

Libertarianism and State Regulation

The period 1905-1937 is sometimes called the *Lochner* era in American constitutional law, after the case of *Lochner v. New York*. The defining characteristic of the period is that the Supreme Court's decisions about economic regulation in effect use a libertarian philosophy. Government regulation of markets—including labor markets—is seen as intruding on basic constitutional liberties. To achieve a better understanding of libertarianism, then, we want to see how it operated in constitutional practice.

1. The *Lochner* Era

In 1905, *Lochner* came to the Supreme Court, asking that the Court overturn his conviction under a New York statute that prohibited employers from requiring or permitting bakers to work more than 60 hours a week, or more than 10 hours a day. The Court agreed. The law was, it said, an unconstitutional abridgment of *Lochner's* liberty of contract.

In the ensuing 32 years, the Court overturned more than 200 federal and state economic regulations, also as unconstitutional abridgments of *liberty of contract*.¹ The Court overturned minimum wage laws²; federal and state laws against "yellow dog contracts" (contracts requiring employees to pledge not to join a union as a condition of employment)³; price regulation⁴; and restraints limiting entry into an industry or type of work.⁵ In short, the Court endorses an economic philosophy of relatively unregulated markets.

The doctrine expressed in these decisions—sometimes called "economic due process"—has three main elements:

1. The Court interprets the 5th and 14th Amendments—which bar government from making laws that deprive "any person of life, liberty, or property without due process of law"—as requiring stringent protection for market liberties, in particular the liberty to "purchase and sell labor" (53).

2. These liberties are important, but not absolute, and can be regulated for a limited set of purposes, including the "safety, health, morals, and general welfare of the public." "Public morals" is on this list, so the Court does not endorse a libertarian constitutional philosophy. But on economic regulation, the Court is libertarian in its elevation of economic liberties to a position of basic constitutional importance.

3. Because the liberties are so important, the Court examines economic legislation to ensure that the means used by the legislature to further its legitimate purposes are well-designed to achieve those purposes—to see that there is no way to achieve the purpose that is less restrictive of market choices.

2. NY law may be a labor law, and what's wrong with that?

Using this line of analysis in *Lochner*, the Court considers two purposes that the New York statute might serve: as a "labor law" or a "health law."

Interpret it first as a labor law. This means that the purpose of the law is to regulate the terms of the labor contract (say, wages, hours, working conditions), rather than simply enforcing terms that the parties agree to. The idea behind a labor regulation might be that the state needs to police agreements, at least agreements in the labor market, to ensure that their terms are fair or non-exploitative, even if the parties have agreed to them.

In *Lochner* and related cases the Court says that labor laws do not serve legitimate purposes. And it offers two reasons.

The first reason is anti-paternalist. In *Lochner*, the Court says that regulating the terms of a labor agreement interferes with the “independence of judgment and action” (57) of the parties to the agreement. But those parties are “in no sense wards of the state.” The allegation is that labor laws impermissibly substitute the government’s judgment for the workers’ own judgment, and thus limit “the hours in which grown and intelligent men may labor to earn their living” (61).

Is labor market regulation paternalistic? A regulation is paternalistic when it is based on the claim to know better than the agent what the agent's interests are or how best to advance them. But labor laws often have a very different rationale. They are based on the idea that unequal wealth means unequal bargaining power and unequal bargaining power—not imprudence or sloth or shortsightedness—prevents workers from defending their own interests. The idea is that limits on a person’s bargaining power may force a person to accept an option he/she knows is very bad because the alternatives are all worse. Trying to ensure that people are not in such circumstances—and regulating agreements made when they are—is not being paternalistic. If I put a gun to Joe’s head and say “your money or you life,” and Joe says “take my money,” I can’t then complain that the state is being paternalistic if it forces me to return his money. Joe agreed, but circumstances forced him to accept an option that he knew to be very bad. And if I see you drowning in a lake, and I say “all your money or your life,” and you say “save me and you can have all my money,” the government is

not being paternalistic if it refuses to enforce the agreement—even if I did not push you into the lake. You were compelled by circumstances to accept an option that you knew to be very bad, and I was exploiting those circumstances.

