

REPUTATION
*and other skills for the
next generation of leaders*

By
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*Fight for ideas.
Live for amazement.
Pray for leaders.*

The Introduction ...

The Ideal ...

The Toolkit ...

The Paradigm ...

The Focus ...

The Sunlight ...

The Leaders ...

The Introduction

How do you encourage new ideas, resolve contested viewpoints and take useful action in a landscape of digital echo chambers and wayward leaders?

Pundits and policy-makers have never before had faster access to better information. However, the temptation to filter details to feel informed, but unchallenged, has left them too self-absorbed to lead. Untempered by debate, their solutions are stale and unconvincing. Untrained to find the harmony of different, yet complementary, notes, they miss the opportunity to resolve competing ideals.

Financial moguls are also awash in free information, but they have withdrawn to opaque and illiquid worlds, such as derivatives, hedge funds and private equity to seek an advantage. As a consequence, capital contracts and their insurance cousins, which might appear to have substance in the glow of a computer screen, can evaporate in the sunlight. The trades are not always illusory, but price discovery, the main point of a market, gets lost in the jungle.

Journalists have faltered in their roles as watchdogs and idea market makers. The competitive jostle for the big scoop has yielded to the easy pleasure of self-righteous indignation. Hard facts remain elusive. They are costly to gather and might disturb the audience-preferred narrative. Instead of the relish for public debate of a William F. Buckley and Danial P. Moynihan, opinion leaders right and left indulge forgone micro-audiences with solipsism instead of solutions, retreat instead of renewal. Why invite a challenge in a working marketplace of ideas when you can field a virtual foe just slow enough for your audience to feel good and smug?

Financial markets have devolved. Why face challenges to your valuation gambit in a healthy market, when you can pull profits from a faceless and suspect one? With the government increasingly moving from beat cop to house player in these closed feedback loops -- Long Term Capital Management, Fannie Mae, AIG-Goldman Sachs, pension fund bailouts, General Motors, and now sovereign debt auctions and currency manipulation -- the risks to society have magnified exponentially.

An examination of technological change and the natural human response provides explanations, but academic exploration alone does not suffice. We

are living daily with severe consequences. The disquiet is palpable, the possibility of violence real. We need capable and convincing leadership that can overcome these limitations with a new set of tools and an invigorated sense of purpose. If such leaders do not emerge, we will face not only the inevitable market cycles and periods of malaise, but foundation-threatening shocks from deep, unresolved tensions.

With only the pre-convinced and pre-wired tuning in, winning solutions remain isolated and are often lost. Under these circumstances, the art of persuasion is like learning Latin: nice erudition, but when do you need it? And without persuasion, decision-making does not evolve into leadership.

Even worse, as pandering replaces persuasion, an ethic of argument and resolution becomes deaf absolutism, if not absurdism. The pages of mainstream newspapers cannot be distinguished from *The Onion*. Late night satirists are more credible than news anchors. Political candidates are qualified by a combination of blank slate, tone deafness, and a willingness to flip the bird to their ideological and professional rivals. These traits are the opposite of the disarming talents and outward-looking spirit that leadership has always required.

In a supermarket of vindication candy, everyone buys a personalized notion they have been terribly wronged, and must seek redress without compromise. Leaders that oblige such demands abdicate their duty to engage competing ideas and to persuade others of their own merits. As a result, decisions are convenient fictions (or avoided altogether); and the seams in our economic, political and social fabric stretch to the breaking point.

Leaders cannot remain so disengaged, self-centered, and uncompromising and expect to be successful in the long term.

The isolation of our political world is mirrored in our financial markets, where clever, but obscure, novelties outpace a regulatory mindset unable to connect critical dots. In the fall of 2008, a poorly ventilated credit default swaps market belied the bond world's view of AAA mortgage-backed securities. With global bank balance sheets resting on over a trillion dollars of these suddenly "toxic" mortgages, inter-bank lending rates jumped to unsustainable levels, and exchange ground to a halt. Equities plummeted in the uncertainty.

Our regulators were at a loss: which was cause and which effect? They faced a crisis they had themselves abetted by promoting a dubious rating oligopoly, applying inflexible accounting conventions and making markets in shaky housing credits -- all of which skewed pricing and drove a bubble.

Confessing those failings, while the right starting point, did not come under consideration. Politicians and moguls stepped into the limelight mostly to angle for advantage or cover their own hides. A generation of well-remunerated careerists had risen to key posts by shifting responsibility, avoiding accountability, and advancing in the shadows. Unsurprisingly, they led the financial system into chaos. Credible leadership based upon information, clear analysis, debate, and action (in that order) vanished from public view.

