The Chicago Roots of the Virginia School

by

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Introduction

The story of the Virginia school of political economy is in large part the story of how graduates of the University of Chicago developed a new paradigm in a new location. As noted by Mueller in 1986, the founders were still working and imparting their insights some thirty years from the time James M. Buchanan and Gordon Tullock were first associated. Now, over twenty years later, this continues to be the case. Insert A

In order to better understand the origins of the Virginia school, this paper raises, and seeks to answer, two questions. First, what are the distinctive characteristics of the Virginia school? Second, which of these characteristics have roots in the Chicago school? The latter question is most effectively addressed by focusing on James Buchanan.

This paper, as an exercise in intellectual history, goes beyond economics to include the sociology of knowledge and an account of the strong-willed personalities at Chicago who had a major influence on Buchanan, the principal founder of the Virginia school. To some extent this process was replicated at UCLA where Armen A. Alchian (post-doctoral fellow, 1968) and Harold Demsetz (Chicago 1963-71), worked on the economics of property rights. An appropriate metaphor to describe these emissaries at UCLA and Virginia is that of spores. Those involved were characterized by a deep and abiding respect for the intellectual tradition of economics at the University of Chicago and through their achievements reflected well on their alma mater.²

² A more remote connection to the Chicago school is the New Institutional School
What the Virginia school stands for

From its roots in the late 1950s at the Thomas Jefferson Center for the Study of Political Economy at the University of Virginia, the Virginia school of political economy has challenged the supremacy of mainstream neoclassical economics and interventionist presumptions by providing a new vision of the market order and an economic explanation of government failure. Those associated with the Virginia school have been critical of abstract mathematical modeling and high-powered econometrics which does not take into account the complex institutional arrangements of advanced economies. James Buchanan and Gordon Tullock founded the field of public choice and Ronald H. Coase was a founder of the new field of law and economics. In recognition of their contributions to economics, the Nobel Prize in Economic Science was awarded to Buchanan in 1986 and to Coase in 1991.

The leaders of the Virginia school were pioneers in the application of economic analysis to new topics like, bureaucracy, voting, constitutions, and law and economics. Buchanan’s early work on subjectivism was important in challenging the equilibrium focus of mainstream economists. Imbued with these subjectivist insights, Buchanan’s approach recognized that individuals act according to their own perception of costs and benefits. From this it follows that politicians are self-regarding and not necessarily promoters of the public interest broadly conceived. It is not surprising that this view of

associated with Douglass C. North, formerly at the University of Washington (Seattle) and latterly at Washington University at St. Louis, who employs the insights of Alchian and Demsetz on property rights. North was a student of Frank H. Knight’s brother Bruce
politicians, which became associated with the Virginia school gave rise to charges that the school embraced an ideological point of view and this perception was used to criticize the Virginia school then and now. While the founders of the Virginia school have been recognized as major innovators in the development of economic analysis, the acceptance of their work has been slow.

Mueller (1986) describes the Virginia school as focusing on how self-interested individuals interact with political institutions, and how we can step outside the system and design institutions with incentives that would better achieve our ends. The Virginia school recognizes that, as actors constrained by a system of rules, individuals play two roles. First, they are the beneficiaries of the existing institutions and therefore may oppose changing the rules. Second, the rules will only get changed if they are persuaded to do so. As an example of changing the rules, if super majorities replace simple majorities, special interest group politics will be less important and will limit undesirable outcomes.

Congleton (1999) points out that there is no textbook treatment of the Virginia School of Political Economy and he notes the several ways in which it differs from the mainstream. Underlying this approach is the idea that self-regarding individuals learn to use the rules of a political system in ways to achieve their ends. Therefore, only by reforming the rules can we alter the outcomes. The Virginia school recognizes that both good and bad economic policies are the outcomes of rational individuals making choices within specific institutional arrangements. Undesirable public policies such as protective

Knight who taught philosophy at Berkeley.
tariffs, costly and ineffective regulation, distortionary taxes, wasteful expenditures, and ill-conceived transfer programs are not accidents or mistakes waiting to be corrected, but the consequences of self-interested individuals choosing within particular institutional settings. In order to improve the outcomes of particular institutional arrangements, it is necessary to change the rules of the game, not simply to change the players or to give them better economic or policy advice. Institutional arrangements should then be compared to each other and relative to what is feasible. Finally, in so far as we consider people’s goals as given, the role of the Virginia school economist is to find the most efficacious means to achieve those goals. This approach therefore entails positive rather than normative prescriptions.

The essentials of the Virginia school may therefore be summarized in four points. First, the focus is on institutional arrangements as the reason for economic success or failure. Second, it recognizes that the only way to turn economic failure into success is by changing the institutional arrangements. Third, institutional arrangements are compared by reference to the outcomes they yield and with reference to their feasibility. Finally, the analyst is constrained to provide positive rather than normative recommendations.

*What the Chicago school of economics stands for*

We begin with a brief description of the Chicago school and its early faculty, and then focus on how some of these people influenced James M. Buchanan (b. 1919), Gordon Tullock (b. 1922), G. Warren Nutter (1923-1977), D. Rutledge Vining (1908-
The main characteristics of the Chicago school are twofold: the belief in the power of neoclassical price theory to explain observed economic behavior; and the belief in the efficacy of free markets to coordinate individual actions, and to allocate resources and distribute income. The ideas associated with the Chicago school include Adam Smith’s “invisible hand” postulate, opposition to government intervention in general and Keynesianism in particular, monetarism, and, as a later development, the economic analysis of the law. The “invisible hand” describes the phenomenon by which desirable outcomes are achieved without human design. It is used to explain some of the consequences of individual behavior and the evolution of institutions. The methodology associated with the Chicago school is that articulated by Milton Friedman in his renowned essay on positive economics (Friedman 1953), which has for decades been the dominant paradigm within the economics profession.

The founders of the Chicago school

Jacob Viner (at Chicago from 1919–1946)³, Frank H. Knight (1927-1952)⁴,

³ Jacob Viner (1892–1970) was born in Montreal, Canada. His education included McGill (A.B., 1914) and Harvard (Ph.D. 1922). He taught at the Univ. of Chicago (1919–46) and Princeton Univ. (1946–60). A specialist on the subject of international trade, Viner was an adviser on trade issues to the U.S. Treasury (1934–37)and the State Dept. (1943–52). Viner's work ranges from specialized writings on the theory of costs (1931), in which he laid out the envelope cost curve, to histories of economic thought (1937) and (1991).

