

THE SAVINGS & LOAN MESS: REPEATING THE TRAGEDY OF THE COMMONS

By GARRETT J. HARDIN and EDMOND G. MIRANNE, JR.

1997

(Endnotes supplemented subsequently)

ABSTRACT

This paper is an adaptation of Garrett Hardin's famous essay "The Tragedy of the Commons," published in *Science* magazine in December 1968.¹

Professor Hardin showed how a village common pasture suffers from overgrazing when each herdsman in the village puts as many cattle on it as possible, because the cost of grazing is shared by everyone, but the profits go to the individual herdsman alone. This paper applies the theory of the tragedy of the commons to the savings and loan debacle of the late 20th century and shows how privatizing gain and socializing loss ruined a once thriving sector of the American financial services industry. Our thesis is that there is a class of "no-technical-solution problems" and the savings and loan crisis is a good example.

At the end of a thoughtful article on nuclear war published in 1964, J. B. Weisner and H. F. York concluded that "both sides in the arms race are ... confronted by the dilemma of steadily increasing military power and steadily decreasing national security. It is our

considered professional judgment that this dilemma has no technical solution. If the great powers continue to look for solutions in the area of science and technology only, the result will be to worsen the situation.”²

This paper will not focus on any specific subject matter, such as the Cold War arms race addressed by Weisner and York. Our concern is rather about the kind of conclusion they reached, namely, that society’s problem-solving ability is becoming impotent and the viability of technical solutions to problems is defunct. For example, the principal root cause of the savings and loans debacle was government’s implementation of ill conceived technical solutions which were doomed to fail. Government’s failure to consider American economic human nature in the context of the connection between market deregulation, non-market forces and deposit insurance before adopting sweeping banking reforms, created a commons and foreordained tragic consequences. Good judgment and common sense were proven to be rare attributes of regulators and law makers responsible for the welfare and policies affecting savings and loans.

An implicit and almost universal assumption of policy debate is that the problem under discussion has a technical solution. A technical solution may be defined as one that requires a change in the techniques or methods, demanding little or nothing in the way of change in human values or ideas of virtue and morality. In the late twentieth century, though not in earlier times, technical solutions were and they continue to be welcome. But we must become wary of technical solutions and search for a new criterion of

judgment and a system of weighing. We will show that in economic affairs sometimes this means we must mitigate the spirit of Adam Smith.

Smith's *The Wealth of Nations* (1776) popularized the idea of the "invisible hand," *i.e.*, the notion that an individual seeking his own gain is "led by an invisible hand to promote ... the public interest."³ Smith did not claim that this was invariably true, and neither did any of his followers, but unwittingly he established a mind-set that has, ever since, interfered with positive action based on rational critical analysis. In other words, Smith's work, at least as understood by Americans, established a tendency to assume that the best decisions for individuals will, in fact, be the best decisions for society as a whole.

One of the first rebuttals to the "invisible hand" was offered by Rev. William Foster Lloyd (1794-1852), a professor of political economy at the University of Oxford (1832-6).⁴ In Lloyd's sketch the scenario of a "tragedy of the commons" is best understood using the word "tragedy" as the philosopher Whitehead used it who said, "The essence of dramatic tragedy is not unhappiness. It resides in the solemnity of the remorseless working of things." According to Whitehead, the "inevitableness of destiny can only be illustrated in terms of human life by incidents which in fact involve unhappiness. For it is only by them that the futility of escape can be made more evident in the drama."⁵

The tragedy of the commons develops this way: Picture a common pasture open to all herdsmen in a village. Naturally each herdsman keeps as many cattle as possible on

the commons; each seeks to maximize his own gain. This approach works for a time, because wars, poaching, and disease keep the numbers of both men and beasts well below the carrying capacity of the land. Finally, however, there comes a day when due to some natural or artificially imposed change in conditions, each herdsman explicitly or implicitly, more or less consciously, asks: "What is the utility to me of adding one more animal to my herd?" Each herdsman realizes that the utility of the question has one positive component and one negative component. The positive component is a function of the increment of one animal. Since the individual herdsman receives all the proceeds from the sale of his additional animal, the positive utility is nearly +1. The negative component is a function of the additional overgrazing created by the addition one more animal on the entire commons. Since, however, the effects of overgrazing are shared by all of the herdsmen, the negative utility for any particular decision-making herdsman is only a fraction of -1. Adding together the component partial utilities, each rational herdsman concludes that the only sensible course for him is to add another animal to his herd; and another, and another, and another But this is the conclusion reached by each and every herdsman sharing the commons. So, the commons is then irreparably over-grazed, and all the cattle die. Therein is the tragedy. Each herdsman became locked into a system that compelled him to increase his herd without limit, on a commons that was finite. The ruin toward which all the herdsmen rushed when each pursued only his own best interest came to fruition.

Some will agree that freedom in a commons brings ruin to all. Others will say that the concept is a platitude. This is the familiar Cassandra/Pollyanna dichotomy.⁶ In a sense it was learned thousands of years ago, but natural selection favors the forces of psychological denial. The individual benefits as an individual from his ability to deny the truth even though society as a whole, of which he is part, suffers. Education can counteract the natural tendency to do the wrong thing, but the inexorable succession of generations requires that the basis for this knowledge be constantly refreshed. A simple incident that occurred in the mid-sixties in Leominster, Massachusetts shows just how perishable knowledge is. During the Christmas shopping season the parking meters downtown were covered with plastic bags that bore tags reading: "Do not open until after Christmas. Free parking courtesy of the mayor and the city council." In other words, the city fathers instituted the system of the commons at the worst possible time. Cynically we suspect that they gained more votes than they lost by this retrogressive act.

