

deficiencies in ability or professional expertise.¹⁶ The converse does not apply: not even the greatest talent or professional experience can make up for a lack of loyalty, reliability, or compliance.

When the antecedents of the classical system are examined one finds no such respect for loyalty or compliance either in Marx or in the pre-revolutionary traditions of the European labor movement.¹⁷ The earliest stratum in which the roots of such respect can be found is the revolutionary movement in the period before the establishment of the socialist system in countries where socialism triumphed through its own internal resources [→2.3]. These countries were repressive regimes where the revolutionaries, and in particular the members of the Communist party, were working amid persecution, and in many places and periods in a state of illegality. The movement could never have survived without discipline. Moreover, it was preparing for a revolution that would entail armed struggle, guerrilla warfare, revolutionary onslaught, and civil war, all of which required military discipline as well. After the victory of the revolution, civilian, peacetime power is taken over by persons who have grown accustomed to orders and obedience.

In the transitional period the party requires its members and the functionalities of the party and state to act in a disciplined fashion, because they are surrounded by chaos, because society has disintegrated and a new order must be established, and because a military struggle is in progress against inside and outside enemies. The nationalization of factories and other organizations has begun, and their management also requires discipline.

The most important layer of historical soil in which the attitude of considering discipline and loyalty as moral imperatives can grow is the process by which the classical socialist system is erected. Later in the book [→7.3, 21.10] there will be a detailed treatment of the bureaucratic regulation of society and the economy, for which this ethical stance is indispensable.

The virtues of discipline are closely linked with those of willing sacrifice. Individuals must be prepared to subordinate their own interests to higher interests, as defined in a specific situation by the bureaucracy. If need be they should take on extra work outside the officially prescribed working hours. If need be they should renounce the pleasures of improv-

¹⁶This criterion was formulated in an extreme form by S. Stasewski, a Warsaw secretary of the Polish Communist party at one time: "The party's personnel policy [is]: No one has to be competent in any post; he merely has to be loyal." Quoted by R. Toranska (1987, p. 187).

¹⁷Marx, an out-and-out member of the European Jewish intelligentsia, to whom these "military" qualities were totally alien, considered *de omnibus dubitandum* (one should be doubtful in all things) his favorite motto. See D. McLellan (1973, p. 457).

ing their material standard of living. If need be they should accept the subordination of family life to state interests, for most of the time of all adult family members is taken up with work and political activity. In this respect again, the official ideology embraces a kind of "military spirit"; all citizens should feel they have been mobilized. Metaphors taken from military life are common: "the labor front," "hero of socialist labor," "the battle for production," and so on. The building of socialism is likened to a long campaign in which all must do their duty. Those who do not (or are suspected of not doing so) are cowards, deserters, or traitors.

This "war consciousness" demands other virtues, such as vigilance against internal and external foes. Since there are no peaceful and civilized forms for expressing political agreement or opposition (e.g., voting between alternatives), one can never be quite sure whether anyone supports the system and agrees with the political line that happens to be in force at the time. What if they do not? One has to be on the watch for concealed enemies. That requirement in itself engenders an atmosphere of distrust, secrecy, and suspicion that requires the development, in fact the multiple development, of supervision.

The reason why distrust of the outside world and the capitalist environment arises is plain from the predicament of the socialist countries. Across the frontiers there are plenty of politicians and political movements opposed to the power of the Communist party and the creation of the socialist system and inclined to support (or actually supporting) activity aimed against that system. All this breeds a self-imposed isolation from the outside world. Insofar as possible, all influences emanating from the capitalist countries must be rejected, whether they are political, cultural, or simply expressive of their alien lifestyle. The greatest caution must be taken with any political or any economic, commercial, or financial relationship, because the outside enemy may abuse such relations and use them for blackmail or as means of applying political pressure. A symbol of this public atmosphere might be a defensive circle of wagons turned inward and prepared for an attack. Anyone consistently exhibiting this isolationist attitude counts as virtuous.

4.6 Power and Ideology

Once the party has seized power and become its sole possessor, it must never relinquish it under any circumstances. Stalin quotes Lenin's dictum that "the question of power is the fundamental question of the revolution" and then adds the following: "The seizure of power is only the

beginning. . . . The whole point is to retain power, to consolidate it, and make it invincible.¹⁸

In the official ideology's system of values, power is no mere means of attaining other primary objectives; it becomes in its own right a primary good of intrinsic, ultimate value. This must be borne in mind when assessing how the socialist system performs. To return to an earlier analogy [→ 1.7], when grading the system the following can be considered as one of the subjects of study or assessment criteria: How firmly is power in the Communist party's hands? The official ideology would suggest that this subject has great weight in the school report. As mentioned in chapter 3, the classical system scores well in this subject, since it erects the institutional frame ensuring that power is retained.

As the introduction to the chapter emphasized, power and the official ideology are as inseparably linked as body and soul. It would seem futile to ask which came first, the institutions and organizations that created the classical system, or the ideas that motivated the members of those institutions and organizations. Throughout the process, before the revolution, in the transitional period, and during the evolution of the classical system, the word is made flesh in the deeds of living persons. Conversely, these deeds, and subsequently the emerging system's need to legitimate and justify itself, constantly adjust and modify these ideas until the official ideology of the classical system matures. Institutions, organizations, and movements, on the one hand, and programs, expectations, convictions, moral imperatives, and values, on the other, all combine to bring about and maintain the classical system.

In this respect there is some similarity between the role of the Communist party under the classical system and the role of the Catholic church in the Middle Ages. Both enjoy "secular" power bound up with state power, and both exert a vast ideological influence. Each in its period has an ideological monopoly guaranteed by power and persecutes all heresy and heterodoxy. Each has a strictly organized, centralized, hierarchical structure and maintains a tough discipline in its own apparatus.

Of course, one should not take the comparison too far. The role of the Communist party and official socialist ideology in the classical socialist system is something historically unique and incomparable with any other historical phenomenon.

Max Weber argued that Protestantism played an important part in creating and consolidating capitalism; that the diligence and thrift instilled by the Protestant ethic were an inducement and ideological support to capitalist accumulation, which relies upon expansion of private

¹⁸See J. V. Stalin (1947, p. 39).

wealth.¹⁹ But neither Weber nor anyone else has claimed that the great or even monopoly influence of Protestantism was a vital prerequisite for the development of capitalism. Catholics, Jews, and Moslems too were among the pioneers of capitalism, which was able to flourish also where those religions predominated. By contrast, the classical system discussed in part 2 of this book develops and consolidates only where the official ideology of socialism just described enjoys a commanding influence.

