous weak individuals form a cooperative group to take property rights from the powerful individual and his support group.¹⁹ The American Revolution clearly provides an example (as does the unsuccessful whiskey rebellion against the newly constituted American government). Thus, the internal dynamics of the transfer system appears to be relatively unstable (Levi 1988: 44). Other groups outside the ruler's jurisdiction may also pose significant threats to the ruler, or they may see the ruler as a significant threat to them and mount a preemptory offensive against him as a defensive tactic, suggesting that there are external sources of instability as well. There are ways to reduce such instability (i.e., insure against disruption of the newly imposed property rights system), however, and rulers have strong incentives to exploit them: "They choose among the feasible set of options, and they can act to change that feasible set... [T]hey must interact with constituents, agents, and the representatives of other polities. To achieve their ends, they must coerce and bargain, develop their resources, and, often, alter their constraints" (Levi 1988: 11). The kinds of institutional developments which arise are discussed in Levi (1988), Holcombe (1994), and Benson (1999) so they are not detailed here. However, many of these institutions have implications for the evolution of beliefs about what constitutes moral behavior, so let us consider a few examples.

Bureaucratic Norms. Part of the extortionist organization will become specialized in policing and punishment in order to induce compliance with discriminatory rules and reduce internal instability.²⁰ Instituting rules such as standardized weights and measures, monopolization of money to standardize the measurement of taxable value, developing land surveys and records of title, conducting population censuses, and so on, also all tend to lower measurement and monitoring costs (Levi 1988: 29), so bureaucratic institutions tend to multiply. For these organizations to fulfill their functions, cooperation in production and exchange (e.g., of information and support) is necessary. Initially they are likely to be made up of members of the close-knit group (e.g., tribe, mafia family) that was successful in aggression and subjugation, but if the territory and/or population under control is large enough, more employees will be recruited into the bureaucracy. New cooperative arrangements will be required.

The cooperation that develops in bureaucracies tends to be within spontaneously-evolving "informal networks" that serve as the non-market institutions of exchange through which individuals from the ruling elite, politically influential individuals and organizations, and members of the bureaucracies cooperate in order to obtain information and benefits from each others, and to circumvent various administrative rigidities that inevitably characterize bureaucratic organizations (Breton and Wintrobe 1982: 78-87, 99-106). Informal arrangements within bureaucracies have to be built on trust (Tullock 1965: 37), of course, so behavior in these networks can be quite "moral" in the senses discussed above - behavior based on honesty, generosity, cooperation, and group loyalty. Indeed, Tullock (1965: 37) emphasizes the importance of the almost unconscious influence of "cultural environment" in these networks and suggests that "As a result of his indoctrination in a native cultural pattern, the individual simply will not realize that there may exist alternative ways of doing things. This unconscious cultural indoctrination will tend to be reinforced by rational considerations. In order to be successful, the politician must be trusted.... He must become an organization man." The informal networks bind an individual to behavior expected by others within his network, although not to behavior demanded by people outside the network (Tullock 1965: 37). For example, Tullock (1965: 38-40) explains that a successful bureaucrat must be loyal to his immediate superior even if it means frustrating the desires of someone higher up in a bureaucratic hierarchy. Superiors may rationally expect to be treated with respect by subordinated, and feel morally justified in expecting considerable deference, as suggested by the issues discussed in the second quote at the beginning of this paper (Clarence Thomas' belief that he had done nothing wrong in pursuing certain favors from his subordinate). Such loyalty is valued even by those higher up, to such degree that when they look for people to promote to positions immediately below

them (e.g., to replace someone who has been frustrating their desires) they often promote those who were strongly loyal to a direct superior (even if the person was frustrating their desires). This suggests that loyalty and cooperative behavior towards other individuals tends to be turned off and on as changes in job assignments create new loyalties and end old ones, perhaps explaining the other aspect of the second quote (Anita Hills willingness to testify against Justice Thomas when they were no longer in the bureaucratic relationship that they had been in, even though she did not raise such charges when they were in that relationship). Endogenous norms are institution specific, not individual specific.

The primary purpose of many bureaucratic institutions is to take wealth from some and transfer it to others.²¹ In order to do so "in good conscience" the members of the bureaucracies are likely to develop beliefs that justify their actions. Thus, for instance, in the "bureaucratic feudalism" that developed in China, Rosenberg and Birdzell (1986: 88) note that "A class of scholar-bureaucrats held classical learning in high esteem and, at the same time, cultivated a contempt for material goals or acquisition" through productive and commercial means, but the authors follow that observation with the parenthetic: "Not that these values dictated an ascetic life-style to the mandarins themselves." By developing beliefs that the pursuit of "private interests" is contemptuous, the bureaucrats can easily rationalize their expropriation of the wealth created by such pursuits, and their consumption of substantial benefits purchased with that wealth. They also probably rationalize the activities of their bureaucracy as serving some "public good," of course, making such takings even more justifiable. As Breton and Wintrobe (1982: 152) explain, "One need not assume Machiavellian behavior, deceit, or dishonesty on the part of bureaucrats, because in all likelihood the pursuit of their own interest will be, as it is for everyone else, veiled in a self-perception of dedication and altruism."

Aristocratic norms. The extortionist/ruler may be able to reduce the threat posed by other powers using the types of strategies employed by entrepreneurial leaders within cooperative communities, but in this case they apply in a different perhaps less close-knit network. As Ridley (1996: 123) notes, for instance, lavish gift giving was widely practiced among European monarchs, and similarly, Gambetta (1993: 47) explains that "acts of generosity are among the preferred means of advertising" for mafia leaders. The purpose of such gifts is to create "an unspecified debt whose settlement is postponed" (Gambetta 1993: 47), but the nature of the debt is well understood. It is one of loyalty to the giver - a debt of "honor." A mafia leader is in fact referred to as a "man of honor", for instance (Gambetta 1993: 111 and elsewhere), and Gambetta (1993: 54) explains that "creating lasting bonds" constitutes the usual organizational method of the mafia. Essentially, some of the extorted wealth is transferred to potentially powerful individuals in exchange

for an agreement to recognize ("honor") the extortionist's jurisdictional claims (i.e., not to oppose his extortion efforts directed at others). If the relative power of a ruler and the potential rival is quite similar, such exchanges may produce a non-aggression alliance by recognizing each others' jurisdictions. In other words, the extortionist leaders cooperate by agreeing to direct their power against other less powerful individuals and groups rather than against each other. Each honors the other as an equal while viewing those who have been subjugated as inferior. Gambetta (1993: 46) quotes mafiosi Antonino Colderone, to indicate the inflated self-image that such a system creates: "You will forgive me if I make this distinction between mafia and common criminals, but it really matters to me. It matters to all mafiosi. It is important. We are mafiosi, the others are ordinary men. We are men of honor. And not so much because we have taken an oath, but because we are the 'elite' of the underworld. We are far superior to common criminals." Such attitudes also characterize the aristocracy of a feudal monarchy. They are, in their own minds, morally superior to commoners.