In a general way the logic of the commons has been understood for a long time, perhaps since the discovery of agriculture or the advent of private property. But it is understood mostly only in relation to specific cases; the understanding is hardly ever generalized. Even today cattlemen leasing national land on western ranges demonstrate no more than an ambivalent understanding of it. They constantly oppose increases in grazing fees on federal lands and pressure federal authorities to increase the head count to the point where overgrazing produces erosion and weed-dominance.⁷ Likewise, the

oceans of the world continue to suffer from the philosophy of the commons. Maritime nations still holding to the “freedom of the seas” shibboleth have brought species after species of fish and aquatic mammals closer and closer to extinction.⁸

The savings and loan debacle of the late twentieth century represents another example of the tragedy of the commons. The ideas which spawned the rash economic deregulation that produced the savings and loan tragedy, began to surface in the Kennedy administration. In 1962, the year Kennedy declared the U. S. faced only technical and administrative problems, he established a Committee on Financial Institutions which considered the recommendations of the Commission on Money and Credit, a private sector group. That Commission recommended “the establishment of federal savings banks with wide ranging investment powers.”⁹ During the sixteen years that followed, more ideas supporting more flexible lending and investment powers for savings and loan associations surfaced in a series of commission reports, congressional committee hearings and other studies and recommendations.

The Johnson, Nixon and Carter administrations contributed to the movement. For example, in 1972 President Nixon’s Hunt Commission concluded that “without changes in their operations, there is serious question about the ability of thrift institutions to survive.”¹⁰ Most of the studies, hearings and recommendations prompted legislation which gradually broadened the powers of savings and loans.¹¹ The trend was evolutionary until 1978 when federal regulators and their friends in Congress supported

by like-minded thrift managers and trade association officials, launched a more radical program. By mid-term of Jimmy Carter's presidency, the collective judgment of these groups had become severely impaired and tainted by sectarianism and clientelism.¹² The pace and scope of change then shifted into high gear and the deconstruction of what remained of the fences and guardrails originally erected to maintain a stabilized monetary commons began.

The final crusade to the financial commons began with the repeal of Regulation Q, which became effective on June 1, 1978. Regulation Q controlled the interest rate level that savings and loan associations were allowed to pay on passbook savings and the rate differential between banks and savings and loans. It had remained fixed for a long time under the regulation, favoring savings and loans by $\frac{1}{4}$ of 1%, and it served as a market counterweight to the banks' use of compensating balances. It was thus a key to a stable supply and cost of funds for savings and loans. But after the introduction of cash management account ("CMA") in Utah in 1977,¹³ the savings and loans watched anxiously as the popularity of those accounts grew. By the end of 1977, over \$20 billion had seeped away from the savings and loans and into the CMAs. The thrifts saw the hand writing on the wall, and they moved to staunch the threat to their deposit base. Regulation Q became history. Upon its repeal, a savings rate commons replaced the regulation and this attracted new players such as Merrill Lynch. Over the ensuing four years the CMA accounts attracted an additional \$150 billion.

Between 1980 and 1983, wide-ranging legislation was pushed through and new and revised regulations were promulgated which, among other things, lowered capital requirements, raised the deposit insurance limit to \$100,000 from \$40,000 and created new “products” including NOW and Super NOW accounts. These financial “products” opened the way for the conversion of a staggering amount of time deposits to interest-bearing demand deposits. Unnoticed by the Fed, for decades the only regulator of the money supply, the money multiplier effect was thus brought into play for the first time ever against the aggregate of deposits at the nation’s savings and loans. More laws and rules were enacted which further expanded investment and lending, or “asset” powers, to help the savings and loan industry “grow” out of its problem. Regulatory Accounting Principles replaced Generally Accepted Accounting Principles, and these “RAP” principles caused an inflation of the amount of capital reported by savings and loans and disguised the insolvency of the industry.¹⁴ Other dynamics intervened and added fuel to the fire: A timid Fed,¹⁵ deception on the part of savings and loan regulators, Congressional accommodations,¹⁶ and deliberate ignorance sealed the fate of the savings and loan industry.¹⁷

By the time Ed Gray became Chairman of the Federal Home Loan Bank Board in May of 1983 the damage was irreparable. Basically impotent in his new position, Gray became a tragic figure of sorts; reduced to unseemly hand wringing, giving “Chicken Little” speeches and making desperate pleas to Congress to throw good money

after bad. With misplaced devotion to the moribund Federal Savings and Loan Insurance Corporation, he solicited funds to recapitalize the savings and loans' deposit insurer. But it was too late, and many in the upper echelons of powers knew it, particularly when the Fed "blinked" and relaxed monetary policy in late 1984. The Fed's new policy "unleashed the greatest tidal wave of credit creation in our economy in a short period of time that we have ever seen."¹⁸ The savings and loans lacked the institutional memory to cope with such a market and, consequently, "credit standards broke down ... under the gale force of ... massive monetary liquidity."¹⁹ Some very powerful officials well understood the essential obsolescence of the thrift/bank distinction and adopted a "let it fail" philosophy.²⁰ Under these unique economic circumstances, in a system armed with a license to print deposits, and where "profit was privatized and loss socialized,"²¹ disaster became inevitable. The iniquitous partnership of the liberated monetary commons and the moral hazard of deposit insurance inexorably and remorselessly took its toll. The debacle is now history.²²

Lloyd warned that "[i]n an inclosed [sic] pasture, there is a point of saturation [by which we mean here a barrier depending on considerations of interest] beyond which no prudent man will add to his stock. In a common pasture also, there is in like manner a point of saturation. But the position of the point in the two cases is obviously different. Were a number of adjoining pastures, already fully stocked, to be at once thrown open, and converted into one vast common, the position of the point would immediately be

changed. The stock would be increased, and would be made to press much more forcibly against the means of subsistence.”²³ But no heed was paid to this truth, and the mistake was both practical and philosophical. Government failed to take heed of the characteristics and presuppositions of Americans, and it set the stage for unbridled acquisitiveness. Financial reforms became increasingly more liberal and it encouraged and energized men to act in ways inimical to the institutions of money and banking, property and the mutual benefit and security of society. Now, as each new post mortem is filed, which is only another set of symptoms rather than an integrated diagnosis,²⁴ the insight of Solzhenitsyn’s Professor Varsonifiev gradually soaks deeper into the public consciousness: “Who is conceited enough to imagine that he can actually devise ideal institutions? The only people who think that nothing significant was ever done before their own time, that their generation will be the first to achieve anything worthwhile, people who are convinced that anyone who doesn’t agree with them is a fool or a knave.”²⁵ With a sense of foreboding many are now convinced that government is incompetent.