⁴ Frank H. Knight (1885-1972) was born in McLean County, Illinois. He was educated at Milligan College (Tennessee) (B.A. 1911), University of Tennessee (B.A. and M.A. 1913), and Cornell University (Ph.D., 1916). His academic career included appointments
Henry C. Simons (1927-1946)⁵, and Aaron Director (1946-1965)⁶ are the more familiar names associated with the early years of the Chicago school. Among the founders of the Chicago school we may wish to distinguish those with a crusade or mission (Henry Simons’ crusade for what he believed was freedom and equality), those with a passion (Knight and Director were puzzlers), and those who sought to develop a system (Viner’s rigorous analytical framework). The approach and contributions of some of the founders and their successors fit more than one category.⁷ Simons’ mission was to advance political freedom and some measure of income equality which he thought could be obtained by a progressive tax structure and restraints on monopolies.⁸ He feared that government would expand dramatically during the 1930s and that this development that would be difficult, if not impossible, to reverse.

Both Knight and Simons emphasized the need to be critical in evaluating scientific work and that the age or high office of the researcher was of no consequence. Along with Director, their inquiry left no stone unturned and considered no doctrine at Cornell, Chicago, and Iowa.

⁵ Henry Calvert Simons (1899-1946) was born in Virden, Illinois. He was educated at the University of Michigan. He became an instructor and member of the faculty at the University of Iowa with subsequent appointment to Chicago in 1927 where he remained until his death.

⁶ Aaron Director (b. 1901) was born in Cherterisk, then in Russia, now in the Ukraine. His education included a PhB (Yale 1924) and graduate work at the University of Chicago (1930-1938).

⁷ In a similar vein, Milton Friedman and George J. Stigler had a mission to empirically test economic theories. As noted by Stigler, Friedman (and this was true of others), refused to “accommodate nice dichotomies, for he was a masterful peddler. He is above all, however, a great theoretician, the discoverer of powerful systematization of reality” (Stigler 19xx).

⁸ While Simons advocated steeply progressive income taxation, the Chicago school is associated with a proportional income tax or “flat tax.” See Blum and Kalven 1952,
sacrosanct no matter the identity of its originator. Chicago economists in general have been problem-oriented and advocates of the use of the simplest theoretical tools necessary to accomplish the task at hand. The causes determining a particular economic event are numerous and complex, but exponents of the Chicago school believe that economists should focus on the role of incentives in explaining human behavior. General equilibrium theorists, on the other hand, seek comprehensive and rigorous mathematical theories to show how the economic system can attain equilibrium under a set of rarefied assumptions.

Although the principal members of the Chicago school had similar leanings toward key elements of economic theory and policy, their personal approaches differed greatly and these differences affected the development and dissemination of their ideas, and hence the development of the Chicago school. The Chicago tradition of Viner, Knight, Simons, and Director was a crucial element in the various strains of the Virginia school constructed by Buchanan, Nutter, Tullock, Vining and Coase.

Later, during the 1950s and early 1960s, the Chicago school became widely known for the work of Milton Friedman in monetary economics and George J. Stigler in industrial organization and regulation. Although Buchanan and Nutter, as students at Chicago, knew these men, they were not influenced by them.

Hayek 1960, and Friedman 1962.

Milton Friedman (1912-2006) was born in New York City and was educated at the Rutgers (B.A. 1932), University of Chicago (M.A.1933), and Columbia University (Ph.D. 1946). He received the Nobel Prize in Economic Science in 1976.

George Joseph Stigler (1911-1991) was born in Seattle, Washington and was educated at the University of Washington (B.B.A. 1931), Northwestern University (M.B.A. 1932), and University of Chicago (Ph.D. 1938). He received the Nobel Prize in
Jacob Viner (1892-1970)

Viner was a systematizer who held fewer of the ideas associated with the Chicago school than did Knight. However, he may be credited with the emphasis of the Chicago school on microeconomics and his view of the economy as a complex system which could be modeled. He was both economic theorist and historian of economic thought, and he possessed a strong empirical orientation. Viner worked primarily on problems in international trade and related issues in monetary theory. Viner not only had an analytical mind that held many original ideas but he combined this with an expansive understanding of the humanities and social sciences (Spiegel 1997, 813).

Although Viner did consulting and other work for the federal government, he was foremost an academic. In 1950 Viner published The Customs Union Issue, which, by carefully distinguishing between trade creation and trade diversion, had a lasting influence on the policy debate in international trade. He jointly edited the Journal of Political Economy from 1929 to 1946. Much of this was with Knight, although they were known to differ on many issues. Viner and Knight shared an interest in the development of economic thought, were both devotees of neoclassical price theory, and resisted the theoretical innovations of the 1930s, including the theories of E. H. Chamberlin and Joan Robinson on imperfect competition and J. M. Keynes’ General Theory. Further they opposed the interventionist aspects of the New Deal and the full employment policies of the latter part of the New Deal. Like Knight later in his career, Viner sought to explore the relationship between religious and economic thought.
Viner’s emphasis on rigorous analysis is likely to have influenced Buchanan and other students. According to Buchanan, Viner was “the classically erudite scholar whose self-appointed task in life seemed to be that of destroying confidence in students,” and “he along with others were not the persons who encouraged students to believe that they too might eventually have ideas worthy of merit” (Breit and Spencer 1995, 174). Viner’s overbearing personal style explained his lack of acolytes (Buchanan 1995, 75) and his students never constituted a club but were dispersed in time and intellectual interest with little in common except their contact with Viner (Reder 1982). However, despite his teaching style, Viner established successful research programs, enlisted graduate students as participants in his work, and supervised far more doctoral dissertations than Knight.

Having said that, Viner’s influence on the Chicago school was not as great as that of Knight or Simons perhaps owing to their personal charisma and intellectual ability to convert students to their way of thinking. According to Coase, although Director took courses from Paul H. Douglas, Knight, Theodore Yntema and Henry Schultz, the course which changed his way of looking at the world was one from Viner on Marshallian economics (Coase 1997, 603). Buchanan and Knight’s other students wrote well, networked widely, and became effective advocates of the ideas they held. In that they

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11 Harry Johnson shared a similar opinion of Viner, but noted with admiration that J. M. Keynes’ tried (sometimes almost heroically), to find something of value in the views of graduate students (Skidelsky 2001). His desire to nurture independent thinking and development contrasts with Viner.