Another alternative arises when power is less equal, but winning a violent confrontation is still very costly and/or uncertain. When one extortionist organization is relatively powerful but perhaps not powerful enough to be assured of victory, it is rational for the weaker rival to agree to "honor" the ruler and accept certain obligations in interacting with the strongest rival (e.g., as between feudal kings and their powerful "vassals" - barons, earls, etc.) while retaining a good deal of power within his jurisdiction. The person with less power is, in a sense, a subject of the person with more power, but they are near equals. A hierarchical cartel of political elites is created. Such Lord and vassal relationships place strong emphasis on courtesy, loyalty, obedience, bravery, and honor. These characteristics become norms defining rights and duties that are adopted by those who are powerful enough to be in a position to trade for mutual support, as in the feudal relationships in much of Europe during the medieval period. They are not unique to medieval Europe, however. Early Confucianism in the semi-feudal age in China, and the Zen philosophy in feudal Japan both involved strong norms of this type (Reischauer 1956: 42-43). Indeed, the "ethical code" in Japan included "an acute sense of honor, which when sullied could only be assuaged by revenge or by *seppuku* (also known as *harakiri*, suicide through disemboweling)" (Reischauer 1956: 43). Such "mythical beliefs" also characterize the mafia, where mafiosi set themselves up to be "radically different from everyone else" (e.g., honorable, loyal, generous) in an effort to "induce blind loyalty rather than trust" (Gambetta 1993: 46).

An individual who may have enough power to resist the extortionist might not actually have his own jurisdiction for extortion, of course. He may simply agree to be subjected to the extortionist's protection

racket as long as he is relatively free to pursue his own objectives and does not have to pay much in the way of protection. Indeed, the extortionist may offer to use his institutions of violence to grant to and even protect property rights claimed by such an individual. In this way that individual can gain protection from other potential extortionists in exchange for pledges of loyalty and support, and perhaps some tribute. As a result, the "protection racket" can involve a mix of rules supporting extortion of the weak and protection of the relatively powerful. In the mafia, for instance, a potentially "powerful customer is always treated with respect" (Gambetta 1993: 165). Gambetta (1993: 21) quotes a mafioso describing such a relationship: "With regard to the nature of these relationships, I must stress that they cannot be explained as the result of coercion. Those who cooperate expect certain advantages. True, one cannot expect these relationships to be on an equal footing, as it is always clear that one of the parties is a man of honor; yet the other party makes himself available."

Despite the emphasis on loyalty and honor in relationships between the political elite, these relationships actually can be quite fragile if they are conceived of as applying between individuals rather than characterizing a particular institutional environment. Loyalty will appear to be quite powerful as long as the distribution of power is stable, but if the ruler appears to be weakening, or if the holdings of some member of the aristocratic cartel appear to be vulnerable to takeover, loyalties can quickly change. Gambetta (1993: 24) suggests, for instance that "loyalty and friendship - key terms in the mafia lexicon - are, as it were, killed by inflation: everyone is invited to betray everyone else, and friendship never stands in the way of commercial gain." Collusive agreements can keep such activities in check, but "honor" must be earned by vigilantly maintaining positions of relative power. In this same vein, Tullock (1965: 31) contends that because someone who conforms strictly to a cooperative moral code in a political environment has fewer options available in competing for the attention of those with power to grant privileges, budgets, and so on (rulers as well as superiors in bureaucratic agencies, legislators, etc.): "the man who is a success in most political systems has had to cut corners, to lie, or at least to distort the truth, and to engage in some back stabbing." Thus, Tullock (1965: 26) proposes that understanding the behavior of successful political actors (including higher level bureaucrats) requires understanding the "behavior of an intelligent, ambitious, and somewhat unscrupulous man in an organizational hierarchy." But if Tullock is correct, other members of the political community are also likely to be "somewhat unscrupulous" in their relationships with successful politicians because they recognize that the promises and claims made by these politicians are not always credible (i.e., they depend on the perceived political power of the other party). Thus, the unscrupulous behavior can be rationalized as the

"right thing to do" under the circumstances. The behavior that former President Clinton is attempting to justify with the second quote listed at the beginning of this paper clearly falls into this category. Given the reputation for opportunistic takings that virtually everyone with political power has, however, "political intrigue" in the form of constant maneuvering by various powerful groups in an effort to gain some advantage, shifting alliances of convenience, "corruption" and so on, is likely to be a better characterization of behavior in such an environment than morality involving unconditional loyalty to a particular individual. Loyalty will be to those with power as long as they can maintain their power, but when a new power arises, loyalty can quickly shift and be just as strong (or tenuous) as it was under the previous ruler. As suggested above, behavior is dictated by the institutions of power.

Class norms. The us-against-them tribalism of inter-community rivalry tends to be replaced by a "class" morality when one group is conquered by another. The members of the "upper classes" initially consists of those who are part of the extortionist's group (e.g., the war-chief's clan or tribe, the "royal family" and household in a monarchy), but it expands to include those with sufficient political power to obtain privileges and protection from the ruler (e.g., the aristocratic elite, and other groups discussed below such as religious leaders and politically powerful merchants) and perhaps those who sell their services to the extortionist organization (e.g., bureaucrats, at least at the upper levels of the bureaucratic organizations). Rationalizing their "us-against-them" beliefs can lead to a class morality wherein members of each class tend to respect and cooperate with their fellow members, while feeling morally justified in treating members of the other class differently.