Political scientists and political philosophers will no doubt hasten to point out that behavior cannot be characterized independently of intentions, and intentions cannot be characterized independently of the settings that make those intentions intelligible. They may agree with Alasdair MacIntyre that there “ought not to be two histories, one of political and moral action and one of political and moral theorizing, because there were

not two pasts, one populated only by actions, the other populated only by theories.”²⁶

Such views are not to be dismissed, so we submit the following hypothesis:

The savings and loan debacle began when deconstructive statutory and regulatory changes were imposed upon on the savings and loan industry by zealous innovators. The innovations were initially driven by the perceived need to make the industry more competitive. The movement reached a critical pitch after Wall Street’s introduction of cash management and money-market funds in the late-1970s and the onslaught of brokered deposits.²⁷ Added impetus came from an overlapping combination of the left’s innovation ideology and tendencies to broaden access to power and status (dominant in the Carter administration) and the right’s commitment to free markets, individualism and anti-statism (dominant in the Reagan administration).

After the debacle became apparent and reached crisis proportions, the realization set in that the blame is trans-ideological and trans-partisan. New Right political and bureaucratic operatives then subsumed the energies of the innovators, “circled the wagons” and fabricated a red herring to pass the buck and serve as historical cover for the real cause of the problem. This alliance operated in all three branches of government and included a subjugated press as an agent.²⁸ American individualism and entrepreneurialism was condemned as unbridled private-sector greed,²⁹ which was personified in the likes of Michael Milken, Charles Keating, David Paul, Jess Rodrigues, Don Dixon, Tom Gaubert, E. Frank Neisch, E. Michael Sheheen and others. Tactics such

as massive intra-agency criminal referrals,³⁰ and sensationalistic, payment-not-really-expected, multi-million dollar restitution orders³¹ were utilized. The public sector became deliberately ignorant of the fact that the American democratic tradition is deeply charged with a strong emphasis on achievement, personal success and self-orientation. But the ends-oriented entrepreneurs and their institutions, who dared to reach for the American dream when their ambitions were elevated by the liberalized regulatory landscape offered to them, were vilified and expurgated by means-oriented regulators and prosecutors who, in order to cope with the problem, stage-managed a studied theater of power: conspicuous menace from the judge's bench.

Government's efforts to bury the truth of one of its most spectacular blunders ever became extremist, which was revealed in frequent violations of democratic and judicial norms.³² The purpose was to ensure that government's characterization of the problem, *viz.*, the result of countless negligent, dishonest and criminal excesses of the private sector, was perceived to be substantiated, despite the fact that reliable data to support this portrayal was meager. Ignoring its power and its duty to counteract these strains, the press assisted in promulgating the pretext offered by its public sector client.³³ The result was that competition from rival answers was suppressed and crowded out of the realm of public opinion. The press satisfied its illegitimate duty to create public docility toward government administration.

On a philosophical level the reforms involved a not generally recognized principle

of morality, namely, that the morality of an act is a function of the situation and the state of the system at the time and in which it is performed.³⁴ Using a commons as a cesspool does not harm the public under frontier conditions because there is no public. The same behavior in a metropolis is unbearable. One hundred and fifty years ago a plainsman could kill a bison, cut out only its tongue for his dinner, and discard the rest of the carcass. He was not in any important sense being wasteful. But today with only a few thousand bison left his act would be nearly criminal, certainly immoral.

Morality prohibitions have in the past usually been couched in “Thou shalt not” formulas. But, because such traditional moral directives make no allowances for particular circumstances, they are poorly suited to govern the modern complex, crowded, quickly changing world. Our epicyclic solution has been to augment statutory law – our legal equivalent of broad moral directives – with administrative regulations and guidelines and to vest the authority to interpret and enforce them in administrators. Since it is impossible to spell out all the conditions under which it is safe to burn trash in the back yard or to run an automobile without smog-control, we have delegated the power of making decisions on the details to bureaus and bureaucrats.³⁵ The result is administrative law which is rightfully feared for an ancient reason, namely, *quis custodiet ipsos custodies?* (Who shall watch the watchers themselves?) John Adams said that we must have “a government of law and not of men,” but bureau administrators, trying to evaluate the morality of acts in the total system, are singularly susceptible to corruption, producing

a government of men, not of laws.

We limit possibilities unnecessarily if we suppose that the notion of *quis custodiet* denies us the use of administrative law. We should rather retain the phrase as a perpetual reminder of the fateful dangers we cannot avoid. The great challenge facing us now is to invent the necessary feedbacks that are needed to keep the watchers honest. We must find ways to legitimate the needed authority of both the watchers and the corrective feedbacks.

It is a mistake to think that society can convince the individual exploiting a commons to restrain himself for the general good. To appeal to conscience is nothing but trying to browbeat a free man in a commons into acting against his own interest. Responsibility is a verbal counterfeit for a substantial *quid pro quo*. It is an attempt to get something for nothing.³⁶ The only social arrangements that produce responsibility are those that create coercion of some sort. Consider bank robbing. The man who robs money from a bank acts as if the bank were a commons. How do we prevent such action? Certainly not by appealing to his sense of responsibility. We arrest him and punish him, and that we infringe on the freedom of would-be robbers we neither deny nor regret.

The immorality of bank-robbing is easy to understand, because we accept its complete prohibition. We are willing to say “thou shall not rob banks,” without exception. But behavior can also be controlled by another sort of coercion. For example, taxing is an effective coercive device. And to keep downtown shoppers temperate in their

use of parking spaces we introduce limited-term parking with stiff fines for anyone who overstays. We do not actually forbid a citizen to park for as long as he wishes, we merely make it expensive for him to do so. Carefully biased options, not prohibitions, are what we offer him. And only this kind of mutual coercion is appropriate, *i.e.*, coercion mutually agreed upon by a majority of the persons affected. To say that we mutually agree to coercion is not to say that we are to enjoy it. Who enjoys taxes? We all grumble about them, but we recognize that we all have to be taxed. Voluntary taxes would favor the unscrupulous and those without a conscience. We have to have compulsory taxes as well as other coercive devices to escape the horror of the commons.