In an 1898 case (*Holden v. Hardy*), the Court upheld eight-hour-day legislation for mining workers on precisely these grounds: “the proprietors of these establishments and their operatives,” the Court said, “do not stand upon an equality.” Workers, according to the Court, are “practically constrained” by their circumstances to “obey” the dictates of owners. Labor laws try to remedy the low wages or unsafe working conditions that may result from such unfair bargaining conditions. They are not paternalistic, but instead ensure that people are not compelled by circumstance to take on low-paying or dangerous work, rather than starve, or take on still lower-paying and more dangerous work.

So the Court’s reasoning in *Lochner* suggests a libertarian outlook, not because the Court objects to paternalism, but because of its presumption that paternalism underlies the concern about remedying unfair bargaining conditions.

Later, in *Coppage v. Kansas* (1915), the Court suggests a second objection to labor laws. A Kansas law outlawed “yellow dog” contracts. Such contracts—in which workers agreed not to organize a union as a condition of employment—were understood to both reflect and reinforce the bargaining disadvantage of workers: workers might be compelled by economic circumstance to sign away their right to organize, and once they signed away that right, they would remain relatively weak in future bargaining. In *Coppage*, the Court say that such laws are paternalistic. What is the problem?

The Court begins with the premise that the constitution strongly protects economic liberties. But once we accept that premise, they say, we must also accept substantial inequalities of income and wealth: "It is from the nature of things impossible to uphold freedom of contract and the right of private property without at the same time recognizing as legitimate those inequalities of fortune" that are "the necessary result" of choices individuals make in exercising of those rights (17). But inequalities of fortune produce inequalities of bargaining power and shape future labor contracts. And the legislature cannot legitimately do anything to prevent that shaping. Why?

Suppose wealthy owners negotiate with poorer workers and the result is a very low wage bargain. But that greater wealth is the "necessary result" of the previous exercise of economic liberty. Now it would be illegitimate for the state simply to take control of the property of the owners: to attack the inequality of fortune directly. But if seizure of the property is illegitimate, then it is also illegitimate to regulate the outcome of unequal bargains by setting minimum wages. Why? Because that regulation would deprive owners of *one of the benefits* that naturally flows from what they rightfully own: viz. the benefit of greater bargaining power. Setting minimum wages would be seeking to do "indirectly" (17)—by regulating outcomes—what is illegitimate to do directly through confiscation: override the property rights of individuals. You cannot seize control, and it is equally objectionable to regulate the flow of the benefits.

We have heard this before, about Nozick: the idea that a right to the full benefit is an essential component of ownership. Given that assumption, a minimum wage law is not paternalistic: it is *stealing*. Instead of taking control of

the resource, the regulation takes the right to benefit fully from it. But the right to benefit is just as much part of ownership as the right to control. And taking any right is a kind of stealing.

But how might the Court respond to the point I made earlier: that workers are in effect coerced into these agreements. Nozick offers a response: “Other people’s actions place limits on one’s available opportunities. Whether this makes one’s resulting action non-voluntary depends on whether those others had the right to act as they did” (262). Applying this to market exchanges between owners and workers, Nozick says: “Z is faced with working or starving; the choices and actions of all other persons do not add up to providing Z with some other option.... Does Z choose to work voluntarily? . . .” Yes, “if the other individuals acted voluntarily and within their rights. . . . *A person’s choice among differing degrees of unpalatable alternatives is not rendered nonvoluntary by the fact that others voluntarily chose and acted within their rights in a way that did not provide him with a more palatable alternative*” (263-64).

Thus the Court might have said that workers who accept low wages or poor working conditions are making voluntary decisions, not because they have good alternatives, but because the limits on their choices result from the rights of others, including the rights of others to maximal benefit.

In summary: Either labor laws are paternalistic and, as such, illegitimate infringements of economic liberty; or they are *not* paternalistic, but still unacceptable because they in effect involve stealing. I will come back to this line of argument later on.

3. NY law may be a health law, and what's wrong with that?

The second line of argument that the court considers is that the New York law is a public health law, aimed in particular at protecting the health of bakers.