Wesson (1978: 203) notes that "the real or supposed benefits of superior position make for a mentality of privilege and ... makes the inequality of elite and masses more acceptable. Superiority has to acknowledge no need for improvement." The elite look down upon the masses and find their feelings of superiority justified. After all, those subject to extortion recognize that much of the wealth they produce will be appropriated and that upward mobility is extremely unlikely, so they do not have incentives to be very productive. As Wesson (1978: 167) notes, for instance, after Italian commercial cities fell directly or indirectly under the control of Spain in the sixteenth century, the "reduction of independence and importance brought a spirit of immobility, indolence, and conformism; commerce and manufacturing slowly sank in an atmosphere of sloth and lethargy, as Italy became a supplier of raw materials for more progressive lands."²² Thus, the privileged classes tend to see the "lower classes," the politically disenfranchised, as "lazy and unwilling to contribute to the public good," and their views are born out because of the incentives that

have been created. This justifies the imposition of rules (e.g., vagrancy laws, prohibition) intended to "reform" their behavior, as well as involuntary relocation (e.g., transportation to colonies) when the needs for cheap labor dictate it or when their numbers become large and threatening. For instance, Hobbes (1651: 387), the supporter of the monarchy, writes that the able-bodied poor "are to be forced to work.... The multitude of poor, and strong people still increasing, they are to be transplanted into Countries not sufficiently inhabited: where nevertheless, they are not to exterminate those they find there; but constrain them to inhabit closer together, and not range a great deal of ground, to snatch what they find." The third quote listed at the beginning of this paper suggests that this view can be rationalized as a belief in the moral superiority of the upper classes. Those with power also have relatively secure property rights so cooperative behavior, living up to promises, and other types of ethical behavior between upper class individuals may be relatively likely. Ostracism threats can be extremely powerful, so prudent morality may dominate interaction within the privileged classes, at least outside the political arena. This gives them more reason to feel morally superior, since the lack of secure property rights and short time horizons among those who remain disenfranchised (or relatively disenfranchised) mean that intra-class cooperation for those groups may be much less likely than it is for the upper class.

Rent Seeking and the Rationalization of Theft. North (1981: 230) suggests [also see Levi (1988: 10-14)] that a ruler does not simply want to create a monopoly in violence; he will also "attempt to act like a discriminating monopolist, separating each group of constituents and devising property rights for each so as to maximize ... revenue." Indeed, the extortionist also has incentives to redistribute wealth as the relative power of subgroups within his sphere of influence changes, much as a consensual system's mutual insurance arrangements do when the incentives to cooperate change.²³

Given the incentives to use transfers as a low cost mechanism of insuring against competition, members of sub-groups have incentives to compete for favorable treatment from the extortionist.²⁴ Tullock (1967) stresses that theft and involuntary wealth transfers through the political arena (monopoly franchises, protective tariffs, taxes and transfer payments) have identical economic implications: wealth is dissipated in this competition as individuals invest resources in an effort to benefit from redistributions while others invest to prevent them.²⁵ They also have similar implications for beliefs about what is moral. Benefactors who openly condone the process can not acknowledge an obligation to respect other people's property rights. They could simply recognize that their activities are immoral, but a lower cost option is to rationalize their behavior as moral. Thus, they not only claim but probably believe that they have the "right" to take property from

others through political action.²⁶ Modern manifestations of such beliefs include "rights" or "entitlements" to public education, medical care, social security, disaster relief, farm subsidies, jobs protected from competition, limits on neighbor's uses of their land through zoning laws, and so on, all of which require taking wealth from someone else.

Little wonder that those who do not have the political power necessary to gain benefits from such rent-seeking transfers adopt a similar attitude toward property rights and easily turn to theft. Seeing those in the upper classes (e.g., those who gain wealth through political action) as elitists and snobs, they feel morally vindicated when they can take advantage of someone in that class (e.g., steal from them, shirk in work done for them). Indeed, people with wealth may be seen, rightly in many cases, as "enemies" who simply obtain wealth at the expense of others.²⁷ Since the transactions costs of determining how a person actually gained wealth are high, the tendency will be to view all wealth with suspicion, and the wealthy are likely to be popularly perceived as attractive targets for future reverse transfers or theft as individuals attempt to get back what they feel is "rightly theirs". Such actions can be rationalized, as indicated by the fourth quote listed at the beginning of this paper. Those without political influence often believe that they are actually victims themselves and that their thefts and other "crimes" are easily rationalized in their own minds as morally justified.

Opposition Norms. The transactions costs of coercive control mean that some interactions between the targeted victims of extortionists and some of their wealth will remain outside even the most powerful extortionist organization's control. Indeed, Nee (1998: 88) explains that "opposition norms" inevitably evolve as the incentives created by formal institutions and sanctions are weak relative to the incentives to pursue conflicting interests. An accepted "norm" of behavior for many people subject to extortion may be that "breaking the coercively-imposed rule is OK if you can get away with it" (e.g., a "moral obligation" supporting tax evasion and avoidance may be widely adopted). For instance, as European governments attempted to establish control over maritime trade in order to tax it, and granted franchises for numerous trading monopolies between 1500 and 1800, the "average merchant and seaman" responded with piracy and smuggling, and a substantial part of maritime commerce was carried out in violation of the laws of some nation-state (Rosenberg and Birdzell 1986: 92-96). Furthermore, the middle and even the upper classes willingly wore, drank, and ate smuggled goods (Rosenberg and Birdzell 1986: 93). Smith (1776: 898) describes the moral implications of such illegal trade, beginning with a characterization of the typical smuggler as

a person who, though no doubt highly blameable for violating the laws of his country, is frequently incapable of violating those of natural justice, and would have been, in every respect an excellent citizen, had not the laws of his country made that a crime which nature never meant to be so. In those corrupted governments where there is at least a general suspicion of much unnecessary expense, and great misapplication of the public revenue, the laws which guard it are little respected. Not many people are scrupulous about smuggling, when, without perjury, they can find any easy and safe opportunity of doing so. To pretend to have any scruple about buying smuggled goods, though a manifest encouragement to the violation of the revenue laws, and to the perjury which almost always attends it, would in most countries be regarded as one of these pedantic pieces of hypocrisy which, instead of gaining credit with any body, serves only to expose the person who affects to practice them, to the suspicion of being a greater knave than most of his neighbours. By this indulgence of the public, the smuggler is often encouraged to continue a trade which he is thus taught to consider as in some measure innocent; and when the severity of the revenue laws is ready to fall upon him, he is frequently disposed to defend with violence, what he has been accustomed to regard as just property.