Stanley Parry theorized that ideological progressivism, *i.e.*, proposals for instituting new programs, and reaction, *i.e.*, proposals for re-instituting previously abandoned programs, are the two basic responses to crises.³⁷ But these two responses do not rule out the *status quo* as an alternative. As A. M. Rosenthal correctly observed, bureaucrats in particular have repeatedly shown a “real passion ... for the *status quo* Problem is, once they have been proven wrong ... bureaucrats stay on the job, tirelessly trying to justify the error by perpetuating it. Former bureaucrats often have a way of using platforms in academia, print, TV, international business, think tanks ... [and] lobbies to do the same thing. Traditional American bureaucratic support of the *status quo* sometimes comes from political infantilism – paralyzing fear of the unknown. It can be passed on to presidents like some psychic disease.”³⁸

“The *status quo* forces in this country are formidable, and are powerfully organized to thwart change, no matter who governs,” is the recent verdict of syndicated columnist David Broder.³⁹ His comment was inspired by Jonathan Rausch’s essay on what he called “demosclerosis,” *i.e.*, government’s now ingrained and growing inability to adapt.⁴⁰ Rausch explained that one of the causes of demosclerosis is the proliferation of special interest groups which “make their members better off by seeking subsidies, tax breaks, monopolies, favorable regulations and so on.” These groups slow the implementation of new ideas by clinging to the *status quo*. “They distort the economy, and so reduce its efficiency, by locking out competition and locking in subsidies.”⁴¹ Rausch’s sobering assessment of government has broad implications,⁴² and he is not the only one who has taken notice of government’s problems. The conditions which led him to coin the term “demosclerosis” were observed by others before he wrote his article and, judging from recent publications, they seem to be persistent and perhaps worsening.⁴³

Bureaucrats, entrenched interest groups, and other worshipers of the *status quo* often argue that effective reform is possible only with unanimous, *i.e.*, apparently perfect, agreement. But that idea this is an absurdity. It presupposes that the choice is between perfect reform and no action at all. Clearly we cannot wait for the perfect proposal, because we would never do anything.

Every new enclosure of the commons involves infringement of personal liberty. Infringements made in the past are accepted because there is no one left to complain

about them. Newly proposed infringements, however, are vigorously opposed with cries of “rights” and “freedoms.” But what does “freedom” really mean? When mankind agreed to pass laws against fraud, theft and robbery, mankind became more free, not less. Individuals locked into the logic of the commons are free to bring universal ruin when freed to do so. But once the watched and the watchers see the necessity of mutual coercion, they become more free. Whether the emphasis is on the free marketplace or reliance on government to regulate the distribution of society’s resources, there will be “winners” and “losers.” But there will be far more winners when we affirm that an alternative to the commons need not be perfect to be preferable. The alternative of the commons is too horrifying to contemplate.

Someone – it may have been Hegel – once said, “freedom is the recognition of necessity.” We must learn to recognize necessity in order to avoid creating a tragedy on the commons, but there is little evidence that we are developing this faculty. In the early years of the 21st century teams of global development, world trade and free-trade negotiators, indifferent to the causes of disparities in wages, standards of living and business costs, are engaged in long-running discussions aimed at lowering trade barriers. Articles and essays extolling the virtues of an emerging “global economy” abound. International compacts such as the North American Free Trade Agreement⁴⁴ established trading blocs opening the economies of industrialized nations to Third World countries. The European Community doles out billions to poorer member nations to bring them up

to standards. Corporations continue to formulate and implement plans which export more and more jobs from the First World to the Third World, thereby adding to the tens of thousands already lost across those borders. Cross-border capital investment is up a staggering amount since the early 1980s. Hundreds of thousands of Third World immigrants continue to pour into the First World, and even more clamor to come.⁴⁵

“[A]mbition for a better life is now universal. We earn our livelihood in America today in peaceful competition with people all across the Earth.”⁴⁶ And because this “globalization” process is being driven to a large extent by private enterprise without treaties or legislation it has, according to Rubens Ricupero, Secretary General of the U.N. Conference on Trade and Development, “contributed to the increasing vulnerability and instability of large parts of the world economy.”⁴⁷

It seemed so logical and permanent when, in the early 1970s, we adopted replacement-level fertility as a social policy. We thought the days of having to build more streets, sewers, schools, etc. were over; that we could concentrate on improving existing institutions. We were wrong. Newly revised government estimates now project that 200,000 illegal immigrants will arrive, without decisive check or credible monitor, each year in the United States for the next 60 years.⁴⁸ All this activity proceeds in spite of the fact that public officials and private sector leaders are aware that the industrialized world cannot maintain all those demanding maintenance. As if we’ve found some new addition, we continue to pursue policies and practices that admit into competition for the

wages and resources of the First World all those who can possibly compete.⁴⁹ We have thus created a global economic commons wherein the share of each competitor will be determined by the number of such admissions, rather than by a division of shares into a definite magnitude sufficient for the comfortable maintenance of a family.

We may be in more trouble than the pioneers ever were. When night fell or adversity threatened, they bolted the gates of the stockade. But things were less complicated then. Good judgment was often only dry powder. Now we struggle with an inscrutable myriad of interrelated and interdependent cultures, systems and economic interests.⁵⁰ But complexity and the fact that much has yet to unfold does not excuse us from evaluative judgment.

Our conclusion is that because we have survived some very toxic doses of social, political and judicial decay, we have made available to future leaders and generations a reservoir of valuable analogues which will help them judge when fences and guardrails should and should not be erected or dismantled. We hope they will be able to recognize this valuable cache, that they will weigh these analogues astutely *vis-à-vis* future problems for likenesses and differences, and that their judgment will be thereby enhanced. Only the future will tell. Frankly, we are less than optimistic. We expect that the reservoir will continue to fill and very little will be drawn from it. As the French would say, "*Plus ça change, c'est plus la même chose.*"

EPILOGUE

Although endnotes were added as late as November 2006 to note the continuing nature of certain issues and conditions this paper was completed in 1997. Since then, we have remained concerned that our readers would judge our conclusion as weak, since it is not a bold statement and it leaves the reader wondering whether something like the savings and loan crisis could be repeated. It was all we could do, however, since the future is unknowable and human nature can change or not. Be that as it may, from our perspective as of the time we completed this paper we submit that a single word answers the question whether things would remain the same. The word was unknown to us even as late as the addition of the latest endnotes to this paper. The word is “subprime.”⁵¹