¹⁹See M. Weber [1904] (1930).

Property

THE DISCUSSION begins with an explanation of the concepts involved in the problem. This is followed by a methodical examination of property rights under the classical socialist system.

5.1 Explanation of the Concepts

A simple distinction is often made: capitalism is associated with private ownership and socialism with public ownership. The statement is basically true, but a more accurate understanding of the situation requires a somewhat subtler system of concepts.

First of all one must distinguish *private goods* from *public goods*. An example of the former might be a garment, and of the latter the signal from a lighthouse at sea. If person A is wearing the garment, person B is precluded from wearing it at the same time. By contrast, the fact that skipper A is taking his bearings from the lighthouse signal does not preclude skipper B from taking his from the same signal. Three other examples of public goods are sunlight, the human language, and the knowledge of production processes that have entered the public domain.¹

One must not confuse the concept "public good" with "public property." The mark of a public good is that one cannot establish at a particular moment whose property it is, whereas a private good can be owned. (The latter may be the property of an individual, a group, or the state, but the last case is still one of collective ownership of a private good.) This brings one to an important constituent of the property concept: its exclusivity. A nonowner may use an owner's property only by permission. For one to be able to speak of property at all, there has to be a social mechanism that enforces the assertion of the property rights, in

¹There is no universally valid dividing line between private and public goods. The dividing line varies through history, depending on the state of technology and the social conditions. The high seas are public goods, but the maritime countries retain the prerogative of regulating fishing rights in coastal waters. This property right is enforced by international courts, by legal and economic sanctions, and as a final resort by naval force. To take another example, language is a public good, but in practice ordinary people are precluded from using it with the accent of well-to-do people; this language used by a particular social stratum serves as a private good for that stratum, whose property right is secured by the social mechanism of upbringing and education.

other words, excludes nonowners from making arbitrary use of the property without the owner's consent.

So property means, on the one hand, a relation between a person and a thing; for instance, a garment is the property of a single person. On the other hand, it means also a social relationship between persons:² the specific relationship between owners and nonowners supported by the social mechanism for the enforcement of property rights.

Property is a compound, comprehensive concept that is worth breaking down into its constituents. These will be examined by means of a number of different classification criteria.³

The first such criterion concerns what it is that the owner has in his or her possession. Here are some of the more important alternatives:

- An object (such as a garment or a machine).
- A resource (such as land or a natural asset).
- Information (such as a discovery or knowledge of a production process).

■ Someone's personal faculty: physical and mental capabilities by virtue of which some service can be offered. (It is not self-evident that such a capability is owned by the person concerned. One only has to consider the case of slavery.)

It is common for one owner to possess several kinds of objects, resources, and information at once. For instance, the owner of a factory containing a variety of machines and buildings may own the patent for a production process as well. It is also worth noting, however, that a great many things "belonging" to the factory are not owned by the proprietor at all. For instance, one does not own the workforce, one only hires its physical and mental abilities. One may simply rent the site of the factory and some of the equipment in it. One may have received some of the capital for the factory as a loan, and so on.

In studying socioeconomic systems it is particularly important to clear up who owns the means of production with which further products and services can be made. Attention will be centered on this in the subsequent

²This aspect gets special attention in the Marxist approach to the problems of property.

³The seminal contribution to the development of the "property rights" school was the works of A. A. Alchian (1965) and A. A. Alchian and H. Demsetz (1972). The main ideas of this school originate in various earlier theories. To mention only the most important antecedents: F. Knight's theory on uncertainty and risk [1921] (1965) and R. H. Coase's classical work on the theory of the firm and transaction costs (1937, 1960).

E. G. Furuborn and S. Pejovich (1972) were the first to apply the property rights approach to the behavior of a socialist firm. See also F. L. Pryor (1973).

sections of the chapter. On the other hand, I will ignore the problems of property rights over objects for the owner's personal use.⁴

The second criterion for classification concerns who the owner is. Is it an actual person—an individual, family, or specific group of persons? Or is it a legal entity—a firm, a university, a pension fund or state organization, a central government or local authority?

The third criterion, which needs discussing in a little more detail, concerns what the owner is entitled to do. In the following, property rights are divided into three main groups, which are referred to in the ensuing analysis as property rights of type a, b, and c. It is necessary to emphasize even in advance that we are dealing in all three cases with a group consisting of a large number of concrete, specific property rights.

The individual may exercise the property rights all alone or share, under specified conditions, the ownership of one and the same property with other individuals. The latter applies in case of a joint stock company, for instance, where an individual's ownership of a property is defined by his or her share in it. In the first abstract discussion of the three main types of property rights in this section the above alternatives are not distinguished yet and the "owner" is talked about in the singular. I shall return to this problem later [→5.2].

a. *Rights to residual income.* The owner has the right to dispose of the income generated by the property. One generally arrives at a more accurate description by defining this right as one to the residual part of the income, meaning that having deducted all the costs associated with utilization of the property from the income obtained with the help of it, the remaining income belongs to the owner.⁵ The owner is free to decide how much of the residual income to use for such specific purposes as individual and family consumption, investment, the acquisition of further property, and so on.⁶

The rights of disposal over the residual income are full if the owner can, if he or she so wishes, spend it all on personal consumption. (It will be seen later that in the case of a state-owned firm in a socialist society the rights of disposal are restricted in this respect.)

⁴This is termed personal property in the teaching of official political economy in the socialist countries.

⁵To clarify the concept of residual income it is worth considering the position of a tenant farmer who pays a fixed rent to the landowner for the use of the land. In this case the residual income is made up of the income from the produce of the land, less all costs, including the rent. To that extent, it is the tenant who has type a property rights over the produce and not the landowner.

⁶In the case of capitalist production, this right is described as follows in Marxian terminology: the owner of the capital has control over the surplus value. By analogy, this property right can be interpreted as existing under other social systems as well.

Full rights of disposal over residual income may be accompanied by an obligation on the part of the owner to assume financial responsibility for the debts incurred through use of the property, at least to the value of the property in question and possibly beyond this to the total value of the owner's private wealth.⁷

Full rights of disposal over residual income provide an extremely strong automatic, spontaneous incentive to the owner. If one makes successful use of the property there will be a positive residual income that one can use as one likes. If one fails one misses out on that income, and the property concerned, and under certain conditions even other personal wealth, may go toward making up the loss. All other individuals who collaborate in the utilization of some piece of property without enjoying full rights of disposal over the residual income must be given an artificial incentive before they have an interest in the success of the utilization. This is nothing other than the simple and well-known relationship whereby everything in the case of type a rights affects the owner's own pocket: the owner profits from a positive residual income and loses from a negative residual income. The statement can also be reversed: type a property rights are full if, and only if, the utilization of the property affects the owner's own pocket.⁸

b. *Rights of alienation or transferability.* Rights of this type are those that allow the owner to sell property for money, rent it out, present it as a gift, or bequeath it to heirs. Not all the four rights necessarily coincide. For instance, it may be permissible to rent out an object or resource, but not to sell it, or vice versa.