Promoting health is a legitimate regulatory purpose. So the constitutional issue depends, then, on whether the legislative means—maximum hours regulation—has a "direct relation" to the legitimate end of protecting health.

The majority finds insufficient evidence of such a direct connection: they are not prepared to defer to the New York legislature's judgment that there is good enough evidence. Because the case for health effects is not so clear, the Court majority concludes that the New York statute is really a labor law in disguise (64): that the legislature enacted legislation designed to improve labor's bargaining power, but pretended to be enacting a health law, which would be more likely to get through the courts. But labor laws are illegitimate.

- Here, the reasoning is libertarian-inspired in its high degree of suspicion of restrictions enacted in the name of the general welfare. The Court does not reject such restrictions completely, but subjects them to high scrutiny.

4. What happens with *West Coast Hotel*?

In *West Coast Hotel v. Parrish* (1937), the Court upholds a Washington minimum wage law for women. In so doing, it overturns *Lochner*, affirms the permissibility and importance of labor market regulations, and rejects libertarianism as a constitutional philosophy.

- How does the Court arrive at this conclusion? In part, the Court focuses on the fact that the law applies to women, whose health is said to be important to

the "strength and vigor of the race" (394), and who are thought to be especially prone not to fully assert their rights (394-95).

- But the main point in the decision is about the permissibility of regulating agreements in which the parties do not "stand upon a footing of equality." Citing the language of *Holden v. Hardy*, the Court says: Such inequalities lead workers, as a result of their "fear of discharge[,] to conform to regulations which their judgment, fairly exercised, would pronounce to be detrimental to their health or strength. In other words, the proprietors lay down rules and the laborers are practically constrained to obey them" (394). To free people from such constraints, the state may permissibly enact labor laws. Notice the emphasis on freeing workers from "practical constraint" and on "*their judgment, fairly exercised*:" The Court denies that labor laws are paternalistic. The Court is firm on this matter: "The point that has been strongly stressed that adult employees should be deemed competent to make their own contracts was decisively met nearly forty years ago in *Holden v. Hardy*, where we pointed out the inequality in the footing of the parties."

- So the Court accepts that labor laws are not paternalistic. What about the (Nozickian) argument that correcting for the results of unequal bargaining power invades basic rights? How do they respond to the point that people are making decisions under constraints, but that they constraints result from choices that others had a right to make? Essentially by denying that individuals have a fundamental right to the maximal benefit.

In a passage that brings this point out with particular force, the Court says that a *failure* to impose a minimum wage law would "provide what is in effect a

subsidy for unconscionable employers" (399). Thus, when the state fails to establish a minimum wage, it is in effect subsidizing employers. The suggestion, put otherwise, is that a minimum wage does not take from owners; instead, the state redistributes from workers to owners when it enforces wage bargains struck within an unregulated labor market. How so?

Suppose bargaining between owners and workers were fair. Workers would not then accept a subminimum wage. But—and here we have the crucial idea—assume that people are only entitled to what they get in fair conditions, in which they are treated as equals, each with the powers to govern his/her conduct. Then, employees are entitled to a decent wage; the employer is not entitled to what he/she gets in a system with deep inequalities of bargaining power. So fixing a minimum wage does not take from owners in the name of equality, but ensures that owners do not steal from workers by illegitimately benefiting from an unfair bargain—by taking some of the wage that workers are entitled to. In his *Political Economy*, John Stuart Mill makes the essential point: owning something entitles you not to all the benefits you can get others to pay, but to whatever you can get for that thing “in a fair market.” So *West Coast Hotel* can be read as suggesting that an idea of fair bargaining conditions helps to define what people are entitled to. When laws are made to preserve fair conditions, they may help to ensure that people get what they have a right to—rather than, as Nozick urges, taking from them what they have a right to in the name of some high-minded value.

Endnotes

¹ *Coppage*, 14.

² *Adkins v. Children's Hospital*, 1923.

³ *Adair*, 1908, for federal laws; *Coppage*, 1915, for state laws.

⁴ *Williams v. Standard Oil*, 1929.

⁵ *Adams v. Tanner*, 1917.