1. Philip Bagus points out that Hardin was not the first to explicate the concept of the *tragedy of the commons*. See “The Commons and the Tragedy of Banking,” Ludwig von Mises Institute, posted November 12, 2003, available at <http://www.mises.org/story/1373>. Bagus notes that Ludwig von Mises described the concept in 1940 “in relation to external costs.” See *Nationalökonomie: Theorie des Handelns und des Wirtschaftens*, § VI, Ch. 10, Pt. IV, Editions Union, Geneva 1940, 2nd ed. of Philosophia Verlag, Munich (1980), pp. 599–605. Bagus also reminds us that in *Human Action* (1949) von Mises wrote:

If land is not owned by anybody, although legal formalism may call it public property, it is utilized without any regard to the disadvantages resulting. Those who are in a position to appropriate to themselves the returns — lumber and game of the forests, fish of the water areas, and mineral deposits of the subsoil — do not bother about the later effects of their mode of exploitation. For them the erosion of the soil, the depletion of the exhaustible resources and other impairments of the future utilization are external costs not entering into their calculation of input and output. They cut down the trees without any regard for fresh shoots or reforestation. In hunting and fishing they do not shrink from methods preventing the repopulation of the hunting and fishing grounds.

Bagus differentiates Hardin’s *tragedy of the commons*. He says Hardin’s version “has a more recent and direct connection to Austrian economics.” Bagus also points us to Huerta de Soto’s work on the concept of the *tragedy of the commons* in the context of an analysis of fractional reserve banking which, he says, “explains why fractional reserve banks, by their very nature, are always tempted to expand credit.” See *Huerta de Soto, Dinero, Crédito Bancario y Ciclos Económicos*, 2nd ed. Madrid: Unión Editorial (2002), pp. 518-21.

2. J. B. Weisner and H. F. York, *Scientific American*, Vol. 211, No. 4 (1964), p. 27.

3. Adam Smith, *The Wealth of Nations* (Modern Library, New York, 1973), p. 423.

4. W. F. Lloyd, *Lectures on Population, Value, Poor-Laws and Rent* (A. M. Kelley, New York, 1968), Lecture I, p. 30 ff. Originally published in *Two Lectures on the Checks to Population* (S. Collingwood, Printer to the University, University of Oxford, Oxford, England, 1832); reprinted in *Lectures on Population, Value, Poor-Laws and Rent* (Roake and Varty, London, 1837); reprinted in part in *Population, Evolution, and Birth Control*, G. Hardin, Ed. (Freeman, San Francisco, 1938), p. 37.

5. A. N. Whitehead, *Science and the Modern World* (Cambridge University Press, Cambridge, England, 1945), p. 13.

6. Explicated well by Charles Mann in another context. See “How Many Is Too Many,” *The Atlantic Monthly*, Vol. 271, No. 2, February, 1993, p. 47.

7. R. Devine, "The Cheatgrass Problem," *The Atlantic Monthly*, Vol. 271, No. 5, May, 1993, p. 40; R. Berke, "Clinton Backs Off From Policy Shift on Federal Lands," *The New York Times*, Wednesday, March 31, 1993. p. A1; J. Nesbitt, "Battle Rages for the Soul of the 'Real West': Old Methods Clash with New Values," *The Times-Picayune*, Sunday, May 2, 1993, p. A-12.
8. K. Brower, "The Destruction of Dolphins," *The Atlantic Monthly*, Vol. 263, No. 1, July, 1989, p. 35; Kenneth R. Weiss, "Devastating Results of Overfishing Reported: Waters Once Teamed with Marine Life," *The Times-Picayune*, Friday, July 27, 2001, p. A-8 (reprinted from *The Los Angeles Times*). See also E. Stokstad, "Global Loss of Biodiversity Harming Ocean Bounty," *Science*, Vol. 314, No. 5800, November 3, 2006, p. 745. This study was widely reported in over 600 newspapers and internet news web sites worldwide. See, e.g., "World's Fish Supply Running Out, Researchers Warn," *Washington Post*, Friday, November 3, 2006, p. A-1, reporting that the "14 researchers from Canada, Panama, Sweden, Britain and the United States spent four years analyzing fish populations, catch records and ocean ecosystems to reach their conclusions." The Northern Territory Seafood Council supports the report's conclusions. See "Fish Stock Collapse Prediction Correct, Says Seafood Council," *ABC NEWS ONLINE*, November 4, 2006, available at <http://www.abc.net.au/news/newsitems/200611/s1781138.htm>. But Seafish, the Scottish Fishermen's Federation, called the report "superficial." See "Vanishing Seafood Study Dismissed," *Guardian United*, November 3, 2006, available at <http://politics.guardian.co.uk/homeaffairs/story/0,,1938938,00.html>. Other scientists have questioned the study as "just mind-boggling stupid." See "Will Seafood Nets Be Empty? Grim Outlook Draws Skeptics," *The Seattle Times*, November 3, 2006, available at http://seattletimes.nwsourc.com/html/localnews/2003340489_seafood03m.html. Boris Worm, a marine biologist and lead author of the study's peer review, is optimistic that the "trend could be turned around with more marine conservation zones." "We have a whole portfolio of options. What it takes is political will," Worm said. *Id.* If, however, Stokstad's analysis of our marine systems is correct, the world will run out of seafood by 2048.
9. Fmr. Senator Jake Garn (R-Utah), Statement to the National Commission on Financial Institution Reform, Recovery and Enforcement [hereinafter the "Commission"] (January 27, 1993), p. 2, quoting the Report of the Commission on Money and Credit, Ch. 6 (1961).
10. J. Garn, *op. cit.*, pp. 1-8.
11. J. Garn, *op. cit.*, pp. 1-8.
12. Editorial, "The Office of the President," *The St. Croix Review*, Vol. XXV, No. 5, October 1992, p. 2; E. Alterman interview with Bill Moyers, "Moyers on Washington," *The Washington Post Magazine*, September 1, 1991, p. 30; J. A. Rodrigues, *Power Above the Law* (Presse Forward, Inc., 1990), p. 87; G. C. Hill, "A Never Ending Story: An Introduction to the S & L Symposium," *Stanford Law & Policy Review*, Vol. 2, No. 1, Spring 1990, pp. 21-24; J. A. Grundfest, "Lobbying into Limbo: The Political Ecology of the Savings and Loan Crisis," *op. cit.*, pp. 25-36; C. Keating, "Quest for Truth: A Search for Sanity in a \$500 Billion Tragedy," *op. cit.*, pp. 147-158; Edwin J. Gray, Fmr. Chairman of the Federal Home Loan Bank Board (May,