Into this vacuum stepped an odd breed of cipher. Out of ignorance or opportunism, they pursued a hair of the dog solution that failed the paper bag test, but provided a convenient scapegoat: “greed” on “Wall Street”. This was hardly a diagnosis, much less a prescription. Without honest consideration and presentation, the cure -- print more money, bail out cronies, sweep market anomalies under the rug, and thoughtlessly breed more of the same failed rules -- was worse than the disease.

In the wake of these leaderless efforts, unemployment has surged and wealth creation has stagnated.

Despite this bleak assessment, a ray of hope shines through. That hope comes from an idea -- both time tested and promising -- that can deliver us from the weary stand off between advocates of “free markets” on the one hand and “regulation” on the other. Leaders need to understand that both terms are misleading, misused and survive from an irrational appeal. Markets can never be free because of the costs to install and maintain the market plumbing; while the current paradigm for regulation is so dysfunctional it makes any such cure worse than the disease.

Fortunately, among other qualities and tools, modern leaders can look to a powerful market-centric paradigm with a growing set of applications. Amid the self-indulgence of modern politics and the video game ethos of our financiers rests an idea so fertile, so powerful, that it created the fastest \$1 billion revenue company in history (just Google that one). Web search is

just one of the many exemplars recently born of reputation theory. Not only has this new set of applications changed the way people seek and share information, it can move us beyond the 20th Century regulatory Leviathan that must perish in order for us to progress.

Reputation is ancient, but it is relatively unstudied in its application to modern markets and our leaders understanding of how to use them. At its heart, reputation theory focuses on trust mechanisms (often quite simple ones) to generate pairing efficiencies. It matches the bona fide buyer and seller, lender and borrower, investor and entrepreneur, seeker and sought, benevolent and needy, ally and allied, trendy and trend, doctor and patient, diagnosis and treatment -- all with a speed and efficiency no central authority could possibly match.

Reputation is the most elemental building block of the information economy and the secure, trusted peer networks that power it. Properly applied, reputation theory can dramatically reduce the size and increase the efficiency of organizations, improve the effectiveness of our vital markets, and increase our nation's wealth by turning our energies to promising pursuits. There are a number of ways that reputation can manifest itself, but trust is at its core. Trust, in turn, is an essential component of exchange, and exchange a key catalyst for social and economic progress through market competition.

Google's PageRank algorithm, which instantaneously matches simple search terms with more detailed information, determines who, what and when to trust. Trust mechanisms explain why Wikipedia is so eerily relevant, and how Twitter and LinkedIn have added users at rates that turned earlier web portals in to wallflowers. You can now find a reliable car repair shop on Yelp in seconds instead of thumbing through a thousand page phone book, where your attention could hinge on the number of "A"s in the name. And reputation powers Kiva, so you can lend money to an entrepreneur five thousand miles away with a few mouse clicks and more likelihood of repayment than when the bank next door makes a loan with documentation two inches thick.

For leaders, the use of reputation goes deeper than finding a good plumber or a forgotten classmate. Reputation rests at the foundation of effective markets, and the next generation of leaders cannot survive without understanding and fostering effective markets -- whether the currency is goods, services, money, securities, contracts, labor or ideas.

All the technology in the world does not create progress without working markets to prioritize choices. These essential, but inherently dynamic, systems demand transparency, trust, information, dedicated and ethical market makers, reliable counter-parties, policing and cost-sharing agreements -- all with the ability to survive the ebb and flow of personal delusion, partisan ambitions and inevitable rigging schemes. The payoff is worth the effort: working markets deliver progress in a way no other systems can. This book's ambition is to ensure that leaders embrace the market paradigm and are able to foster and fix markets -- or shun them if they have gone hopelessly off track. Reputation is the key.

Our current organizational rule-making paradigm was born over a century ago to grapple with industrialization and urbanization. It remains willfully ignorant of this simple tool of the information era as the result of a lingering bias against markets in an increasingly influential academic, non-experiential environment.

Faced with a proliferation of rigged systems, our leaders flail, steadfast only in a mild autocracy and the application of byzantine behavioral rules overlaid one upon another since the dawn of the telegraph era. More often than not, this kind of leadership culls the salutary animal spirits of reinvention, slows the process of adaptation, ignores obsolescence, exacerbates existing problems, and plants seeds for new ones. Anyone seeking to lead the next generation forward must change trajectory.