12 Apparently Viner’s rigid approach was manifest in other ways. Coase (1997, 601) noted that students were seated alphabetically and this seating arrangement resulted in Rose Director (sister of Aaron) getting better acquainted with Milton Friedman whom she
displayed rigorous analysis, Buchanan’s methodological views were, ironically, more similar to Viner’s approach than to Knight’s.

In a 1970 letter to Patinkin, Viner elaborated on his peculiar niche in the Chicago school. While Viner’s views on *laissez faire* and government intervention were consistent with the views held by members of the Chicago school, “on the whole he was a more pragmatic thinker and more aware of the need for qualification and consideration of circumstances of time and place” (Spiegel 1997, 814). For example, unlike Friedman and others at Chicago, Viner supported discretionary monetary management rather than a monetary rule (Spiegel 1997, 814).

Like Knight, Viner urged deficit spending during the Great Depression, and he went so far as to call the plea for an annual balanced budget a “mouldy fallacy” (Speigel 1997, 814). He was critical of Hayek’s libertarianism (Viner 1961, 232). However, in common with Knight, Viner denied that perfect competition was both a norm and normal. He further argued that monopoly was so prevalent in modern western economies that competition seemed to him “academic in the only pejorative sense of that adjective (Viner 1960, 66).” Like Knight and Simons, Viner was skeptical about received doctrine.

*Frank Hyneman Knight (1885-1972)*

Knight’s work focused on the conceptual underpinnings of neoclassical price theory, and his main concerns were to clarify and improve its logical structure. Buchanan described Knight’s qualities of mind as his willingness to question anything and anybody on any subject at any time. He categorically refused to accept anything as sacred and had later married.
a genuine openness to all ideas. Although Knight was sympathetic to the aspirations of those seeking to quantify economics, he was outspoken about his skepticism of their prospects for success. Buchanan describes Knight as having a basic conviction that most ideas peddled are nonsense or worse when examined critically (Buchanan 1995, 5). According to Buchanan, Knight (like Viner as noted above) recognized that the model of perfect competition is an idealization of reality, not a description (Buchanan 1968, 424). Buchanan argued that “lesser theorists who followed Knight overlooked this essential point and erroneously expected real world institutions to match up descriptively with the idealized model” (Buchanan 1968, 424). It was their overly simplistic comparisons of theory and observed reality that are responsible for allowing the critics of a competitive economic order to undermine effectively much of its general social support, especially when comparisons failed to consider the flaws of alternative arrangements (Buchanan 1968, 424). Buchanan acknowledges Vining’s emphasis on the importance of rules in economic analysis.

According to Stigler (Breit and Spencer 1995, 97) and Buchanan (Breit and Spencer 1995, 169), Knight’s teaching style made him difficult to follow and his refusal to accept anything uncritically made him the source of endless ideas for student discussion and research. Buchanan further described him as a teacher who gave us who bothered to listen the abiding notion that all is up for intellectual grabs, that much of what paraded as truth was highly questionable, and that the hallmark of a scholar was his or her courage in cutting through the intellectual haze. The willingness to deny all gods, the courage to hold nothing as sacrosanct— these were the qualities of mind and character that best describe Frank Knight.
Knight was an inveterate puzzler; but his thought process probed depths that the scholars about him could not realize even existed. To Knight, things were never so simple as they seemed, and he remained, at base, tolerant in the extreme because he sensed the elements of truth in all principles... Knight left us with the awful realization that if we did not have the simple courage to work out our own answers, we were vulnerable to victimization by false gods. (Buchanan 1992, 5)

Nutter, on the other hand, was said to have taken immediately to Knight’s teaching style and found his ideas easy to absorb (Tullock 2001). Knight’s views were highly idiosyncratic and his expository style made few concessions to listeners. Endless questions were spawned about what Knight really meant. Stigler described Knight as alternating between a great teacher and an absurd teacher, but communicating beyond any possible confusion the message that intellectual inquiry was a sacred calling, excruciatingly difficult for even the best of scholars to pursue with complete fidelity to truth and evidence (Breit and Spencer 1995, 96). The debates among students occasioned by Knight’s lectures became a very important part of the Chicago tradition.

Knight viewed the aim of economic theory as to provide guidance on practical matters of economic policy. He believed that the basic principles of economics were derived from human motivation and were straightforward and obvious to most observers. Emphasizing that these simple principles were the most useful tools for understanding the real world, Knight sought to analyze the incentives generated by various institutional arrangements. In building his model, he distinguished between risk and uncertainty. He contrasted risk as a possible event, to which an objective probability calculus can be applied and which can be insured against, with uncertainty that described those possible events to which no such calculus can be
applied. Profit (and loss) arose as the result of uncertainty, which was central to his theory of economic organization. Knight’s monograph *Economic Organization* (1933) was prepared in the early 1920s while Knight was at Iowa and was later duplicated for student use at Chicago. It contains the elements of theory that helped to establish for Chicago its pre-eminence in neoclassical economics. While, according to Buchanan, there was little in the monograph that was wholly original, its value was in its emphasis on key points, its clarification of ambiguous concepts and notions, and its integrated approach to the economy as a social organization. According to Buchanan, several generations of undergraduate students at Chicago obtained their vision of the totality of the economic process only after encountering Knight (and Simons).

*Economic Organization* did not circulate widely beyond Chicago, which explains why Knight’s theoretical contributions became known primarily from his first work, *Risk, Uncertainty, and Profit* (1921), the book of his doctoral thesis, and from a series of important papers in the 1920s. Later Chicago students Milton Friedman, Homer Jones, George Stigler, and Allen Wallis published a selection of these papers as *The Ethics of Competition* (1935). Their objective was to make available to students of the social sciences some of Knight’s essays (primarily on social control and its implications) which they believed were particularly relevant to the social problems of the day. They noted that “had the selection been made by the author, not only might the contents have been different, but some revisions might have been made (Knight 1935, 7).”