1983 through June, 1987), Testimony before the Commission (January 15, 1993), pp. 204-207, 222; Bert Ely, financial institutions consultant, and Joseph Hutnyan, financial writer, Testimony before the Commission (January 14, 1993), (transcript available from Neal R. Gross, Washington, D.C., transcriber); E. Gray, Testimony at Hearings Before the Senate Ethics Committee, 101st Cong., 2nd Sess. (November 27-29, 1990); William K. Black, Fmr. Deputy Director of the Federal Savings and Loan Insurance Corporation, Testimony at Hearings Before the Senate Ethics Committee, 101st Cong., 2nd Sess. (December 5-6, 1990); Edwin J. Gray, Address at the Conference of the Committee on Larger Institutions, U. S. League of Savings, Palm Springs, California (May 29, 1985).

13. Donald T. Regan, Fmr. Secretary of the Treasury, Testimony before the Commission (February 17, 1993), p. 63 ff.

14. Karen Shaw, consultant; George Gould, Fmr. Under Secretary of the Treasury; Joseph Hutnyan, financial writer; Bert Ely, financial institutions consultant; and John Hill, Testimony before the Commission (January 14, 1993).

15. On January 14, 1993, the Commission began hearings. Its members questioned some of the “key participants about how the industry, with the government’s help, went so horribly off track in the 1980s.” See S. Schmidt, “4 Years After S&L Collapse, A Panel Starts to Ask Why,” *The Washington Post*, Thursday, January 14, 1993, p. D10. On January 15, 1993, Paul Volcker, former Federal Reserve Board chairman, testified before the Commission. He said he could have warned more forcefully about problems in the S&L industry but was worried at the time about panicking depositors. See DIGEST, Business Section, *The Washington Post*, Saturday, January 16, 1993, p. C1.

16. The Commission issued a subpoena ordering former House Banking Committee chairman Fernand St. Germain (D-R.I.) to testify January 30, 1993. During his appearance before the Commission, Mr. St. Germain said, “Who’s responsible? Everybody. Everyone.” indicating the courts, Wall Street, Congress and the Carter and Reagan administrations. In particular he said, “regulators were not forthcoming with Congress” and that he was never told of the real condition of the industry. Confessing that he served as a rubber stamp for the industry, he told the Commission that former Federal Home Loan Bank Board chairman Richard T. Pratt wrote much of the Garn-St. Germain Act. He also testified that increasing the deposit insurance to \$100,000 from \$40,000 was former California Democrat Senator Alan Cranston’s idea. Mr. Cranston, one of the “Keating Five,” responded, “It’s not true. I was not the prime mover. His memory is playing tricks on him.” Mr. Pratt, who also testified on January 29, 1993, said that the regulators knew the industry had been insolvent since 1979. See S. Schmidt, “Ex-Lawmaker Blames Others for S & L Crisis,” *The Washington Post*, Saturday, January 30, 1993, p. C1.); Elliot Levitas, Commissioner, Comment during the Commission interview with Jim Wright (February 10, 1993), p. 46.

17. In a paper prepared for presentation at the Annual Conference of the Western Economic Association, June 30-July 4, 1985 entitled “Insolvency and Risk-Taking in the Thrift Industry:

Implications for the Future” (originally presented in an earlier version at a Financial Forum held at the University of California, Riverside, on March 1, 1985) James R. Barth, E. Daniel Brumbaugh, Jr., Daniel Sauerhofs and George K. Wang, offered the following observation:

Some insolvent institutions taking greater risks may tend to grow, and in order to grow will offer higher interest rates on liabilities. The most aggressively growing insolvent depository institutions may then determine the level of interest rates paid, and assuming that the supply curve of funds is upward sloping, interest rates on insured deposits may rise to the level necessary to sustain the institution's desired rate of growth. Competing solvent institutions may then react to a shrinking market share of deposits. If the competitors wish to maintain their market share, they will meet the interest rate paid by the insolvent institutions. In order to maintain expected profitability, both the insolvent and solvent institutions will select assets with greater expected return and, simultaneously, greater risk. The ceilings on the level of risk taken by the institutions will be set by insolvent institutions and that risk level will be governed by the risk-return preference of the insolvent institution's perception of how much risk can be taken before the insurer will close an institution.

This paper discusses the development of federal deposit insurance and regulation of depository institutions. The paper discusses causes of the financial difficulties faced by thrift institutions in the mid-1980s and the policy responses to those problems. It examines the effect of the recent 511 thrift failures on the risk-taking behavior of institutions and the Bank Board's policy responses to risk-taking. The paper suggests possible responses to the large and growing number of insolvent institutions that have an economic incentive to pursue extremely risky portfolio opportunities. As a practical matter, publication of this paper served notice on Congress of deep trouble in the thrift industry and the imminent consequences of the moral hazard of deposit insurance. In October of 1985, eight months after the paper was first presented, Jim Wright (D-Texas), Speaker of the U. S. House of Representatives, canceled committee hearings on the problem shortly after the hearings began. He later resigned.

See also “Thrift Industry Problems: Potential Demands on the FSLIC Insurance Fund,” United States General Accounting Office Briefing Report to the Honorable Stan Parris, House of Representatives, *passim* (February 12, 1986); E. Gray, Testimony before the Commission (January 15, 1993), pp. 290-292; Senator Donald W. Riegel, Jr. (D-Mich.), Statement to the Commission (January 28, 1993), p. 32; Congressman Henry B. Gonzales (D-Texas), Statement to the Commission (January 29, 1993), p. 4; John W. Hill, Associate Professor of Accounting, Graduate Sch. of Business, Indiana University, Statement to the Commission (undated), pp. 1-4.

The authors obtained this paper on or about August 8, 1985 from Senator J. Bennett Johnston (D-Louisiana). It was written by three FHLBB employees and a Visiting Scholar from the Department of Economics of the George Washington University, who acknowledged that helpful comments were received from, among others, Robert Litan, who served on the Commission.