Indeed, many smugglers were highly respected members of the merchant community, as well as their geographically localized communities (e.g., John Hancock).

Taylor (1982: 65) notes that the basic cooperative means of maintaining social order still exist, even in the most modern system of centralized authoritarian rule, although they may exist in "atrophied and attenuated forms." Numerous examples of centralized coercive systems can be cited where "parallel" predominately cooperative systems of norms and institutions actually dominate many and at times even most interactions (e.g., de Soto 1989; Ellickson 1991; Benson 1989, 1995; Nee 1998: 88). As economic activities are moved "underground" in order to produce wealth within the domestic economy and protect the wealth that is created, cooperative groups arrangements are likely to persist, but the fact that they must avoid detection and/or measurement will tend to alter their characteristics relative to an unhindered voluntary community. De Soto's (1989) detailed analysis of the "informal" sector in Peru is particularly revealing in this regard, as he explains that the "squatter communities" are very well organized, that members respect each others's property claims, cooperate to enforce rules of behavior, and so on. Nonetheless, the existence of a coercive ruler raises transactions costs for such groups. For instance, ostracism is less effective when property rights are tenuous due to the threat posed by the extortionist, making time horizons short and reputations less valuable. If

prudent morality is ineffective the victim may opt for retributive morality. Cooperative clusters may still aid the victim in the "illegal vigilante" exaction of retribution, of course. Under such circumstances, a considerable amount of "crime" may be "undertaken to exercise social control" (Ellickson 1991: 213; also see de Soto (1989)). Furthermore, since commitment making tends to be chilled, retributive morality (unconditional cooperation until a violation occurs, followed by exit and retribution) may not even be able to support cooperation in many situations where it could under other circumstances.

Moving underground is not the only possibility, however. If the relevant group member's wealth is mobile so they can interact across the jurisdictions of different authorities, inter-jurisdictional competition to attract their wealth production is likely. Thus, for instance, under the most successful imperial dynasties in China, a large portion of the Chinese merchant community became involved in Indian Ocean trade as "one of the most advanced entrepreneurial groups in Asia was forced to operate outside the reach of the state system and to create its own self-protection" (Chaudhuri 1985: 208). Similarly, the international merchant community of medieval Western Europe established its own commercial law, *lex mercatoria* or the "Law Merchant", consisting of rapidly evolving customary norms, and disputes were resolved in the merchants' own courts (Benson 1989). Strong incentives to cooperate through exchange, to live up to promises, to respect one another's property rights, and to support an unbiased and fair dispute resolution system arose because of positive benefits associated with repeated dealing reciprocities and reputation effects, and because of the potential for ostracism. Modern international commercial law remains as a largely voluntarily produced and enforced system of spontaneously evolving norms, despite many attempts by various coercive governments (some supported by politically powerful merchants seeking special privileges) to subjugate it over the centuries (Benson 1989). Indeed, as Hayek (1973: 81-82) explains, "The growth of the purpose-independent rules of conduct which can produce a spontaneous order will ... often have taken place in conflict with the aims of the rulers who tended to try to turn their domain into an organization proper. It is in the *ius gentium*, the law merchant, and the practices of the ports and fairs that we must chiefly seek the steps in the evolution of law which ultimately made an open society possible." Not only is trust, honesty and cooperations vital to the functioning of competitive markets, but through history, it has been the international merchant community that has probably been the most successful at resisting the political forces that undermine the incentives for such behavior.

Nationalism, Patriotism, and Other "Public Good" Norms. Since the transfer process must have losers, there will always be potential opposition, and the ruler also has incentives to undermine the disruptions and

discord that such opposition might cause. Therefore, as Levi (1988: 52-70) explains, rulers attempt to instill incentives and beliefs that lead to "quasi-voluntary compliance." For instance, rulers often have taken advantage of religious beliefs by claiming to be a god or to rule through "divine right." And "When rulers are viewed as gods, or ordained to be legitimate by gods, it is difficult for mortals to question their legitimacy" (Holcombe 1994: 160). In order to make such claims, the ruler often must bargain with religious leaders to obtain their explicit recognition of the alleged divine status. Such a bargain may result in special privileges and wealth transfers for these leaders that are comparable to the treatment of individuals who have a considerable level of military power (church leaders were often treated on a par with barons in medieval England, for instance), and/or in the use of the ruler's coercive power to support the establishment of a single religion within his jurisdiction.²⁸ Thus, people may be forced to act as if they believe the ruler's designated religion whether they do or not, but it may be quite rational to actually adopt this belief as well, for reasons suggested above.

Another legitimization tactic for rulers is to create the belief that only he can provide, vital "services" to everyone in the jurisdiction. One obvious "public good" is defense against outside threats. In fact, the ruler will have to defend the territory against outside threats in order to maintain power and protect the source of his income, but if the ruler can convince the populous that these outside threats will treat them much more harshly than his organization does, he may be able to legitimize some transfer payments to "purchase" defense (Holcombe 1994: 160).²⁹ This is a very real possibility, since these outsiders may not expect to be able to maintain power over a distant jurisdiction and therefore their time horizon may be shorter, making plunder relatively more attractive than extortion - the implications of a ruler's time horizon is discussed in more detail below. In addition, "Discontents may be diverted to a foreign cause, internal divisions may be overridden, and the common emergency justifies extraordinary discipline and demands" (Wesson 1978: 187). Indeed, the ruler actually has incentives to create an outside threat even if one does not exist. Foreign wars may be efforts to expand the ruler's domain, but even when rulers do not expect to win such wars, they have been manufactured and maintained as a way to legitimize protection money or reduce domestic opposition (Fox 1971: 52, Levi 1988: 43). If successful, such legitimization creates widespread norms like "nationalism" and "patriotism" that tend to increase quasi-voluntary compliance. Such legitimization tactics are apparently successful in many cases since national government revenues grow dramatically during wars and they apparently do not shrink back to their prewar levels after a war (Higgs 1987), perhaps in part because the ruler finds a new threat and another war arises before the quasi-voluntary compliance effects diminish.