The importance of Knight’s influence was notable at the London School of Economics, where, largely at the urging of Lionel Robbins, *Risk, Uncertainty, and Profit* became required reading for an economics degree in addition to P. H. Wicksteed’s *The
Common Sense of Political Economy (1910). These two books were thus important works for Coase and others. Coase notes that Knight was one of the most important influences in shaping his views (Kitch 1983, xxxx). Coase got to know Knight personally during Knight’s time at the Thomas Jefferson Center at the University of Virginia. He reflected that, although elderly and formally retired, Knight was still professionally involved and that one could still detect in him the “fiery competitor” he once was (Demsetz 1997, 264).

Knight’s contributions to economic theory went beyond his work in price theory. In Risk, Uncertainty, and Profit, Knight laid out his now familiar double dichotomy which distinguished between statics and dynamics and between the individual and the social economy. He described in detail his conception of an economic system, an approach that has become received doctrine in introductory textbooks. Knight’s wheel of wealth emphasizes the circular flow of income in the economy as money is exchanged for factor services and final goods at successive stages in the production process. His emphasis on equalization of returns at the margin implicitly made his model an equilibrium one. And as Israel Kirzner explains, Knight’s approach contrasts with Carl Menger’s which emphasizes how the demand for final goods determines the prices of factors of production. He stressed the importance of opportunity cost, a characteristic feature of both his economic theory and the Virginia school of political economy.

Henry Calvert Simons (1899-1946)

While Knight questioned received doctrine and Viner emphasized rigorous theory, student attention tended to center around Simons, first when he was exclusively a
member of the economics department and later when he had a joint appointment to teach economics in the law school. In the 1940s Simons taught mainly students for the baccalaureate, including Gordon Tullock who was an undergraduate candidate for the LL.B. Tullock, who grew up in the Midwest as Republican and conservative found Simons to be of a different stripe in rejecting the gold standard, balanced budget, and protective tariffs. Simons’ manner was cordial towards not only faculty but also students. W. Allen Wallis described Simons as a friendly man with brown hair, brown eyes, and warm manners, who demonstrated consideration toward others (apparently not always a hallmark of the academy). Simons lived at the Quad Club, where according to Wallis, he had a fine phonograph (a “Victrola”) and many good records. The Club had a rule about noise after 10:00pm, but, at the request of many of the residents, had waived it for Simons’ phonograph (Wallis 1992). Simons’ copy of the Brandenberg concertos was very popular among the students. Simons became known for his “Positive Program for Laissez Faire,” which was published as a pamphlet in 1934. Director’s prefatory note of March 1, 1947 to Simons’ posthumous book Economic Policy for a Free Society (1948) provides an insight into Simons’ influence on the Chicago School.

Through his writings and more especially through his teaching at the University of Chicago, he was slowly establishing himself as the head of a “school.” Just as Lord Keynes provided a respectable foundation for the adherents of collectivism, so Simons was providing a respectable foundation for the older faith of freedom and equality. (Simons 1948, v)

One might argue that Simons versus Keynes is not an apposite contrast. Keynes considered himself in some respects to be a liberal in the older sense of that word. On the other hand, many of Simons’ positions would not be considered those of a classical liberal. Although Simons, like other classical liberals, defended the market process (and
this was not common in the 1930s), he made two departures. First, he insisted on government intervention to eliminate monopoly, and not just to remove the government-sponsored monopoly, by tackling its root causes. Second, he sought steeply progressive income taxes to reduce income inequality, not only to promote equality of opportunity but also because he found inequality to be “unlovely.” Simons’ use of the words “positive” and “laissez faire” set him apart from both non-interventionist conservatives and the interventionist liberals. Many would argue that Simons’ use of the term “laissez faire” was a misnomer. But Simons’ use reflects his view that there should be a division of responsibility between the government and the market. In Simons’ model the market would determine what gets produced, how it is produced, and for whom it is produced. On the other hand, the role of the government in Simons’ model was to maintain overall stability, to keep the market competitive, and to avoid extremes in the distribution of income (Simons 1948, xxx). He viewed an activist government as inevitable, but greatly feared it.

Simons was an avowed radical. He did not propose new policies as an overlay on the existing set of (ineffective) monetary rules, but insisted on a complete overhaul of the entire financial system. With regard to monopoly, Simons’ aim was not to regulate it, as advocated by others, but to eliminate it. In Simons’ mind the elimination of monopoly power would lead to greater price flexibility which in turn would lessen the impact of economic cycles. However, he recognized that these actions alone were not sufficient to guarantee stability.

Free markets and some equalization of income were the essential components of
Simons’ “positive program for laissez-faire.” He did not see the two as inconsistent.13

**Simons believed that taxes should be simple and direct and believed that tax policy should ensure that the true cost of government be levied equitably on the citizens.**

The primary virtue in Simons’ mind was liberty, which he defined as a condition which could be obtained only by preventing concentrations of economic power by removing the sources of monopoly. By 1934 Simons believed that the absence of widespread interference (which for Simons would permit the proliferation of monopoly power) and promiscuous political interference (which for Simons would strengthen such power) threatened “disintegration and collapse” of the economic organization (Simons 1948, vi). He saw that only the “wisest measures by the state” could restore and maintain a free-market system. The Virginia school, on the other hand, sees the government as primarily responsible for the existence of monopolies and that removing its support would eliminate the problem. One may also compare Simons’ and that of Buchanan with regard to inheritance taxation. Buchanan has argued that the game would be more fair and exciting if inheritance were largely taxed away. Simons believed in steeply progressive income taxes but for the most part did not favor inheritance taxes.

Simons admired Knight, having served with him on the faculty at the University of Iowa prior to their simultaneous moves to Chicago in 1927. Their interests complemented each other well – Knight focused on theoretical issues while Simons concerned himself with policy. Their social philosophy stressed that the preservation of

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13 See Walter J. Blum and Harry Kalven’s discussion of Simons’ views in which they note that “whether the argument for redistributing income is put in terms of increasing general welfare or of redressing the injustice of the existing rewards, it is always precariously close to being rested simply on envy.” (Blum and Kalven 1952, 505)
individual freedom was a goal far more important than the achievement of mere economic objectives. As a result of their reluctance to favor government over private actions in a market economy, each was branded a “conservative.” For Simons the appellation of “radical conservative” was awarded. As we have seen, Knight’s work focused on the conceptual underpinnings of neoclassical price theory, and his main concerns were to clarify and improve its logical structure. No doubt their reluctance to support the New Deal stemmed in large part from their Midwestern mistrust of bureaucratic power. Simons was Knight’s ally, but with a very independent mind.