These rights combine with an automatic, spontaneous incentive as well. If the owner has obtained the property by purchase and disposes of it again by sale, he or she has an interest in ensuring that the net value of the property increases as much as possible between the two transactions. The same interest in increasing wealth applies, of course, if the property has been obtained by the owner as a gift or a legacy, or if it is disposed of as a gift or a legacy. The owner also has an interest in seeing that the property is rented out on the best possible terms, assuming the decision is to rent it out at all.

⁷The modern form of joint-stock company and other, similar legal institutions arose in order to limit this liability [→5.2, property form no. 3].

⁸An individual who can only dispose of the residual income provided he or she does not make use of it for his or her own direct profit and who is not liable to the extent of his or her own property for any loss incurred also belongs among those who need an "artificial" incentive in the sense used above. Even though he or she has partial type a rights, the way the property is used does not affect his or her own pocket, and in that sense he or she is not the owner.

c. *Rights of control.* Other important property rights are those that concern the utilization of property (management, decision making, and supervision). The simplest example of this is a small company in private hands, whose proprietor decides which employees to hire and fire, what to produce, what price to sell the products for, and so on.

As the example shows, there is not just a single "right of control," but a collection of numerous, specific rights of control. The owner can delegate to others, usually to paid employees, one or other, or even the majority, of these rights. The owner may delegate to different employees different functions of control. He or she may erect a stratified, hierarchical control organization. The owner may ensure that employees perform the functions of control satisfactorily by using a variety of incentive schemes.⁹

Although the spheres of rights grouped under a, b, and c can be closely linked to each other, they are detachable from one another to some extent. There is a particular significance in the fact that a high proportion of type c rights can become detached from type a and type b rights in many respects, that is, the rights of ownership can be separated from the rights of control.

There is a complementary relationship between the automatic, spontaneous incentive provided by full rights of ownership and the artificial incentive given to those with partial property rights but without that automatic incentive. Determining where and in the performance of which social functions to rely on automatic, spontaneous incentive and where on artificial incentive is one of the fundamental problems facing economic systems.

The fourth criterion for classification is to decide what constrains the owner in exercising property rights. In real life an unconditional property right is extremely rare. Many property rights are constrained by state and legal regulations, or at least by customary law, tradition, and accepted codes of morality. Even under the systems that allow the greatest freedom to enterprise and competition, the owner's hands are tied by a myriad of constraints.

⁹The *principal-agent* relationship is analyzed in a wide-ranging body of writing that covers an increasing number of problems. The pioneers of this research program are K. J. Arrow (1964), T. Groves (1973), S. A. Ross (1973), and J. A. Mirrlees (1974, 1976). Comprehensive summaries of the theoretical writings in this field are provided by O. Hart and B. R. Holmström (1987), the study by B. R. Holmström and J. Tirole (1989), and the entry by J. E. Stiglitz in *The New Palgrave* (1987, 3:966-72).

There is a noteworthy literature on hierarchies. The pioneer was O. E. Williamson (1967, 1975). The theoretical and mathematical analysis of hierarchies is dealt with in numerous works. See, for instance, G. A. Calvo and S. Wellisz (1978), T. C. Koopmans and J. M. Montias (1971), Y. Qian (1990), and S. Rosen (1982).

PROPERTY

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Finally, there is a fifth classification criterion: the distinction to be drawn between nominal property rights laid down in legally valid documents and real property rights.

5.2 Some Characteristic Property Forms before the Advent of the Socialist System

In terms of the classification criteria discussed in the previous section, a variety of *configurations* of property rights (or, to use a synonymous expression, a variety of *property relations*) can come into being. Each configuration can be described according to what object constitutes the property or what set of objects together makes up the object that constitutes the property, who the owner is and what property rights he or she possesses subject to what constraints, and finally, to what extent this "package" of property rights is nominal and to what extent it is real. In theory, the number of possible configurations is infinite,¹⁰ but in fact, historical systems give rise to specific types of configuration. From now on these types of configuration will be called *property forms*. Each property form is actually a theoretical model in which one or other of the specific features in the previous classification is ignored and only a few general characteristics are emphasized.

Before turning to the actual subject of the chapter, the property forms that operate under the classical socialist system, it is worth considering briefly three property forms typical of contemporary capitalism.

1. *The family undertaking.* The main item in this category is the family farm, but, of course, family undertakings appear in industry, trade, and other service sectors as well.

Remaining with the example of the family farm, the family owns the land, all the main means of production for working it, and the livestock. The family owns its own house and farm buildings.

¹⁰This is one of the weightiest arguments against unqualified use of the Marxist interpretation of the category "class" [1-3.4]. The customary Marxist definition of class is the set of those people whose property relations, primarily their relation to the means of production, is the same in the society concerned. But it is hard to decide, because of the large number of configurations of property rights, what degree of similarity to expect from the specific configurations in order to place various individuals in the same class. Are a complete pauper and one who has an interest-bearing bank account and a summer cottage rented out equally members of the "working class"? Can one consider equally as members of the "capitalist class" the person whose family owns an undertaking that employs a couple of hands with all the rights of type a, b, and c, and the opulent shareholder who by and large has type a rights to the extent of shares but does not intervene in the management of the company (type c rights)? Is a senior employee with a good salary who is also a significant shareholder at once a member of the working and capitalist classes?

There is no sharp division between the household and the production undertaking; part of the produce is consumed by the family itself and part is sold on the market. The family exclusively uses its own labor, not employing any outside manpower at all.¹¹

At an advanced stage of economic development there can emerge family undertakings that are highly mechanized, highly capitalized, and very productive, to which it is debatable whether the expression "small-scale plant" applies. But in general this is not the case in the societies where a (self-induced) socialist revolution has taken place [→2.3]. In these societies, family undertakings are indisputably small-scale plants, and their possessor-families belong to the poorer strata in society.

In a family undertaking the owner possesses all the rights of types a, b, and c. There is no separation of ownership from control. The family (in a traditional society, usually the head of the family) is both the nominal and the actual owner, and at the same time the decision maker in all business and production matters. The family has the most direct interest possible in the success of the undertaking, and no outside incentives of any kind are needed for this interest to assert itself.¹²

All of what has been said about the family farm applies by analogy to family undertakings in the other sectors.