Rulers are likely to rationalize their takings in their own minds as well, by identifying and opposing such threats. Fox (1971: 31) points out that "Even the Kings seem to have seen themselves largely as defenders of order" for instance. And while the population in general does not have to consider everything that a ruler and his organization does to be legitimate, if some activities are seen as legitimate the costs of enforcing compliance are reduced (Holcombe 1994: 159). Indeed, subjects have incentives to explicitly recognize the legitimacy of such claims as expressions of "concern for the community gives the citizens a better claim to a share in the state" (Wesson 1978: 186). Wallerstein (1989: 147) notes, for instance, that individuals "have two ways of affecting [economic policies]... They may operate within the political structure of the state or they may operate against the structure of the state in what might be called antinational activity. Patriotism is a calculation." For those who find their best options to be operating within the political environment, patriotism is likely to be internalized as a moral norm.³⁰

Wealth must be produced for it to be transferred, and private property rights create the strongest possible incentives for long-term wealth creation. Therefore, the extortionist faces a trade off. Large levels of extortion in the short-term, reduce productivity, wealth creation, and the potential for transfers over the long run. The actual degree of transfers in any period, therefore, depends in part on the ruler's time horizon (Levi 1988: 13, 32-33; Gambetta 1993: 33; Holcombe 1994: 112). If the ruler is relatively short sighted, perhaps because there are significant competitive threats to his claim of sovereignty, property rights become very insecure as high levels of transfers can be expected. However, a long time horizon implies the present value of potential future transfers are higher, so property rights will be relatively secure in order to stimulate wealth production.³¹ This creates incentives for even those who clearly are net losers to accept the extortionists legitimization claims and adopt quasi-voluntary compliance in order to lengthen the extortionist's time horizon. That is, while they want to resist the takings whenever possible, they also have incentives to recognize and even explicitly promise (pledge) to honor and obey the sovereign. In this light, recognizing a "dynasty" [e.g., a royal family in a kingdom, family succession in the mafia (Gambetta 1993: 59), the "right" of the boss in a "political machine" to select his successor] or strongly supporting an incumbent's repeated reappointment (or reelection), may be very rational when exit costs are high. People rationalize acceptance of such actions because they realize that there is little that they can do anyway, and they may in fact be better off by accepting them. Thus, even though some claims by rulers may be obvious fictions upon careful inspection (e.g., divine rights), they may be "accepted as fact for convenience" because they facilitate an implied improvement in the "agreement" between a ruler and the ruled (Holcombe 1994: 170-171). Acceptance of

these fictions and the accompanying norms of loyalty is not unlike conformity with norms in a cooperative group where the costs of taking calculated action in every case may be high (Holcombe 1994: 171).³²

V. Conclusions: Situational Morality

All of the examples cited in Section IV illustrate the final quote that begins this paper. If individuals' perceptions of morality are not endogenous, the kinds of behavior we observe in politicized societies should not exist, unless in fact, morality is simply irrelevant. However, the fact that individuals often justify their behavior in moral terms suggest that, at the very least, they believe that morality is important to those who observe their actions. But they probably also believe that their actions are morally justified. In closing let us reinforce this argument by considering the fact that individuals apparently adopt different moral norms depending on the situation that they are in. For example, the merchant communities praised above for being the most effective group at maintaining a moral environment characterized by honesty and cooperation in the face of political power (and earlier, for also being the source of considerable benevolence and generosity) are also susceptible to the incentives to take wealth, and they also tend to have considerable bargaining power in the political arena because they can threaten to exit (Smith 1776: 395; Wesson 1978: 195; Jones 1981: 86; Benson 1989). Therefore, rulers have incentives to grant merchants special privileges (wealth transfers) within their domains, perhaps in exchange for a portion of the transferred wealth (e.g., franchise fee, tax, campaign contributions), or perhaps with no charges since a business located within a jurisdiction can generate more wealth production on the part of relatively immobile resources that are inputs to or complements of the merchants' enterprises. Not surprisingly, merchants virtually always take advantage of rulers' coercive powers to obtain wealth transfers within political jurisdictions, often becoming one of the most privileged political classes. Medieval mercantilism was a system dominated by merchants dealing with kings to restrict competition in favor of domestic monopolies and guilds, and that system has a firm hold within many of today's economies (de Soto 1989). In fact, in every political jurisdiction, economic regulations limit competition and generate rents for politically influential businesses (Stigler 1971). These merchants appear to be adopting different moral norms in different situations, rent seeking where it pays, and behaving cooperatively and benevolently where it is likely to generate more profitable outcomes. Modern merchants often belong to trade associations that facilitate trade [e.g., by supporting ethical business behavior with communication channels, arbitration services, ostracism threats, etc. (Benson 1995)] and simultaneously lobby for privileges such as import limits and licensing restrictions that protect them from competitive entry. Similarly, a modern corporation has plants that produce new wealth sold through voluntary exchange, and

other "plants" (lobbying offices) that pursue protection from competition and other political privileges. It is not "economic power" that undermines incentives to cooperate through voluntary exchange and contracting, however; it is political power. After all, business groups are not the only organizations that successfully operate in both the economic and the political sphere.³³ A farmer grows wheat intended to make bread for consumers, and belongs to an organization that lobbies for wheat subsidies and price supports that transfer even more wealth from bread consumers. A member of a labor union cooperates in the joint production of a new product by selling his specialized labor services, and contributes to political actions in pursuit of protective tariffs and quotas, minimum wage laws that raise the price of substitute labor, and so on. An environmentalist who gains satisfaction (wealth) from knowing that certain habitats and species are protected voluntarily recycles and perhaps contributes to an organization that purchases threatened habitats, but also contributes to organizations that lobby for restrictions on the use of other peoples' property without compensation for the resulting loss of wealth. A member of a religious organization voluntarily contributes to build a house of worship and pay for the services of a specialist in religious ritual, expecting salvation in return, while simultaneously lobbying for tax exempt status, business closures on holy days, imposition of "sin taxes" or outright prohibition of activities that the group members believe are sins even though other in the political jurisdiction do not.

The fact is that when sufficient bargaining power is accumulated to make rent seeking an option, individuals will tend to simultaneously pursue both economic and political means of wealth enhancement, but individuals probably rationalize their actions in both political and economic arenas as moral. Thus, they are adopting different moral norms for different types of interactions. If not, they are choosing to selectively violate the moral norms of cooperation because they are simultaneously pursuing wealth through economic and political means, and the psychological costs of such "immoral" behavior would appear to be very high.