Simons believed (to the extent of being a passion) that the world of the 1930s was facing a crisis of historic magnitude and that the survival of both freedom and prosperity in the West were at stake. Simons believed passionately that the crisis of the 1930s had to be handled well or the basic values of civilization would be lost, and he dedicated his life to that task. Knight, on the other hand, believed that the crisis was grave, and that it would be handled as badly as in the past, but that the West would survive.

Like members of the Virginia school, neither Simons nor Knight saw benefits from centralization in the hands of a few — whether it was government or any other group. This perspective became an important influence in shaping the framework of the Chicago school. Both Simons and Knight had his own following among the students, but their personal and teaching styles differed greatly. Simons had an outgoing personality and was held in high esteem by undergraduates. Although Simons was effective in stimulating intellectual inquiry, Buchanan does not consider him on a par with other teachers at Chicago. Knight, the dominant intellectual influence on the graduate students, was the person that
graduate students talked about the most. Among the Chicago graduate students he had many admirers, including Friedman, Stigler, Wallis, and Buchanan.

Buchanan studied under Knight and Viner, but his exposure to Simons came from reading his work. Nutter took courses from Viner, Knight and Simons prior to being drafted in World War II. Resuming his studies after the War, Nutter began his dissertation under Simons. Tullock knew Henry Simons as a lecturer in the one economics class that he took before he was drafted into the U.S. Army in 1941. Thus Tullock experienced only the first six weeks of Simon’s ten-week course (Brady 1999).

Aaron Director (b. 1901)

Aaron Director, whose impact is more difficult to discern because he did not publish, had a less outgoing personality and was not as popular with the students as Knight. The roots of law and economics may be traced to Director’s work in the 1940s. With the help of Knight, he had been appointed after the death of Simons to the law school where he taught the economic analysis of antitrust with Edward Levi. Director’s contributions were mostly behind the scenes as colleague, teacher, and editor of the Journal of Law and Economics for the period 1958-1970. Director’s views regarding industrial organization, e.g., predatory pricing, tying arrangements, and resale price maintenance, became known through the writing of others at the University of Chicago (Coase 1997, 601). Simons indicates that Director had “greatly influenced everything I have written and all my teaching” (Coase 1997, 601) and Coase describes Director as a

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14 His published work included one book, two jointly authored books, and six articles in economics and law journals.
crusader (Coase 1997, 601). However, he probably best fits the category of puzzler since he raised contradictions and dilemmas. He was also a skeptic.

According to Coase,

Director was able to influence so many able people in such a profound way because of his command of economic theory, his wide reading and those personal qualities that Robbins described, all reinforced by his lucidity and persistence in argument. It is impossible to discover in what ways the views of all these people were changed. (Coase 1997, 604)

In 1958 Director and Ronald Coase\(^{15}\) founded the *Journal of Law and Economics*.

Although Coase may have met Director when he first visited Chicago in 1930, we know that they met in 1937 when Director visited London to undertake work relating to his dissertation. The Bank of England was unwilling to allow Director access to their records and he spent much time at the London School of Economics. Coase introduced him to Lionel Robbins and Arnold Plant. Coase brought his distinctive approach to the Chicago school rather than the reverse when he arrived there in 1963 Breit and Spencer1995, xxx). Coase and Director were also instrumental in founding the *Journal of Legal Studies* in 1972 as an interdisciplinary journal of theoretical and empirical research.

*Viner and Simons and economic policy*

In 1992, when he spoke before the Henry Simons Society, Allen Wallis noted that few of the faculty at Chicago were interested in formal participation in the economic policy debates of the day. While Viner served as a high level advisor to US and foreign

\(^{15}\) Ronald Harry Coase (b. 1910) was born in Middlesex, England. He was educated at the London School of Economics, University of London (B. Comm. 1932) and (D. Sc
governments, and sought immediate impact on specific policy questions, Simons was an academic with little interest in direct participation in government and had little concern about what would happen even in the next decade. According to Director,

He had a high standard of excellence, higher for his own work than for that of others. He was continuously in search of arrangements which would inhibit publication while fostering discussion. He had no illusions about the great obstacles to the re-creation of a free-market society, but he held that it was “immoral” to accept as inevitable what is itself immoral. It was his contention that in a democracy the professional economists must hope that serious discussion will gradually and ultimately enlighten public policy and in the meanwhile will perpetuate the faith in discussion. (Simons 1948, vii)

In his 1934 pamphlet, Simons articulated his concern that the government might move toward collectivism in response to public opinion in the 1930s. His concerns had a major impact on the development of the Chicago school and, indirectly, the Virginia school. Unlike some of the more widely known faculty at Chicago, Simons’ focus was on the long term effects of government actions on freedom and equality. James Buchanan and members of the Virginia school are thus more similar to Simons in how they view public policy.

The intellectual environment at Chicago

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The intellectual atmosphere at Chicago played an important role in the evolution of the Chicago school, its methodology, and the questions on which its members chose to focus. According to Allen Wallis (1992), the intellectual atmosphere at Chicago was much different from other graduate schools, then and today. “The graduate students were treated as if they were colleagues and the faculty would act as if they thought they were going to get a good idea from you.” Wallis described many of the students of the 1930s (including himself and Friedman) as arriving at Chicago with an attitude about economic policy that he characterized as Norman Thomas socialist\(^{16}\). Most of the graduate students read *The Nation* and *The New Republic*, which provided the ideological basis for the New Deal. They were soon disabused of the ideas in these publications through discussions with both students and faculty (Buchanan 1995, 22).