In the case of forms 2 and 3, described below, the owners of the basic means of production utilize their property with the help of hired labor.¹³ These owners are *capitalists*. In this case this book adopts Marxist terminology, describing as "capitalist" those who in the above sense are proprietors of firms employing hired labor. The term "firm," by the way, will be reserved for organizations employing labor on a permanent basis. Forms 2 and 3 describe capitalist firms. Socialist firms will be covered in section 5.3.

2. *The owner-managed private firm with unlimited liability.* The decisive distinction between forms 1 and 2 is whether or not outside labor is employed. The difference is not conspicuous if the number employed is small, but it becomes so in the case of medium-sized or large firms.

¹¹For simplicity's sake, casually employed outside labor is ignored. If a farm employs labor permanently, it is no longer a "pure" family undertaking.

The property form described in this book as a pure family undertaking coincides more or less with what is known as a "small-scale commodity production unit" in Marxist terminology.

¹²The problem is put lucidly in the title of an article by Lester Thurow (*Financial Times*, September 6, 1986): "Who Stays Up with the Sick Cow?" On a family farm the answer is clearly: the family, or, more specifically, the member of it to whom the task has been given by the head of the family.

¹³By definition, the category "property rights" includes also the degree to which the individual is in command of his or her own labor or to which it is at the command of another: a slaveowner, a feudal lord, a capitalist firm providing employment, or the state.

The proprietor may be an individual or a family, but outsiders too can associate to bring common property into being. (Along with other differences, this last possibility distinguishes form 2 from form 1, an undertaking that remains strictly within the family framework.) The proprietors fully enjoy both the ownership rights (rights of types a and b) and the basic decision-making rights (type c rights). Production and marketing are directed by the owners themselves, who only concede lower managerial positions with a narrow sphere of authority to paid employees. So the proprietors work together with (and confront) their hired workers as living, visible persons.

The entire net profit belongs to the owners. If the firm should become insolvent, however, they are responsible for its debts to the extent of their private wealth, not just the wealth tied up in the firm. (As will be seen, this is the main way in which this form differs from the company form.) The private income and wealth of the proprietors are closely and unequivocally connected with the income and wealth of the firm.

3. *The joint-stock company in private ownership.* With this form a large number of proprietors own the firm collectively. Sometimes the bulk of the shares is concentrated into relatively few hands, in which case the main proprietors may become "visible," but frequently the shareholders are not personally to the fore, and in contrast to form 2, the property becomes "depersonalized."

The cases in which the majority of (or even all) the shares in a company are held by the state will be disregarded, and the discussion will be confined to companies in which the majority of the shares are the property of private persons, of legal entities not owned by the state, or of private institutions.¹⁴

The company's residual income belongs to the shareholder, who receives part of it in the form of dividends on shares, while the other part is reinvested (type a rights). The shareholder can dispose freely of shares, that is, the property consisting of the proportion of the company each share represents (type b rights).

Furthermore, the company form differs from form 2 in that liability is limited: the owner is liable for the company's debts only to the extent of his or her investment (i.e., the value of the owner's shares). A company is not the same as the sum of its individual proprietors, it is a separate legal entity. Should the firm become insolvent and the shares lose

¹⁴American and British terminology can easily mislead a reader not fully familiar with it. A company is called "public" if its shares are quoted on the stock exchange, having fulfilled the stock exchange's stipulations for quotation. The word public refers not to sold on the stock market. Shares in such a public company may be exclusively in private hands, but they could also be owned by the state.

their value, the shareholders' private wealth is not affected. So the connection of private income and private wealth, on the one hand, and the firm's income and the firm's wealth, on the other, is not so total and symmetrical as it is in the case of form 2. Nonetheless, the connection remains quite strong: the shareholder has a prime interest in seeing that the company is profitable and has good business expectations.

The final word on the proportions in which the residual income is divided belongs to the general meeting of shareholders, but even in the preparations for the general meeting the leading executives play a decisive part. Nominally they are just employees of the owners, who may dismiss them at any time and appoint others in their place. The shareholders are often unorganized, however, and so the managers come to possess a high degree of independent authority. There is a separation of ownership from control not found in forms 1 and 2.¹⁵

So, in fact, one group of property rights, those of control (type c rights) pass largely—but not totally—into the hands of the leading managers. However great the independent authority possessed by the leading managers of a company, they still depend heavily on the shareholders. A variety of incentives emerge. If the company flourishes, grows, and enjoys good business prospects over an extended period, the leading executives will receive very high salaries and bonuses. Perhaps more important still are the negative incentives. Shareholders may vote with their feet: if the executives manage the company badly and the likely results are poor or negative, or if the company's position by comparison with its competitors worsens, the shareholders will try to get rid of their shares, whose price will fall. It can happen that an aggressive new group takes over the company, bringing the reign of the previous managerial group to an end. A manager's whole career can be affected by whether the company succeeds or fails and whether the proprietors earn a high or low profit.

All three forms belong to a broader class of configurations of property rights, that of *private property forms*. The class also contains other configurations that cannot be described here, but in any case, these three examples are enough to convey what should be understood as a property form.¹⁶

¹⁵On this see A. A. Berle and G. C. Means [1932] (1968) for an account of how the shareholders lose power to the management. Also see J. Burnham (1941), who coined the phrase managerial revolution, and A. D. Chandler's seminal work (1977).

¹⁶State-owned firms exist also under nonsocialist socioeconomic systems. Some are wholly owned by the state and some are mixed firms in which state ownership dominates (for instance, a company in which the state owns a majority shareholding). This property form will not be dealt with in any detail.

5.3 The State-Owned Firm

In line with the overall plan of the book, I shall not be discussing the historical process whereby the property forms characteristic of the classical socialist system came into being. Instead, I shall turn immediately to the "end-product," the mature, stabilized forms. At most, I shall mention briefly the course of development for a few forms along the way.

The first and most important property form is the bureaucratic state-owned firm.¹⁷ (For brevity's sake the word "bureaucratic" will usually be dropped.) Table 5.1 shows the share of the state-owned sector in various socialist and capitalist countries.

The property form of the state-owned firm occupies the "commanding heights"¹⁸ of the socialist economy, the positions that allow the other, nonstate sectors of the economy to be dominated: mining, energy production and manufacturing, transport, domestic wholesale trading, foreign trading, banking, and insurance. On the other hand, agriculture, retail trading, and other services to the general public do not qualify as "commanding heights," and although state-owned firms appear in them, other property forms occur alongside and may even predominate.