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ENDNOTES

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1. For instance, see Axelrod (1984), Ellickson (1991) and Ridley (1996). The contention that preferences, including moral beliefs, are endogenous is not new to economics. It goes back at least to Smith (1776). It is also one of the cornerstones of the "Austrian School" which traces to Menger (1883) who emphasized that the origin and evolution process of many social institutions, including systems of rules, is the same as the spontaneous order Smith (1776) describes for markets. Indeed, citing the passage of time, pervasive ignorance, and inherent uncertainty, Austrians see preferences as continually changing as people undergo the experiences of life (Vaughn 1994: 80).

2. For examples, see Ellickson (1991), Cooter (1998), Voight and Kiwit (1998), Ridley (1996), Vanberg and Congleton (1992), and Nee (1998). The economics of crime literature which developed following Becker (1968), also recognizes that rational individuals will behave differently depending on the incentives and constraints they face, of course, although the literature does not explicitly address the issue of morality. The endogeneity of morality is also recognized in the growing economics literature examining social behavior, including both altruism and "rotten kids," within a particular institutional environment - the family [e.g., Becker (1974), Bergstrom (1989, 1995)].

3. The historical importance of deliberately designed rules as actual direct determinants of behavior of the targeted population also is probably much less than is popularly perceived, since people rely on norms to govern much of their behavior even when some formal rules ("positive law") appears to apply (Ellickson 1991; Benson 1989, 1995).

4. See Rubin (1998) for a criticism of the "state-of-nature" approach, but note that many of those criticisms probably do not apply to the following presentation.

5. Violence is defined as the allocation of resources (e.g., capital to build a fort, labor time in guarding and fighting) in an attempt to gain control of property and to exclude other individuals from using claimed property.

6. Where no one has a comparative advantage in violence [e.g., perhaps because the marginal product of investing in conflict is very low for all parties, as in Skaperdas (1992) and Rider (1993)], individuals can contract to recognize a relatively equal initial distribution of private property rights, perhaps based on a rule of first possession, as suggested below (Umbeck 1981a, 1981b). Given the option of employing violence as a means of securing property claims, however, an "agreement ... must ration to each individual as much wealth as he could [expect to] have through the use of his own force" (Umbeck 1981b: 40). If the agreement stems from an initial situation involving highly asymmetric capacities for violence, the individual(s) with a comparative advantage can claim property rights and wealth that others have previously claimed or produced. Indeed, a continuum of property rights arrangements is theoretically possible, ranging from slavery through situations involving a large degree of extortion and concentration of property rights, to modest taxes for individuals who could also produce effective violence if pressed, to a system of voluntary recognition and joint protection of private property rights with no coercive authority (Benson 1999). All such systems can "naturally" evolve under different circumstances, and as explained below, moral behavior varies as a result.

7. See Axelrod (1984), and see Ridley (1986: 53-84) for a review of many of the developments in the literature subsequent to Axelrod (1984). There also are conditions that can produce a cooperative solution even in a one-period game. Skaperdas (1992) and Rider (1993) develop two-person, one-period models of cooperation,

conflict, and power, for instance and deduce three possible outcomes: (1) "full cooperation," when neither person perceives a high marginal product from investments in violence, so neither does and they recognize a private property arrangement (Rider 1993: 152); (2) "conflict" when the marginal product of violence is expected to be high for both parties so each believes that increasing investments in the capacity for violence substantially enhances their probabilities of winning; and (3) "partial cooperation" when one party's opportunity cost of investing in conflict differs substantially from the other party's so that individual invests in violence, subjugating and extracting tribute from the relatively productive individual who chooses a "cooperative" strategy because it produces greater personal wealth than is expected through conflict.

8. Note that the exit option combined with multi-sided, multi-dimensional reputation effects can mitigate the consequences of asymmetries in power discussed above. The relatively weak individuals in an evolving close knit group might well be relatively strong when backed by an ostracism threat (Ridley 1996: 160).

9. The scenario outlined below is consistent with what happened in many areas of the American West where contractual associations such as mining camps, land clubs, and cattlemen's associations formed to support claims of the members and exclude outsiders (Anderson and Hill 1979; Umbeck 1981a, 1981b). Similar arrangements arose in medieval Iceland (Friedman 1979; Solvason 1991).

10. Potlatching is much more complicated than the discussion here suggests. Ridley (1996: 115-124) discusses the process as one of immediate exchange, for instance, in which an individual exchanges a material gift for "prestige", noting that such a gift can also be a "weapon" as the recipient now has an obligation to reciprocate with an even more generous gift (i.e., pay back with interest).

11. In the Italian commercial cities of the thirteenth to the fifteenth centuries, for instance, "actions were judged by success and gentlemen were judged by appearance and worth, not pedigree. Men were not born noble or made noble by a sovereign but ennobled themselves by industry, intelligence, and skill" (Wesson 1978: 160). The wealthy Italian merchants dressed modestly but gave lavishly to public projects such as universities and cathedrals (Wesson 1978: 162-163).

12. An uncalculating conformation to expected behavioral norms may also be rational in part because observing how others behave in a particular situation is a source of accumulated information (Ridley 1996: 184).

13. Many people see religious institutions as the source of moral rules. However, as Hazlitt (1964: 358) explains, morality "and the nature of our duties and obligations, have no necessary dependence on any theological doctrine or religious belief." Rather, they reflect the universal objective of wealth enhancement. This does not mean that religious institutions are irrelevant, of course, since they too can reduce transactions costs within a community. As a system of rules evolve spontaneously within a group, for instance, group members may not fully recognize the importance of their function for facilitating voluntary interaction, instead attributing the results to some mystical source. Similarly, behavior that leads to undesirable consequences might become a religious taboo. As Mises (1957: 240) notes, "Where people did not know how to seek the relation of cause and effect, they looked for a teleological interpretation. They invented deities and devils to whose purposeful action certain phenomena were ascribed. A god emitted lightning and thunder. Another god, angry about some acts of man, killed the offenders." In other words, mythology and religion functions can interact with economic functions, perhaps providing important sanctions against non-cooperative behavior (e.g., excommunication) and sources of dispute resolution (e.g., when individuals cannot decide how to resolve a dispute and avoid violence they might call upon a super-human arbitrator to determine the outcome through a trial by ordeal). On the other hand, religious institutions can also be used for political purposes, as wealth is transferred to religious leaders and their powerful supporters, as explained below.