This paper was “disclosed during a Senate Banking Committee hearing July 25, 1985.” See letter from Senator Johnston dated August 6, 1985, private collection of Garrett Hardin and Edmond G. Miranne, Jr.

18. David Stockman, Fmr. Director of the Office of Management and Budget, Interview with the Commission (February 4, 1993), p. 50 ff.

19. D. Stockman, *op. cit.*, p. 51 ff.

20. D. Regan, *op. cit.*, p. 81.

21. Representative James A. Leach (R-Iowa), Statement to the Commission (January 28, 1993), pp. 1-2; Accord, Michael Raoul-Duval, Commissioner, Statement during testimony of E. Gray before the Commission (January 15, 1993), p. 254.

22. The Federal Deposit Insurance Corporation has established a web page devoted to the history of the savings and loan crisis, which includes a time-line of events beginning in 1966. This “chrono-bibliography” is available at <http://www.fdic.gov/bank/historical/s&l/>.

22. W. F. Lloyd, *op. cit.*, pp. 31-32.

24. NBC Sunday Today: It Happened on Main Street: The Fall of the American S & L (NBC television broadcast, Sunday, September 13, 1992); H. Kurtz, “Asleep at the Wheel: How the Press Bungled the S & L Story,” *The Washington Post Magazine*, Sunday, November 29, 1992, p. 10; W. Niskanen, “Heads I Win, Tails You Lose,” *National Review*, Vol. XLIV, No. 17, August 31, 1992, p. 45; J. R. Adams, *The Big Fix: Inside the S & L Scandal* (Wiley, New York, 1990); S. Pizzo, *Inside Job: The Looting of America’s Savings and Loans* (McGraw-Hill, New York, 1989).

25. A. Solzhenitsyn, *August 1914*, Michael Glenny Tr. (Farrar, Straus and Giroux, New York, 1972), p. 409.

26. A. MacIntyre, *After Virtue: A Study in Moral Theory*, (University of Notre Dame Press, Notre Dame, Indiana, 1984), p. 61.

27. In his testimony before the Commission on January 15, 1993, Mr. Gray testified that Fmr. Treasury Secretary Donald L. Regan was the “father of brokered funds when he was at Merrill Lynch.” *Op. cit.*, p. 217. Secretary Regan denied it. *Op. cit.* p. 57.

28. H. Kurtz, *op. cit.*, p. 10; “Above all, the moderators have lost their authority. The gravitas once exuded by old-time anchors like Howard K. Smith and Edwin Newman has largely dissipated in a miasma of round-the-clock, round-the-dial, off-the-cuff punditry. Voters now view TV journalists not as their thoughtful, disinterested proxies ... but as just another crop of missionaries from inside the Beltway.” See “Presidential Debates: A Modest Proposal,” *TomPaine.common sense*, originally published at <http://tompaine.com/opinion/2000/09/08/>

[index.html](#), Sept. 8, 2000

29. House Committee on Government Operations, Fifty-Seventh Report, Federal Response to Criminal Misconduct and Insider abuse in the Nation's Financial Institutions, H. R. Doc. 1137, 98th Cong., 2d Sess., *passim* (October 4, 1984); "Who's Killing the Thrifts?: Fast-Buck Entrepreneurs, Wall Street Firms and the Government All Share the Blame," *Newsweek*, November 10, 1986, p. 51.
30. S. Bartlett, "Savings Fraud Losses Seen as Lost for Good," *The New York Times*, Friday, February 10, 1989, p. 29; K. Bode, "Justice in Disarray," CNN News, (television broadcast, April 12, 1993) (two-thirds of these cases have been dropped); W. Black, Unsworn comment to commission during testimony of E. Gray (January 15, 1993) (typifies attitude of regulators); James Wright, Fmr. Speaker of the U. S. House of Representatives (D-Texas), Interview with the Commission (February 10, 1993), pp 9, 16, 32-40 (commenting on attitudes of regulators).
31. R. Keil, "Scores of S & L Defendants Haven't Paid Fines," *The Montgomery Advertiser*, Thursday, February 25, 1993, pp. 1A and 7A; K. Bode, *op. cit.* (95% of these fines remain uncollected).
32. K. Bode, *op. cit.*, *passim*; J. Hill, *op. cit.*, pp. 6 ff; J. McGee, "The Appearance of Justice," (A Six Part Series), *The Washington Post*, Sunday, January 10, 1993 through Friday January 15, 1993, *passim*; See generally S. Garment, *Scandal: The Culture of Mistrust in American Politics*, (Times Books/Random House, 1991), *passim*, and B. Ginsberg and M. Shefter, *Politics by Other Means: The Declining Importance of Elections in America*, (Basic Books, 1990), *passim*.
33. H. Kurtz, *op. cit.*, p. 10; E. Levitas, Comments during Commission interview with J. Wright (February 10, 1993), pp. 48-49; J. Schell, "The Uncertain Leviathan," *The Atlantic Monthly*, Vol. 278, No. 2, August, 1996, p. 70.
34. J. Fletcher, *Situation Ethics*, (Westminister, Philadelphia, 1966), *passim*.
35. For insight into the bureaucrat *qua* "character" we owe a great debt to a brilliant analysis by Alasdair MacIntyre. *Op. cit.*, Chs. 3 and 6.
36. The long-term disadvantage of an appeal to conscience should be enough to condemn it, but it has serious short-term disadvantages as well. If we ask a man who is exploiting a commons to desist "in the name of conscience," what are we saying to him, what does he hear – not only at the moment but also in the wee small hours of the night when, half asleep, he remembers not merely the words we used but also the nonverbal communication cues we gave him unawares? Sooner or later, consciously or subconsciously, he senses that he has received two communications, and that they are contradictory: The first intended communication is, "If you don't do as we ask, we will openly condemn you for not acting like a responsible citizen." The second, unintended communication is, "If you do behave as we ask, we will secretly condemn you as a simpleton who can be shamed into standing aside while the rest of us exploit the commons." Thus, every man then is caught in what Bateson has called a "double bind." Bateson

and has made a plausible case for viewing the double bind as an important causative factor in the genesis of schizophrenia. See G. Bateson, D. D. Jackson, J. Haley, J. Weakland, *Behavioral Science* 1, 251 (1956). The double bind may not always be so damaging, but it always endangers the mental health of anyone to whom it is applied. "A bad conscience," said Nietzsche, "is a kind of illness."