The postwar generation of students at Chicago also experienced a Chicago conversion. When Buchanan enrolled for the winter quarter of 1946 (Breit and Spencer 1995, 168), his knowledge of the University of Chicago was almost exclusively from his undergraduate teacher C. C. Sims, who had earned a doctorate in political science at Chicago in the late 1930s. Buchanan credits Sims as impressing upon him the importance of ideas and how the genuine life of the mind was present at the University of Chicago. Once there, Buchanan experienced an excitement that was “unmatched anywhere else in the world” (Breit and Spencer 1995, 168). Within a few short weeks,

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\(^{16}\) Martin Bronfenbrenner expressed a similar view. When he arrived at Chicago, he considered himself a socialist, having read Marx and with the intention to vote for Norman Thomas in 1932 (had he been old enough). He thought the issue was not “control versus the market” but simply “control by whom?” He viewed the faculty as “quite balanced” including a conservative and later anti-Keynesian group (Knight, Simons, Lloyd Mints, and Viner) and a New Deal group (Paul H. Douglas, Henry
Buchanan had undergone a conversion in his understanding of markets and his views on socialism.

Buchanan, like others entering graduate school in the immediate postwar years, were socialists of one sort or another. Some of the students, including Buchanan, considered themselves to be “libertarian socialists” in that they placed a high value on individual liberty but, lacking an understanding of the principle of market coordination, were nevertheless socialists. Buchanan more precisely described them as “libertarians first, socialists second” and viewed them as naive in their thinking about political alternatives (Breit and Spencer1995, 170). In Buchanan’s eyes they had an idealized view of populist democracy which was preferable to what they saw as the establishment-controlled economy.

Buchanan’s conversion from socialism came from understanding the role of markets in coordinating the activities of individuals (Breit and Spencer1995, 171) and distinguishing this from the traditional view of markets as a means for distributing income. According to Buchanan, simply understanding the difference between “allocation maximization” and “catallactic coordination” liberated him.

From Knight, Buchanan got his grounding in the importance of the organizational structure of markets. It was this emphasis that elevated the coordination principle to center stage. By drawing attention toward a decision-making structure as a process, rather than the outcomes it generates, this approach allowed many of the notions of orthodox economic theory to fall away. In Buchanan’s words:

[T]o the allocationist the market is efficient if it works. His test of the market

Schultz, Harry Millis, Simeon Leland and John Nef.
becomes the comparison with the abstract ideal defined in his logic. To the catallactic the market coordinates the separate activities of self-seeking persons without the necessity of detailed political direction. The test of the market is the comparison with its institutional alternative, politicized decision making. (Breit and Spencer1995, 169-70).

Further to the point on the importance of this difference in perspective, Buchanan stated:

Many modern economists remain firm supporters of the market order while at the same time remaining within the maximizing paradigm. I submit here, however, that there are relatively few economists whose vision is dominated by the catallactic perspective on market order who are predominantly critics of such an order. Once the relevant comparison becomes that between the workings of the market, however imperfect this may seem, and the workings of its political alternative, there must indeed be very strong offsetting sources of evaluation present. (Breit and Spencer1995, 170)

Buchanan argued that it was an understanding of this principle that enabled the young student socialists at Chicago to retain their long-held anti-establishment evaluative norms on politics and governance by recognizing that economic interaction need not embody the exercise of man’s power over his fellows. Buchanan argued that, by their libertarian standards, politics appeared always to involve exploitation. Knight emphasized that markets, in contrast, need not involve exploitation.

Buchanan quickly appreciated the difference between these apparently similar, but in fact competing, paradigms. This realization had a major effect on his normative evaluation of institutions and, in particular, his advocacy of the market order (Breit and Spencer1995, 171). Buchanan believed that his conversion stemmed from studying economics from Knight who led him to understand the importance of changing the rules of the game in order to change outcomes. The importance of Knight’s insight became apparent to Buchanan when he examined rules that sought agreement by more than the simple majority which was viewed as the keystone of democratic institutions.
Knight was an important intellectual and personal influence on Buchanan both during graduate school and later over the course of his career. A second major influence was Knut Wicksell. Buchanan’s work in public finance was influenced by Knight and by his discovery of Wicksell’s *Finanztheoretische Untersuchungen nebst Darstellung und Kritik des Steurewesens Schwedens* [*Studies in the Theory of Public Finance*] (1896) which he came across by accident. Wicksell attempted to marry the principle of the sovereignty of the consumer with choices which are made through the political system when market failures require government provision. The use of this approach led him to advocate reform of the franchise, to delineate restrictions which should be placed on the power of the executive arm of the government and to devise parliamentary procedures regarding taxes and expenditure which reflected voters’ choices. He sought methods for accurate reflection of voter preferences and speculated on the consequences of his proposed institutional changes for the future of public expenditure.

Buchanan’s dissertation title was *Fiscal Equity in a Federal State* (1948) which

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17 John Gustav Knut Wicksell (1851-1926), journalist, pamphleteer and economist, was born in Stockholm, the youngest of six children. He studied at the University of Uppsala (BS cum laude 1871) and undertook graduate work over many years but did not receive an advanced degree. Having lived for many years on fellowships and stipends, in 1901 he was appointed associate professor at Lund where he remained until his retirement in 1916. The ideas in *Finanztheoretische Untersuchungen nebst Darstellung und Kritik des Steurewesens Schwedens* had a lasting effect on Buchanan’s views on public finance. Buchanan translated the first part of this book for Musgrave and Peacock 1958. This treatise has been translated but only in part by Buchanan. The untranslated sections provide an historical sketch of the development of Sweden's system of taxation from the early 16th century up to the 1890s.
became the basis for his later work in that subject. Roy Blough\textsuperscript{18} was his first reader because he was the principal figure in public finance at Chicago at that time. However, it was the second reader, Knight, whom Buchanan credits with having read his dissertation critically and having understood it. Public finance was not a major research interest at Chicago at that time and Buchanan was to pursue his research elsewhere.

\textit{The importance of Earl Hamilton in Buchanan's career}

Earl J. Hamilton\textsuperscript{19}, who studied Spanish monetary policy, impressed upon Buchanan the value of learning foreign languages and his ability to read literature in foreign languages was clearly important to his intellectual development. We have just mentioned how Buchanan read Wicksell who wrote in German. Moreover, without a

\textsuperscript{18} Jacob Roy Blough (1902-2000) was born Pittsburgh, PA, received his undergraduate degree from Manchester College and received a master’s degree and a doctorate from the University of Wisconsin. From 1938 to 1946, he was director of tax research at the US Treasury Department and assistant to the treasury secretary. From 1950 to 1952, he was a member of the president’s Council of Economic Advisers. Later in the 1950s, he was principal director of the economic affairs department at the United Nations. He also taught at several universities, including the University of Chicago from 1946 to 1952, and Columbia University from 1955 to 1970 when he retired.