14. Attempting to change a norm that applies generally to everyone in a close-knit community (e.g., a solidarity rule) can be particularly costly since others in the community may not recognize the benefits of doing so, and as a consequence, the norm will be backed by potential community sanctions. After all, for an obligation to achieve the status of a community-wide norm or generally shared moral sentiment, it must be widely recognized and accepted by the individuals in the affected group. The result is analogous to a unanimity (or consensus) rule for collective decision-making (Benson 1999). A unanimity rule implies that if individuals expect a rule to be biased against them,

to fail to support decisions that will enhance their chances for wealth production, or to generate greater personal costs than personal benefits, it is not adopted. Indeed, if individuals are risk averse they will be reluctant to adopt new norms, and that combined with a unanimity rule, suggests that the evolution process for community wide norms tends to be quite "conservative," guarding against mistakes. Once such a norm is adopted and backed by community sanctions, modifying or eliminating it can be difficult if other members of the community are not convinced that the change is desirable. Thus, a new unbiased rule that could enhance wealth for members of the community may not be adopted until the gains become widely recognized.

15. Indeed, some observers suggest norms are very static [e.g., as implied in Hart (1961)], making reliance on them rather than other sources of rules (e.g., legislation) "inefficient" in a dynamic environment. Norms that encourage people to be innovative and to experiment with alternative institutional arrangements can arise in a dynamic environment, however. As explained below, for instance, commercial communities develop norms to support cooperation that mirror those discussed above, and in this regard, Wesson (1978: 161), in discussing the commercial cities of Renaissance Italy, notes that the merchants were convinced that they and their wealth were "respectable and virtuous" as they abandoned the moral restraints that had applied during the medieval period as embodied in the religious beliefs in the Christian Church. When everyone in the relative community expects to be better off as a consequence of the discovery of new ways to deal with evolving circumstances, resistance to changing norms is undermined. Wesson (1978: 161) describes this as a "loosening of the restraints of morals" but a better description would be that norms were evolving rapidly.

16. Frank (1988) suggests that individuals who adopt norms that support both personal honesty and a preference for vengeance (e.g., retributive or prudent morality as described above) will have an evolutionary advantage in a primitive society, for instance, so that such preferences will become dominant through biological selection.

17. Other neighboring communities may compete for the same scarce resources but they also may offer opportunities for mutually advantageous cooperation. Thus, cooperative arrangements can and often do evolve between members of different groups, perhaps leading them to combine. Alternatively, since group affiliation mechanisms can be quite flexible, individuals can belong to more than one group as a society evolves beyond the close-knit primitive groups that have been the focus of the preceding discussion. That is, groups need not formally "merge" and accept an entirely common set of rules governing all types of interaction. Individuals only have to expect each other to recognize a common set of rules pertaining to the types interactions (e.g., trade) that evolve. Indeed, a "jurisdictional hierarchy" often tends to arise wherein each localized group has its own norms for intra-group relationships, with a separate and possibly different set of rules applying for those who establish intergroup relations and form a separate functionally focused group (Brown 1991: 136; Pospisil 1971; Benson 1991). The commercial communities of international trade provide an example of functionally rather than geographically based groups whose members often belong to other communities too. Even in primitive societies, entrepreneurs establish extensive trade networks that cross community boundaries, however (Goldsmidt 1951; Benson 1991; Ridley 1996: 195-211), essentially forming a trading community distinct from the local communities, but as such arrangements evolve they also have to be accompanied by various rules to function effectively (Benson 1991, 1989, 1999). The trading community will have a more narrowly focused set of norms because the interactions between its members are more narrowly focused. Trade is not the only function that can facilitate the formation of other geographically dispersed but functionally focused communities consisting of members of various geographically localized and often functionally extensive communities. Religion can provide similar incentives, for instance, as can the need for defense against a common enemy. In other words, cooperation is one potential solution to inter-group conflict too, although the transactions costs of such cooperation are obviously relatively high, so inter-group conflict can also be expected.

18. A comparative advantage need not result in complete specialization, of course. Indeed, if there are different margins along which individuals can adjust to expand their wealth, they are expected to do so as long as anticipated benefits exceed anticipated costs. Thus, for instance, Jones (1981: 88) asks "When does a pirate become a trader? When he sells his booty to a community too strong for him to attack, or to his own folk, as the Vikings did with the proceeds of their North Sea pillaging." Similarly, Rosenberg and Birdzell (1986: 94) note that "The history of commerce in the Mediterranean, both during and after the Middle Ages, is to a considerable degree a history of trading combined with raiding and freebooting."

19. Opportunistic breaches of promises in cooperative clusters are also possible, of course, but since everyone is likely to be relatively better off in such a community than they would be if the cooperation breaks down, individuals are relatively less likely to breach. A slave or someone subject to heavy extortion could well be better off in a state of nature, given that the master is successfully overthrown, and the status quo is clearly relatively undesirable. Thus, the incentives to find a way to successfully breach are relatively strong.

20. By spreading information, those who employ a comparative advantage in violence can develop a reputation for doing so. Such a reputation can be quite valuable as increasingly, the threat of violence alone may be sufficient to extort transfers; actual violent acts may become unnecessary. Therefore, the extortionist ruler invests heavily in policing and "punishment" to deter opposition (Gambetta 1993: 46; Levi 1988: 70) Both the punishment and policing will generally be conducted in a highly visible way (e.g., hangings and mutilations, uniforms, special weapons). although some of the members of the extortionist organization are also likely to specialize in "spying" on subjects and in investigation of potential non-compliance (Gambetta 1993: 37-38), since uncertainty can also be deterrent.

21. The development of specialists in policing and collections can create principle/agent problems as these individuals will be in a position to skim relatively large shares of the revenues and/or accept bribes to reduce the amount taken from some who are being extorted (Levi 1988: 14). Therefore the ruler is likely doubt the credibility of his own organization members' commitments to cooperate. In order to maintain such relationships, various innovations in organization can be anticipated, but various norms regarding loyalty are still likely to evolve (Benson 1999).