The nominal owner of a state-owned firm is the state represented by the national government. According to official ideology, the sector is the property of "the whole of the people" or "the whole of society." This distinguishes it from other, likewise nonprivate property forms, for instance, from a firm owned by a regional organization of the state, or from a cooperative, in which the owner, according to the official ideology, is only a part of the people (the population of the region concerned or the membership of the cooperative).

To look beyond the nominal ownership and analyze the real content of the property form, one must examine the various specific property rights more closely.

a. The first main group of property rights are those of disposal of the residual income from utilization of the property. Under classical socialism this residual income flows into the central budget of the state. No definitive distinction is made between what is described under capitalist systems as company "taxation" paid to the state and what qualifies as the profits of the firm. The sum of all payments to the state budget constitutes the centralized net income of the state sector.

¹⁷The state-owned firm in the classical socialist system shows a host of pronounced features that can be observed in state-owned firms in capitalist countries as well, although in a less extreme form. (See, for instance, discussion of the problems of depersonalizing of property in this section, the relationship between bureaucracy and the state-owned firm [—7.3-7.5], and the softening of financial discipline of the state-owned firm [—8.4].)

¹⁸The expression was coined by Lenin.

TABLE 5.1
The Share of the Public Sector: International Comparison

| | Year | Share of Public Sector |
|-----------------------------|---------|---------------------------|
| <i>Socialist countries</i> | | |
| Bulgaria | 1970 | 99.7 |
| Cuba ^a | 1988 | 95.9 |
| Czechoslovakia | 1988 | 99.3 |
| East Germany | 1988 | 96.4 |
| Hungary | 1988 | 92.9 |
| Poland | 1988 | 81.2 |
| Romania | 1980 | 95.5 |
| Vietnam | 1987 | 71.4 |
| Yugoslavia ^b | 1987 | 86.5 |
| <i>Capitalist countries</i> | | |
| Austria | 1978-79 | 14.5 |
| France | 1982 | 16.5 |
| Greece | 1979 | 6.1 |
| Italy | 1982 | 14.0 |
| Spain | 1979 | 4.1 |
| United Kingdom | 1978 | 11.1 |
| United States | 1983 | 1.3 |
| West Germany | 1982 | 10.7 |

Source: The data on socialist countries were compiled by P. Mihályi for this book, on the basis of, an official CMEA statistical yearbook (*Finansy i Statistika*) (1989b, p. 49) and Saverzi Zavod za Statistiku (Federal Statistical Office, Belgrade) (1988, p. 93). The data on capitalist countries are taken from B. Milanovic (1989, p. 15).

Note: The figures refer to the percentage of national income in the case of socialist countries and to the percentage of GDP in the case of capitalist countries. The figures on socialist countries include not only state-owned firms and organizations, but also agricultural cooperatives and the net output of household farming, i.e., private plots used by the members of these cooperatives. The unrecorded contribution of the informal economy is disregarded. Because of the inclusion of the output of household farming and the exclusion of the informal sector, the figures do not reflect sufficiently the contribution of the private sector.

^aOnly state-owned sector.

^bOn the basis of Gross Material Product at 1972 prices.

In this context, it becomes a problem to say exactly what is meant by the expression "residual income." One and the same central bureaucracy is deciding on the state-owned firm's selling prices, the wages it pays its workers, the price of the means of production it uses, and the contributions it must pay into the state budget. The bureaucracy decides what proportion of the gross returns must be delivered by each state-owned firm under the heading of centralized net income (or what budgetary support the firm receives, i.e., how much its negative net income is). Of course, the same applies to the sum of all the state-owned firms as to each firm individually: the bureaucracy decides what proportion of the total budgetary income will derive from the centralized net income of the state sector, and the headings and other channels for the rest of the state income. Much the same applies on the expenditure side. The amount remitted from the central budget under any heading to any state-owned firm or to the sum of all state-owned firms does not depend on the amount received from the same firm or from the sum of all the state-owned firms.

To summarize: the residual income in the case of this property form is of an economic magnitude set arbitrarily by the bureaucracy. But once it has been set (in the technical terms of fiscal management) it flows into the central budget of the state, and in that sense the owner is the "state coffers." So one must rephrase the question to ask: Who has control over the state budget? And who sets all the economic parameters (prices, wages, taxes, etc.) that have just been established to be the factors determining the size of the residual income? The answer to both questions is the same: this right of disposal belongs to the bureaucracy. So behind the impersonal institution of the "state coffers" is the group in power, and the type a property rights are theirs.

These type a property rights are broader in one dimension and narrower in another than they are in the case of a private owner. In the private owner's case one is talking of residual income in the strict sense. Although the amount of residual income that remains in the private owner's hands depends on his or her own activity, it also depends on circumstances independent of the owner (such as market prices and state taxes), whereas the centralized net income from the state sector is determined, as has been seen, almost totally by the bureaucracy itself. On the other hand, this right of disposal is narrower, since no individual member of the bureaucracy has a total right of disposal over the residual income. The right of disposal is restricted by a web of regulations and prohibitions.

The type a property rights are concentrated most of all in the hands of those with the greatest influence on the setting of the plans, state income and expenditure, prices, and wages. But at these levels of decision-

making rights, the personal income and wealth of the most influential individuals is unconnected with the income and wealth of the state-owned firms. None of the profit from the state-owned firm passes automatically into the pockets of these members of the bureaucracy, and, conversely, they need not contribute out of their own pockets to any of the state-owned firm's losses. Since the connection between the "personal pocket" and the residual income of the state-owned firm is entirely absent, those who otherwise have the deciding voice in how the residual income is used are not real owners at all from this point of view. The automatic, spontaneous incentive noted with private property does not apply. Society must rely wholly on artificial incentives.

It is customary under the classical socialist system to employ incentive schemes that could give the top executives of state-owned firms a measure of interest in raising profits, and the interest may even extend to the firm's whole workforce. But it is normally a loose and weak interest. The scale (usually small) and precise formula of the incentive are set arbitrarily by the higher authorities, so that it becomes a mere means of control, that is, an incentive of the kind described earlier as artificial, and not a type a property right under which the whole residual income belongs to the owner.

b. State-owned firms do not constitute objects for purchase or sale; they cannot be leased out, given away, or inherited. Under the classical socialist system the property rights of alienation cannot be exercised by anyone, not even the "state" as the nominal owner.

c. The property rights of control are exercised by the bureaucracy. The activities are controlled by a hierarchical bureaucracy within the state-owned firm, and this bureaucracy constitutes the lower levels of a hierarchy embracing the whole of society. There are still numerous levels above it, right up to the peak of the hierarchical pyramid of power, the top person in the system. Although the type c rights are exercised by the bureaucracy as a whole, they are unevenly distributed among it, according to the relative influence of individual bodies in the apparatus and individuals within those bodies. Bureaucratic control will be discussed in detail in the next chapter. Here it is only necessary to put forward a few notions closely connected with the subject of this chapter.