\textsuperscript{19} Earl Jefferson Hamilton (1899-1989) was educated at the Mississippi State University (BS with honors, 1920) University of Texas (M.A. 1924), Harvard University (A.M., 1925, Ph.D. 1929). Earl Jefferson Hamilton (1899-1989) helped to pioneer the field of quantitative economic history during a career that spanned 50 years. His publications include a classic series of books analyzing how American treasure affected price and wage structure in colonial Spain, a history of the Bank of Spain, and some three dozen articles or contributed chapters in the fields of economics and history. Hamilton held professorships in economics at Duke University (1927-1944), Northwestern University (1944-1947), and the University of Chicago (1947-1967), and was Distinguished Professor of Economic History at the State University of New York, Binghamton (1966-1969). He served as editor of the Journal of Political Economy for seven years (xxxx—xxx) and was President of the Economic History Association from 1951 to 1952. His work on the indices of prices, wages, and money from primary sources was, according to D. N. McCloskey, central to the development of the modern quantity theory.
knowledge of Italian, the important insights of the Italian school of public finance would not have come to his attention. Buchanan’s also read French and is able to speak Italian which was fostered during his Fulbright Fellowship in Italy in 1955.

Further, Buchanan credits Hamilton with recommending him to R. Tipton Snavely, chair of the economics department at the University of Virginia, and thus setting in motion a sequence of events that ultimately brought together Buchanan, Nutter and Tullock. Although Buchanan does not know if Hamilton was instrumental in Nutter’s move from Yale to the University of Virginia in 1956, it would be plausible, given the Chicago connection (Buchanan 1999). In reading Hamilton’s papers I learned that in 1967-68 Nutter sought to recruit him to the UVA faculty. There were several letters noting the beauty of Mrs. Hamilton’s garden then at Duke and how Charlottesville had good soil and a pleasant climate. The time was not right for the Virginia department and the negotiations ended amicably although with great disappointment (and some embarrassment) for personal Nutter.

Building on the insights of Knight, Wicksell, and later the Italians, Buchanan laid the foundations for public choice and constitutional political economy, twin pillars of the Virginia school. The next phase was initiated with the arrival of Buchanan and Nutter at the University of Virginia in the fall of 1956.

*The Founding of the Thomas Jefferson Center*

As Buchanan explains in his memoirs, the Virginia school of political economy originated from a conversation with Nutter in the foyer of the Social Sciences Building at the University of Chicago early in 1948 (Buchanan 1992, 95). Nearly ten years later, in
1957 in UVA’s Rouse Hall, Thomas Jefferson Center for Studies in Political Economy and Social Philosophy was established by Buchanan and Nutter, who were later joined by Tullock.

_Daniel Rutledge Vining (1908-99)_

D. Rutledge Vining was also a graduate of the economics department of the University of Chicago. Like Buchanan, he was much influenced by Frank H. Knight. And, like Buchanan, he taught at the University of Virginia, but remained there until he retired. He was born in Birmingham, Alabama on August 12, 1908 and died in Charlottesville, Virginia on December 4, 1999. He arrived at U.Va. in 1945 and remained on the faculty for more than 50 years, taking emeritus status in 1979. Vining is the least known of the Chicago-trained economists at the University of Virginia. Although Vining’s research interests were in business cycles, spatial economics, and statistics, Buchanan credits him with emphasizing the importance of rules and institutions, a cornerstone of the Virginia school. He shared with Buchanan a southern upbringing, an interest in farming, and a Ph.D. from the University of Chicago.

Vining’s doctoral thesis, “,” does not identify his chair or committee which is not uncommon for University of Chicago dissertations. He wrote in the preface that:

Credit for any good that the study may contain must be attributed to the patient encouragement of Professors Oscar Lange, Jacob Marschak, and Lloyd Mints. Also, these acknowledgments must not fail to register the appreciation that the author profoundly feels for the background afforded by his association with Professor Frank Knight, although this influence was not direct and immediate.
Vining received a B.B.A. (University of Texas, 1931), an M.A. (University of Chicago, 1935), and a Ph.D. (University of Chicago, 1944). From 1935 to 1938 he was an instructor of economics and statistics at Westminster College in Fulton, Missouri. Subsequently, Vining was assistant professor of economics and statistics (1938-40) and associate professor (1941-43) at the University of Arkansas in Fayetteville, Arkansas. During his career he held various appointments including statistician at the Federal Reserve Bank in Atlanta (1941) and research assistant at the National Bureau of Economic Research (1948-49). He held visiting appointments at several universities including Columbia University (summer 1949), the University of California at Berkeley (summer 1956), and the University of Minnesota at Minneapolis (summer 1956). He was also a Ford Foundation Faculty Research fellow at UVA (1956-57) and a Southern Regional Science Association fellow, Atlanta (1987).

His career at UVA began in 1945 and included service as director of the McIntire School of Business Administration at the University (1952-54). He remained at the University until becoming emeritus professor in 1979. Vining was known as an independent mind who had limited association with other faculty members. He published in professional journals, contributed to books, and was author of several books and monographs, including *On Appraising the Performance of an Economic System* (1984), which took over twenty years to write (Vining, 2001).

Vining is one of six people (President Eisenhower, President Nixon, Sherman Adams (Eisenhower’s advisor), xxxxxxx and Vice-President Nelson Rockefeller were the
others) whose correspondence with Arthur F. Burns may be found among Burns’ papers in the Dwight D. Eisenhower Library in Abilene, Kansas. Vining’s correspondence provides insight into his personality. For example, he began a letter to Burns by asking whether he could publish a paper which he had prepared for a meeting of bankers at which Burns had delivered the main address. Vining noted that Milton Friedman (a student of Burns, and later a colleague at the National Bureau of Economic Research) had suggested that the paper be submitted to the *Journal of Political Economy*. He outlined the arguments in his paper and also his concerns about being misinterpreted in the following passage:

> If you recall, my paper began with a sort of expression of admiration for the work of the Council of Economic Advisors during the past two years. I felt however that you tended to attribute what appeared to me to be an effective management of the business cycle problem to a growth of a common understanding of business cycle phenomena. I was not prepared to accept this, for I was inclined to attribute the apparent success of the administration to the personnel of its advisers. I went on then to discuss the political matter of rules versus authorities in the administration of public affairs and to propose a task for you to undertake...