22. Similarly, while they were not conquered by a foreign power, the Dutch waged three wars against the English in the seventeenth century and two more against France in the early eighteenth century, and they faced increasing protectionist practices by the governments whose citizens had been the customers for Dutch traders. The result was increasingly heavy tax burdens imposed by a much more powerful and corrupt government wherein advantages could be gained more easily through politics than commerce (Wesson 1978: 174). This "drained the economy of its energy and innovative capacity. Not only did trade decline, but also shipbuilding, textile production, fishing, and agriculture.... Many industries expired without a fight. In 1670 the Dutch considered themselves superior to the British in energy and ability as well as in capital and material resources. In 1779 a Leiden clothier complained of the general lack of initiative among Dutch industrialists, a deep-rooted aversion to experimenting with new methods" (Kindleberger 1978: 141).

23. While mutual insurance arrangements in the cooperative systems described above tend to transfer to the temporarily disadvantaged who may have relatively weak incentives to respect property rights, extortion-based systems tend to transfer to those who are becoming powerful, as they have weaker incentives to respect the extortionist's claim to sovereignty. Of course, there is a potential danger that the disadvantaged will organize effectively and revolt, so some transfers also may flow in their direction if they are perceived as a developing threat. In a relative sense, however, transfers to the powerful will actually dominate, and transfers to the disadvantaged will predominantly flow from others who are not expected to become powerful [the powerless are excluded from any bargaining (Levi 1988: 11)].

24. In this setting a relevant group (or groups) for most individuals is not simply the "class" of politically powerful as a whole, but rather, the sub-group (or groups) that best represents their interests within that class that is competing with other groups in the rent-seeking game. The extortionist also encourages such "rent-seeking" competition (Levi 1988: 12), since by keeping sub-groups divided into adversarial political camps the possibility of a strong coalition forming to overthrow his rule is reduced.

25. The typical economic explanation of political rent-seeking activities is that individuals are seeking private benefits, but Kau and Rubin (1979) suggest that there is a large ideological component to the political process as well. However, if morality is endogenous this ideological component is not at all surprising.

26. The ruler has incentives to take advantage of these incentives in an effort to legitimize a claim to sovereignty and undermine opposition. He can claim that the same morality which underlies voluntary transfers also

underlies and justifies involuntary transfers: "transfers are desirable in order to aid the poor, or the elderly poor, or the family (e.g., family farms), and so on" even though most of the actual transfers go to the politically powerful who have become relatively wealthy.

27. Seeing the success enjoyed by effective political groups, the members of the lower classes are likely to both despise and envy them. Envy suggests that the "lower classes" have incentives to emulate the upper classes by attempting to organize and pursue political power in order to gain similar benefits. As methods of doing so are discovered, more groups may enter the rent-seeking competition (Benson 1984). Thus, the political process further undermines the security of property rights as they are increasingly subject to change as the ruler reacts to changing political conditions. That is, wealth is increasingly treated as a common pool, subject to rent-seeking competition, rather than as private property.

28. As with other efforts to retain control, of course, such special status creates a potential rival for power, so the relationship between the ruler and the religious organization is often similar to the relationship between a ruler and his military/policing bureaucracy or a leader and a parliament (Benson 1999): one reflecting both rivalry and cooperation.

29. There are a number of such services beyond those discussed here. The provision of roads may in fact benefit many people, for instance, although their primary purpose may be somewhat different. Roads serve important functions for the movement of military and policing personnel in order to maintain internal order and defenses against outside threats. In addition, they facilitate the ongoing redistribution process by lowering the costs of obtaining information about changes in the relative power of the sub-groups in order to discriminate among them, and of bargaining with those groups that have or gain power by connecting the ruler's central location with the outlying locations of his potential rivals (Levi 1988: 28).

30. An alternative to foreign conflicts is for an extortionist to focus on threats that are ongoing and undefeatable, but that also are not likely to be able to defeat the ruler. Internal threats, real or manufactured, can serve this purpose. It is not at all unusual for modern rulers to describe never-ending campaigns against crime, drugs, poverty, and other internal problems in the same terms that they describe external threats, for instance, in an effort to create the "moral equivalent of a war." Furthermore, the advent of politicized extortion means that crime and poverty both become more likely (as suggested above) and the provision of both policing and welfare may be seen as "public goods." Other even more sinister examples of such internal "threats" can also be cited (e.g., numerous examples of religious or ethnic persecution such as Hitler's manufacturing of the threat posed by the Jews).

31. Since the ruler must claim authority as a law maker in order to impose the discriminatory laws that produce wealth transfers, another obvious service is the provision of law, including law enforcement. Indeed, the ruler also should recognize that selectively supporting rules that originated within cooperative institutions provides a low cost mechanism for facilitating cooperation in wealth creation that he can then expropriate.

32. In this context, however, Mises (1957: 291-292) explains, political actors "have been eager to falsify historical evidence and to misrepresent the course of events. The endeavors to mislead posterity about what really happened and to substitute a fabrication for a faithful recording were often prompted by the desire to justify the their own or their party's actions from the point of view of the moral code of those whose support or at least neutrality they were eager to win." Indeed, tactics of misrepresentation and falsification of information are common in political institutions (Breton and Wintrobe 1982: 39), as they raise the transactions costs for those who might attempt to obtain bargaining power to oppose the ruler (or use existing bargaining power) if true information was available. And as just suggested, those subject to extortion may also be relatively successful if they do not question such misleading information. Of course, those in power also probably believe they are telling the truth when they offer interpretations of history and facts that confuse and mislead, or that falsification is justified in order to achieve their perception of the "public good."

33. Vanberg and Congleton (1992: 429; also see McCloskey 1994) suggest that, "contrary to a common

perception, markets are not parasitic on moral attitudes that have to rely, for their nourishment, on other social settings. Instead, the more the essential features of markets (coordination by voluntary contract) is applicable, the more the market reinforces the virtues of honest behavior that in turn, make them work effectively." And yet, "business" is widely mistrusted and despised as greedy profit-seekers who cannot be trusted. To the degree that merchants gain advantages through the political process, such views are probably warranted, and since it is very difficult to distinguish between businesses that only gain wealth through production and exchange and those which depend on subsidies, limits on entry, price supports, import tariffs or quotas, government contracts, etc., a general distrust is probably quite rational. Of course, the same people who despise "business" also probably trust many of the local businesses that they regularly deal with, particularly if they are "small" (bigness may well be correlated with political power and privilege, after all).