The bureaucratic apparatus exercising direct control (type c rights) over the state-owned firms is separated organizationally from the apparatus handling the state's financial affairs (and exercising type a rights). Only at the very top are these two branches of the bureaucracy under the common direction of the party general secretary, the Political Committee, and the government.

One can leave open the question of whether the bureaucracy is acting for the good of the whole people or in its own, narrower interest when

it exercises its type a and type c rights, that is, disposal of the residual income and the rights of control, since it is irrelevant to a clarification of the nature of property. A private capitalist owner remains a private capitalist owner even if he or she constantly distributes all income for altruistic purposes and runs a factory in such a way that its production serves the needs of the people to the fullest possible extent. Likewise, even if the leading stratum of a bureaucratic socialist power should live an ascetic life, if it should consider its prime task to be the raising of the population's material standard of living, and if it should carry out this task effectively, the property relations of the state-owned firm remain bureaucratic in the sense described above.

It follows from the line of thinking pursued so far that the expression "property of the whole people" is merely ideological in nature. It does not express the real property relations that subsist in the state-owned firms of classical socialism.

Remember what was established in the previous section in the case of private property forms about the depersonalizing of property and about the separation of the rights of ownership from those of control as one moves from the family undertaking to the joint-stock company. Clearly, in the classical socialist firm both these tendencies are taken to their absolute limits.

The depersonalizing of property becomes extreme. Whatever state-owned firm one takes as an example, there is no individual, family, or small group of partners to whom one can point as owners. Since no one can pocket the profits and no one need pay out of his own pocket for the losses, property in this sense is not only depersonalized but eliminated. State property belongs to all and to none.

Within the impersonal, faceless bureaucracy there is a rigid division between the bureaucratic apparatus collecting the residual income and the one controlling production. But it must be added that by comparison with the division under modern capitalism, there is in a sense a degree of "reunion" taking place. After all, the bureaucracy under classical socialism is a centralized, uniform social formation that uses hierarchical division of responsibilities to exercise a specific set of property rights: some of the rights of ownership and all of those of control.

5.4 Other State Property Forms

Having discussed in some detail the property form of the firm owned by the national government, it is enough to mention briefly that other state property forms exist under this system too.

One widespread form is the firm owned by a regional organization of the state (in federal countries, a national or provincial government, or a county, city, or village council). All of what was said in section 5.3 applies also to this form, except that the nominal owner is the state organization of a smaller territorial unit. But in the last resort this regional state organization is itself part of the all-embracing bureaucratic power, and subordinate to higher levels of control.

The other, equally widespread form is the institution whose material wealth is owned by the state (either the central government or a regional state organization) and under state control, but which does not qualify as a "firm" under state law. The most common name applied to it is *budgetary institution*. This kind of organization is not obliged even nominally to make its income cover its expenditure. All income accruing passes to the state budget, which covers all expenditure incurred. (In this it differs from the state-owned firm, where it is merely the positive or negative balance between income and expenditure that flows between the firm and the state budget.) Examples of institutions in this category are the state-run universities, hospitals, and museums.

It is tempting to compare these institutions with the nonprofit institutions of capitalist countries, which themselves can be contrasted with capitalist firms intent on making a profit. But the comparison is not entirely apt. In fact, there is no real profit motive in the classical socialist state-owned firm either [→8.4], and the decision on whether the legal status of a particular organization should be a "firm" or a "budgetary institution" is fairly arbitrary.¹⁹ In terms of the subject of this chapter, property relations, there is little real difference between them. All the property rights apply analogously in both. Each is a species of bureaucratic state property.

5.5 The Cooperative

The second basic property form under the classical socialist system is the cooperative.²⁰ Its importance is mainly in agriculture, and so this will be dealt with in more detail.

¹⁹In the official analysis of Marxist political economy a distinction is drawn between productive and nonproductive sectors, with education, cultural provision, and health care among the latter. Ordinarily, the organizations in the productive sectors are firms, while those in the nonproductive sectors operate in the legal frame of budgetary institutions.

²⁰The state-controlled cooperatives about to be dealt with have to be distinguished from the small-scale cooperatives that emerge in the course of reforms. These resemble private partnerships [→19.2].

Different countries use different names, for instance, an agricultural cooperative in the Soviet Union is called a *kolkhoz*. In line with the overall plan of the book, the main emphasis will be on examining the features common to them all.²¹

In most countries the classic agricultural cooperative is exclusively a production and sales cooperative. Nominally, it is an organization based on voluntary association of its members, in which the means of production form the collective property of the cooperative, and the membership itself elects its leaders. In practice, it differs substantially from the foregoing description.

The process of mass collectivization took place in almost all socialist countries where the classical socialist system eventually stabilized.²² Data about the collectivization in the Soviet Union are shown in table 5.2 and figure 5.1. Before this happened there existed agricultural cooperatives organized in a more or less voluntary way, but they accounted for only a small proportion of production. The dominant property form in agriculture was the small family undertaking that employed no outside labor on a regular basis. In addition, there were small private agricultural undertakings employing outside labor, but not in large numbers. According to the Marxist classification the former are small commodity producers and the latter capitalist farms. Other criteria besides regular employment of outside labor have been used to classify a farm as capitalist: ownership of more than a specific area of land or number of livestock, or of a threshing machine, or of some other large piece of equipment could suffice to classify a farm as capitalist. Small-scale capitalist peasants in the Soviet Union were known as *kulaks*, a name that spread to other socialist countries as well.

Aggressive persuasion, threats, and brutal sanctions against resisters were used during the mass collectivization to induce the owners of small peasant farms to abandon farming on their own account, join the cooperative, and hand over their land²³ and other means of production. The

²¹Economists inside and outside the socialist countries also use the expression *collective property*. This book refrains from using the expression because it could be misleading: the bureaucratic state property described in the previous section is also "collective," both nominally and in reality. This collective character becomes particularly apparent if one compares it to individual, private property.

²²The history of Yugoslavia and Poland differs from this to some extent. Although there was forcible collectivization, the campaign was not carried through consistently, so that a significant proportion of agriculture remained as noncollectivized family undertakings. In this respect these two countries never arrived completely at the pure form of the classical system.