> I would not want to be misunderstood, and I am asking you if you think that misunderstandings could arise.  (Vining to Burns, February 2, 1955)

This letter is somewhat stilted, perhaps somewhat unnecessary, but perhaps some would view it as simply a reflection of Vining’s southern upbringing. This was not atypical for UVA where Mr. Jefferson’s students wore coats and ties to class. Professors dressed in a similar degree of formality. Others might interpret it as an effort to curry favor with Burns. Burns replied that Vining was welcome to publish the paper.

In a letter of September 14, 1955, Vining tells Burns about a monograph which he had recently completed for UNESCO and relates how Burns’ work fits within the tradition of a “classical economist.” In referring to Burns as a classical economist,
Vining is not referring to his methodology, but rather to the class of problems Burns chooses to address. He argues that Burns, like Adam Smith, was interested in considering “different systems of political economy” by which he meant alternative systems of legislative constraints upon individual action (September 14, 1955, p. 2). Vining describes the sequence of events leading to his interpretation of Burns as a classical economist. After rereading Smith, he viewed Smith’s theory of value as designed to elucidate a particular point, which was incidental to Smith’s main discussion. Vining interpreted Smith as arguing “— and this would seem to be the fundamental supposition underlying the ‘classical’ argument — that under any circumstances allowing freedom of individual action within a system of laws there will be variation among the values of commodities and among the outputs and incomes of the members of a society.” He further argued that the presence of differences among the prices of commodities and among the incomes of individuals is not to be interpreted as indicative of faulty performance of a political economy. Rather he thought that “while there will always be observed systematic variation among any particular system of laws, average income and output will be different for different systems.” This led up to the main part of his work: the consideration of “different systems of political economy,” by which he meant “alternative systems of legislative constraints upon individual action.” He interpreted Burns’ work as “judging the performance of a particular system of laws” and to the variations which may be altered by changing the system of rules. In several letters to Burns, Vining mentioned his search for the underlying principle of a theoretical structure for institutional economics and “to clarify the intent and meaning of institutionalism” (Vining’s letter to Burns, June 10, 1963).
Vining's contribution to the Virginia school

On several occasions, Buchanan credits Vining with emphasizing the importance of rules and institutions in understanding alternative social regimes (1962, xxxx; 1988, xxxx; 1995, xxxx; Breit xxxx). In their discussion on the “Economic Theory of Constitutions” in The Calculus of Consent, Buchanan and Tullock express their debt to Vining for comparing the formation of a constitution to agreeing on the rules of a game, and for his emphasis on the essential differences between such rules and the appropriate individual strategies in playing a specific game (Buchanan and Tullock 1962, 79-80). In this setting no player can anticipate which rules might benefit him during a particular play of the game, and it follows that the self-interest of each player will lead them to support rules that make the game rewarding for the average or representative player. They further argue that agreement over initial rules minimizes the intense conflicts of interest that are expected to arise as the game is played.

In the appendix on “Theoretical Forerunners,” Tullock further argues that the science of economics is rooted in the game analogy, and that early economists had discovered that the attempts of individual “players” to adjust to the strategies chosen by other “players” lead to a determinate result. Tullock noted that if a large number of people were engaged in buying and selling something and each attempted to adjust his strategy to the strategy (guessed or observed), of the others, then this would lead to an “equilibrium” or “saddle point,” to use the term coined by game theorists. Tullock cites Vining as the source of this point (Buchanan and Tullock 1962, xxxn3).
Knight’s visit to the Center

During the first half of 1958, Knight served as the Center’s first Inaugural Distinguished Visiting Scholar. He delivered six public lectures which were taped, transcribed, revised by the author, and edited for publication as *Intelligence and Democratic Action* (1960). Buchanan and Nutter wrote that this book was not the one which Knight would have written in due course, but they wanted a publication to introduce Knight to the large group of scholars who have benefitted from the many contributions he has made during his long and distinguished scholarly career. To those others who may be encountering Frank Knight here for the first time, this little book serves as ample introduction. (Knight 1960, v-vi).

“The Quest for Rational Norms” encourages people to be aware of their natural romanticism and skeptical of diagnoses and remedies, and stresses the limitations of the knowledge existent in our society. “The Free Society: Historical Background” emphasizes that we can act intelligently only in so far as we can distinguish between what is inevitable and what is more or less subject to human control. He focused on the difficulty of learning history and of learning from history. He develops the theme that “history as a whole is against the possibility of a free society; it looks like a strange accident under a very peculiar concourse of circumstances that would not be likely to last very long.” (Knight 1960, 38). “The Economic Order: Structure” focuses on the liberal market order and the role of entrepreneurship and competition. “The Economic Order: General Problems” focuses on two problems which he defines as arising either because the system does not work in accordance with the theoretical description or because it does. He divides problems into mechanistic (arising out of shortcomings of the system and embracing monopolies and cyclical oscillations) and social philosophical issues like
free enterprise. In “The Ethics of Liberalism,” Knight focuses on what social ideals define progress and identifies the direction of desirable change. He emphasizes there is no clear line between social necessity and the socially ideal. Finally, in “Can the Mind Solve the Problems Raised by its Liberation?,” Knight concludes with a discussion of what goes on in society and measures for its improvement. He considers the question in two aspects, the problems raised and our capacity for dealing with them. Like his lectures at Chicago, Knight raised more questions than he answered, thus setting the stage for many fruitful discussions among faculty and students. No doubt Buchanan and Nutter believed that the presence of a senior figure from Chicago would enhance the stature of their enterprise at the University of Virginia.

Concluding comments

This paper has discussed the Chicago influences on the development of the Virginia school. It examines the major figures at Chicago and what Buchanan and Vining brought to the Thomas Jefferson Center. In particular, it emphasizes the little known contribution of Vining with regard to the crucial importance of rules and institutions in explaining how economic performance varies between economies. The key elements of the Virginia school owe much to the philosophical questions raised by Knight. The emphasis on analytical rigor came from Viner. Simons, like Knight, emphasized the need for evaluation of the fundamentals of a question without regard for the position or stature of its advocates. From this it was straightforward to question the fundamentals of democratic institutions with which the Virginia school of political economy would be associated in the years to come.
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