37. S. Parry, "The Restoration of Tradition," *Modern Age*, Vol. V, Spring 1961, pp. 125-138. Parry also describes two analyzed partial responses: economic individualism and spiritual individualism and a fifth response he calls the prophetic response. The rhetoric of Ross Perot and Admiral Stockdale in the presidential election campaign of 1992 represents an example of the response of the economic and spiritual individualist respectively.

38. A. M. Rosenthal, "The Betrayal," *The Times-Picayune*, New Orleans, Wednesday, April 3, 1991, p. B-7.

39. D. Broder, "Is the Government Afflicted with 'Demosclerosis'?", *The Times-Picayune*, New Orleans, Thursday, September 24, 1992, p. B-7.

40. J. Rauch, "Demosclerosis," *National Journal*, Vol. 24, No. 36, September 5, 1992, p. 1998.

41. *Ibid.*, p. 1999.

42. "What demosclerosis means for conservatives is that there is no significant hope of scraping away outmoded or unneeded or counterproductive liberal policies, because nothing old can be jettisoned. What it means for liberals is that there is no significant hope of using government as a progressive tool, because the method of trial and error has broken down." *Ibid.*, p. 2003.

43. In a front page article published in the *Wall Street Journal* in July of 1993, Peter Gumbel wrote, "Voters everywhere are fed up, polls show. They are annoyed by leaders who appear small at time when the problems facing them are so big. They are disgusted with finding indecision and corruption when they look for direction. And it is not just individual politicians who are the targets of public frustration ... the whole political system is being called into question." Gumbel quotes former French President Valery Giscard d'Estaing as saying, "We are witnessing a crisis of representative democracy." See P. Gumbel, "Global Pique: With Voters Fed Up, World Leaders See Their Popularity Sink; Corruption, Bleak Economies and the Cold War's End Are Blamed for Malaise; "Disquiet on Western Front," *The Wall Street Journal*, Vol. XCII, No. 2, July 2, 1993, front page. In 2000, Alan Keyes wrote that we are approaching a moment "in which we will either act as a people to return to moral health, or we will acquiesce in the unraveling of the fabric of liberty. We are reaching a crisis of self-government which, if not effectively addressed, will mean the end of our very capacity as a people to enjoy the times of normal self-government." See Alan Keyes, "Leadership Through Our Moral Crisis," *WorldNetDaily*, January 29, 2000, available at http://www.worldnetdaily.com/bluesky_keys/20000129_xcake_leadership.shtml.

More recently, two books contend that American constitutional democracy is in deep trouble. See A. Wolfe, *Does Democracy Still Work*, (Yale University Press, 2006); and S. Levinson, *Our Undemocratic Constitution: Where the Constitution Goes Wrong (and How We the People Can Correct It)*, (Oxford University Press, 2006). Even federal judges have noticed the problem, and the nation's top law enforcement agency is preparing to respond. See "Ex-Bush Aid Safavian Gets 19-Month Prison Term," *The Washington-Post*, October 27, 2006; and "FBI Willing to Go Undercover in Congress If Necessary," *McClatchy Newspapers*, Washington Bureau, Sunday, November 5, 2006, available at <http://www.realcities.com/mld/krwashington/15937935.htm>.

44. K. Bradsher, "Trade Pact Signed in Three Capitals: But Accord Faces Uncertain Future," *The New York Times*, Saturday, December 19, 1992, p. C1.

45. E. Lerner, "Exodus: Migration Moves World Toward Crisis; Masses Flocking to Crowded Cities, U. N. Report Warns," *The Times-Picayune*, Wednesday, July 7, 1993, p. A-13; The Brokaw Report: Immigration: The Good, the Bad, the Illegal (NBC television broadcast, Sunday, March 28, 1993); P. Range and J. Pinneo, "Europe Faces Immigrant Tide," *National Geographic*, Vol. 183, No. 5, May, 1993, p. 94.

46. Inaugural address by President William Jefferson Clinton, Washington, D. C. (January 20, 1993).

47. P. McDowell (Associated Press writer), "Nations Ponder Globalization," *newsday.com*, Friday, February 11, 2000, available at <http://www.newsday.com/ap/rnmpfn1z.htm> .

48. R. Pear, "New Look at the U. S. in 2050: Bigger, Older and Less White," *The New York Times*, Friday, December 4, 1992, p. A1.

49. President Clinton dated the beginning of this movement in his address to Congress on the economy on February 15, 1993. "For two decades, we've moved steadily toward a global economy in which we must compete with people around the world ... ," he said.

50. C. Morris, "It's Not the Economy, Stupid," *The Atlantic Monthly*, Vol. 272, No. 1, July, 1993, p. 49.

51. Epilogue added July 2008.

ABOUT THE AUTHORS

The late Garrett James Hardin (1915-2003) was trained as an ecologist and microbiologist. He retired in 1978 as professor emeritus of human ecology at the University of California, Santa Barbara after more than 30 years on the UCSB faculty. He is the author of at least a dozen books about ecology, biology and ethics, but “The Tragedy of the Commons” was his most influential work. His books include *Nature and Man’s Fate* (1965) New American Library; *Promethean Ethics: Living With Death, Competition, and Triage* (1980) University of Washington Press; *Filters Against Folly: How to Survive Despite Economists, Ecologists, and the Merely Eloquent* (1985) Viking Penguin; and *Living Within Limits: Ecology, Economics, and Population Taboos* (1993) Oxford University Press. Hardin and his wife, Jane, were members of the Hemlock Society and felt strongly about choosing their own time to die. Shortly after their 62nd anniversary in September 2003 Hardin and his wife were found dead in an apparent suicide. He was 88 and she was 81.

Edmond G. Miranne, Jr., J.D. is a practicing lawyer and businessman who witnessed the progression of the savings and loan debacle as an insider in the 1970s. In February 1993, Professor Hardin granted Mr. Miranne permission to rewrite “The Tragedy of the Commons” and consented to be co-author.