²³In certain socialist countries the land was nationalized immediately after the revolution, so that it was nominally state property before the collectivization, although the property rights were actually exercised by the peasant farmers. (This was the case in the Soviet

TABLE 5.2
Collectivization of Soviet Agriculture

| Year | Collective Farms (thousands) | Peasant Households Collectivized of Total Number of House- holds (percent) | Gross Agricultural Production (index) | Livestock Production (index) |
|------|---------------------------------|---|--|------------------------------------|
| 1913 | — | — | 96 | 87 |
| 1918 | 1.6 | 0.1 | — | — |
| 1928 | 33.3 | 1.7 | 100 | 100 |
| 1929 | 57.0 | 3.9 | 93 | 87 |
| 1930 | 85.9 | 23.6 | 88 | 65 |
| 1931 | 211.1 | 52.7 | 84 | 57 |
| 1932 | 211.1 | 61.5 | 76 | 48 |
| 1933 | — | — | 82 | 51 |
| 1934 | — | — | 86 | 52 |
| 1935 | 245.4 | 83.2 | 99 | 74 |
| 1936 | — | — | 93 | 76 |
| 1937 | — | — | 116 | 83 |
| 1938 | 242.4 | 93.5 | 107 | 100 |

Source: P. R. Gregory and R. C. Stuart (1986, pp. 109, 111).

small capitalist (kulak) farms were confiscated. Their owners in the Soviet Union and several other socialist countries were subjected to terror that extended to mass physical assault, deportation, imprisonment, and execution. Often small-scale producer peasants were classified arbitrarily as kulaks and subjected to the same treatment, which increased the anxiety of those around them and helped induce people to join the cooperative in mass.

The trauma of forcible collectivization²⁴ left permanent scars on cooperative agriculture. After the cooperative sector had become institutionalized and normalized, the brutal mass terror ceased. Since peasants under the classical socialist system have no alternatives, however, the

Union, for instance.) In other socialist countries (e.g., Yugoslavia) the peasants farming individually possess the nominal rights to their land as well.

²⁴For accounts of forcible collectivization in the Soviet Union, for instance, see R. W. Davies (1980), M. Lewin [1968] (1974), and R. Conquest (1986).

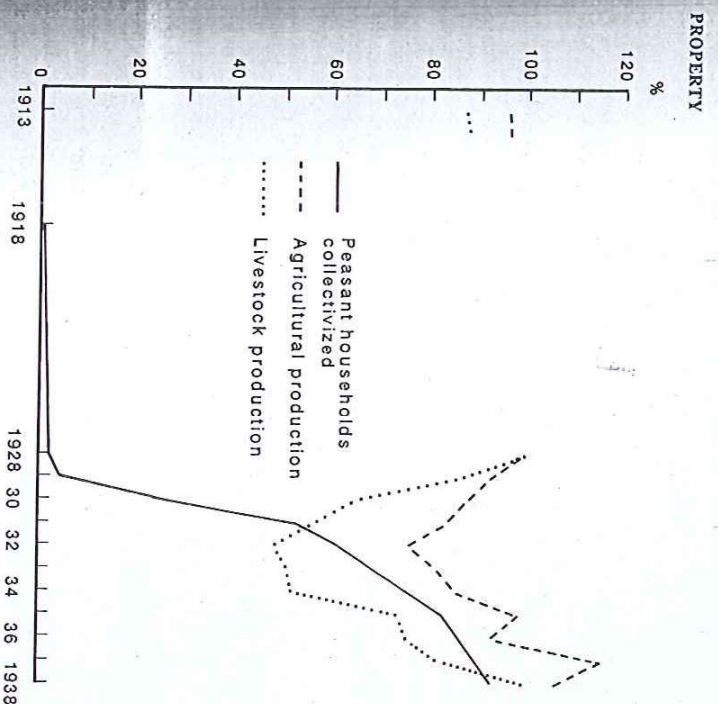


FIGURE 5.1 Collectivization of Soviet Agriculture
Source: P. R. Gregory and R. C. Stuart (1986, pp. 109, 111).

cooperatives cannot be described as truly voluntary associations even after institutionalization. They cannot choose freely whether (1) to leave the cooperative (or, if they have never been a member, to refrain from joining) and work in a family undertaking based on private property instead; (2) to employ permanent outside labor in their own agricultural undertaking if they can afford it; or (3) to join the cooperative on a voluntary basis (or, if they are already members, to remain voluntary members). Anyone wanting to work on the land must be a cooperative member (or possibly an employee of a state farm).

The leadership of the cooperative is only nominally elected by the members. In fact, they are appointed members of the bureaucracy, and in this respect they are in a position no different from elected officials of party or mass organizations or elected members of national or local legislatures [→3]. They too are totally dependent on the upper levels of the bureaucracy.

Nor can the leadership of the cooperative decide independently how to use the cooperative's income. The use is restricted by general regulations and by occasional, specific interventions from above. (Property rights of type a are absent.)

The leadership may not alienate the cooperative's means of production. Higher authorities decide on transfers of particular means of production and in cases where the cooperative merges with another. (There are no property rights of type b.)

The leadership does not have the freedom to decide how the means of production are used. The cooperative is as subject to the control of the centralized bureaucracy as any state-owned firm [→7]. (So property rights of type c are lacking also.)

It follows from what has been said that there is little real, tangible distinction under the classical system between the state-owned and the cooperative property forms. The latter is more or less a species of bureaucratic state property invested with a curious cooperative character. In reality, they operate as "nationalized" cooperatives and their property can be regarded as quasi-state property.

The only essential difference is that cooperative members in the Soviet Union and most Eastern European countries are entitled to till some private land known as a *household plot*. This is a tiny holding, and the peasant actually owns privately only a proportion of the means of production on it. The very small piece of land is assigned to an individual by the cooperative, which can take it back at any time and provide another little piece in its stead. Some of the equipment is rented from the cooperative or the state farm as well. Although the peasant family's property rights over the household farm are only partial, they do include the right to the residual income from it (rights of type a). That suffices to encourage intensive work on it: household farms account for a proportion of the total national production of animal products, vegetables, and fruit far in excess of the proportion of the agricultural land they occupy. Table 5.3 presents data on the household plots of Soviet kolkhoz members.²⁵

What justifies bringing the cooperative sector of agriculture into being? There are two sides to the question. On the one hand, what provided the incentive to eliminate the private property forms? On the other, once that had happened, why was this not done openly, as nationalization?

While the collectivization is going on, great emphasis is put in official propaganda on momentarily relevant arguments. (For example, during the Soviet collectivization the main one was the grave difficulty in supplying the cities with grain.) But from the start the official propaganda

²⁵The conditions in Bulgarian agriculture were comparable to the Soviet situation described in table 5.3. Here 37 percent of the chicken production, 46 percent of the meat production, and 53.1 percent of the egg production in 1985 came from family smallholdings, which accounted for only 12.8 percent of the cultivated land. R. J. McIntyre (1988, p. 105).

PROPERTY

TABLE 5.3

Private Plots in Soviet Agriculture

| Year | Income from Private Plots of Kolkhoz Members (percent of total income) | Contribution of Private Sector to Total Output | |
|------|--|--|----------------|
| | | Meat (percent) | Eggs (percent) |
| 1960 | 45 | | |
| 1965 | | 40 | 67 |
| 1970 | 35 | | |
| 1975 | | 31 | 39 |
| 1980 | 28 | | |
| 1983 | | 29 | 30 |
| 1985 | 26 | | |

Source: Column 1: V. G. Tremi (1987, table A3); columns 2 and 3: P. R. Gregory and R. C. Stuart (1986, p. 270).

about collectivization also lays great stress on longer-term economic considerations: the advantage of a large undertaking over a small, the principle of economies of scale. According to this argument, productivity is low in a small family undertaking and much is consumed by the household itself, so that the farm takes few goods to market. The claim is that in the large-scale undertaking productivity will be far higher. Even if self-consumption by the household does not fall, the proportion of produce sent to market will rise appreciably, according to the official ideology behind collectivization.²⁶

In fact, this line of argument parallels the thinking found in Western economic theory.²⁷ It is worth combining small firms into large ones if the latter are more efficient, which will manifest itself in higher profits. Remaining with this line of thinking for a moment, the key question is clearly whether the efficiency of the large undertaking really is greater. To this question no general answer is valid and true for any sector of the economy or any process of consolidating small undertakings into large ones, irrespective of the social, political, and economic environment in

²⁶Large-scale (state and collective) farming enhances labor productivity through cooperation: "Today . . . the peasants are able to combine their labor power with the labor of their neighbors, . . . and to produce much more than formerly." J. V. Stalin (1947, p. 312).

²⁷See R. H. Coase (1937) as well as O. E. Williamson (1975) on the theories of transaction costs, and on the relationship between hierarchies and markets.

which the small or large undertakings are operating. Ultimately, large-scale cooperative farming under the classical socialist system has not proved more productive or efficient than small-scale farming.

The motives for collectivization, however, are not limited to economic considerations and efficiency. Just as big a part, or even bigger, is played by political intentions, the effort to bolster bureaucratic power.²⁸ Peasant farming based on private property is incompatible with the totalitarian power of the bureaucracy, because it could come to represent an independent social, political, and economic force, whereas large-scale cooperative management incorporated into the centralized bureaucracy fits integrally into the totalitarian power structure. The independence and self-determination of the private peasantry ceases and there is no longer any difference between the dependence of the rural population on the bureaucracy and the dependence of any other strata of the population.

Moreover, the very elimination of private property and creation of public property has intrinsic value in the eyes of those in power. This applies also to the small family undertaking, where it is thought that the peasant farming individually will be infected with "petty bourgeois" self-interest, with avoidance of service to the common good, and with avarice and backwardness. In addition, wherever small-scale production is widespread the process of accumulation will steadily bring capitalist property into being: the most successful or fortunate peasants farming on a small or medium scale will become kulaks [→19.3].

As for the other half of the question, utilization of the cooperative form (instead of open nationalization) and toleration of household farming is a compromise between the real, ultimate intention and momentary social realities. The real and feigned concessions markedly reduce resistance and make it somewhat easier for the mass of the peasantry to accept the loss of the chance to farm for themselves.

The extent to which this is merely a compromise is confirmed by the repeated official declarations that cooperative property is a lower form of social ownership than state property. So it can only be transitional, although the transition may take a long time. Ultimately, all production must be included in the framework of ownership by "the people as a whole."²⁹

²⁸On the relationship between the choice of organization form and the endeavors of political power, see S. Marglin (1976).

²⁹This idea can already be found in Marx: "To save the industrious masses, cooperative labour ought to be developed to national dimension, and, consequently to be fostered by national means." K. Marx [1864] (1975a, p. 12). The last economic study Stalin wrote was a discussion of "what must be done to raise collective-farm property to the level of public

In fact, state farms existed in the agriculture of the classical system from the very start. (In the Soviet Union the name used is *sovkhoz*.)³⁰ The long-term tendency toward relegation of the cooperative form is confirmed by the fact that the ratio of state-owned firms to cooperatives is rising steadily in several socialist countries.³¹

Compared with what has been said so far, the situation of the Chinese commune needs mentioning specially in one respect. Collectivization was taken even further than in the Soviet Union and many other socialist countries. Even such vestiges of private production as household farming on the Soviet kolkhoz were eliminated. Communes have not confined themselves to agricultural production; they pursue industrial, commercial, and other service activities as well. Collectivization of some of the consumption within the commune was introduced. The totalization of power was taken further, since the commune combined the functions of state administration with those of economic control. The commune became a bureaucratic authority, a firm (or rather a conglomerate pursuing a diversity of activities), and a consumption community above the individual households.

So far this section has considered agriculture. One finds cooperatives in other sectors of the classical socialist economy as well, but they do not differ in their basic features from the cooperative farms, and the relative weight of their production in their respective sectors is far less. I therefore refrain for brevity's sake from discussing them in detail.

5.6 Private Property and Production Activity of a Private Nature

Under the classical socialist system, private firms employing hired labor either do not exist or are restricted to a small segment of the economy. The almost total elimination of private capitalism is precisely what the official ideology considers a major, or even the main, criterion of socialism. Only state and cooperative ownership are recognized ideologically as socialist.

³⁰Over a long period another kind of organization owned by the state operated in the Soviet Union alongside the sovkhoz providing agricultural produce. Known as the "machine tractor station," it rented out larger pieces of machinery (such as tractors and combine harvesters) to the cooperatives. For a long time the cooperatives did not even have the right to purchase larger machines, because ownership of them was monopolized by the state machine tractor stations. This further increased the cooperatives' dependence on the "openly" state-owned sector. Such stations were set up in several other socialist countries as well.

³¹In 1953 the sovkhozes (state farms) worked 9.6 percent of the sown area in the Soviet Union. By 1983 the proportion was 53.4 percent. P. R. Gregory and R. C. Stuart [1974] (1986, p. 269).