The stakes are now higher than a handful of marginal efficiencies promised by the "reinventing government" crowd, who are busy rearranging the deck chairs on a sinking Titanic. The very foundation of our liberty is seriously threatened. With layers of gotcha regulatory regimes and agencies, the only certainty is that almost everyone has transgressed some rule somewhere, putting them at the mercy of personal or partisan enemies. When legal jeopardy is ubiquitous, we are no longer a nation of citizens bound by laws and contracts. We are mere subjects of its bureaucratic agents and partisan operators for whom leadership is often anathema.

Partisan ambitions bring to mind a moment three decades ago when I told my grandfather I was interested in politics. He was retired -- the former chief of a Milwaukee steel company, where he started out of college as a bookkeeper. Upon hearing of my interest, he suggested a book to read:

Taylor Caldwell's "A Pillar of Iron" -- a dramatization of the life of Cicero, the Roman philosopher and orator.

Not quite the dialogues of Plato, this novel nonetheless made his point: politics is a brutish affair of personal ambition that preys on peccadilloes and destroys the earnest servants of a higher cause. In the case of Cicero, his service to the state ended on a dark night on the outskirts of Rome pursued by Marc Antony's assassins tipped to his whereabouts by a disloyal servant. His hands and head were severed from his body, which he is reported to have offered up without resistance once detained. Quite obviously, politicians were a more serious species -- and politics an earthier affair -- in those days.

Today, character assassination suffices, and casually circulated half-truths, not daggers, are the weapons of choice. Perhaps that raw threat to one's physical well being was why earlier generations were schooled in the art of persuasion, and the coolness of reason, rather than the half-cocked rumors, teen drama, and wallowing indignation that fill the airwaves and web today.

Similar to the "say that to my face" ethos of another political era, there was value in outcry markets, where traders could look one another in the eye as if to say: "Are you kidding me?" It is this kind of intensity that produces confidence, direction and leadership, and it is this environment that is fading rapidly from our view unless a new generation takes up the mantle.

As Cicero proved, powerful ideas ultimately outlive temporal enemies. Where even the best leaders may disappoint, ideas perpetually animate. We know his work inspired successive generations of Romans, including the sons of those who had him assassinated. Leaders throughout history, including our own Harry Truman and Calvin Coolidge, were motivated and instructed by his ideas. I hope this book taps in to a similar flow of positive ideas.

You can't keep a good idea down when championed by a tenacious, persistent and persuasive leader. Plenty of adversaries will certainly try. As Edwin Friedman counsels us: leaders must expect sabotage. The struggle to free up those ideas is nothing short of a calling for anyone who aspires to a leadership role; and the final chapter of the book reviews a handful of leaders that are fighting that good fight in this day.

This book is dedicated to Henry Charles Fechtmeyer. My grandfather was hard-working and thoughtful. Evidently, he also enjoyed overwrought historical dramatizations by conspiratorial authors. After 25 years, he left his perch following a takeover. The board gave him a gold watch and a set of golf clubs, and, given that this was before the days of 401Ks, pensions, and golden parachutes, he spent his final years as a modest standout in an Arizona retirement community designed for social security retirees. He was one of the multitudes of unnoticed men and women that are needed to lead a remarkable nation.

The Ideal

In any field of endeavor, the first challenge of leadership is choosing the ideal to which it aspires.

I focus (though not in order) on five Ps in leadership --

Principles

Priorities

Personnel

Policies

and

Persuasion.

The final four follow directly from the first one: the ideals (or principles) you are defending. Persuasion is an essential and challenging skill to foster, but no matter how well you master the persuasive arts, your efforts will eventually falter without a principled foundation.

Whether she acknowledges it or not, a leader has an insurmountable obstacle in successfully choosing and motivating a staff, setting an agenda, or honing and implementing policies in the absence of an idealistic focal point, a clear cause. The majority of leadership efforts veer off track because the cause pursued is not well chosen, defined, explained, argued, reinforced or adapted to the organization and its resources. Paraphrasing Ralph Waldo Emerson: “The person who grasps principles can successfully select their own

methods. The person who tries methods, ignoring principles, is sure to have trouble.”

With so much riding on the first step, leaders must choose their guideposts wisely. But how do you tell a good principle from a bad one? And how do you give an ideal the right size and shape for the institution and its objectives? How does a leader give life and example to that cause, so it does not fall flat in the form of an empty precept?

These are the essential questions I hope to first answer.

When we are born, we step in to a flow of ideas (or ideals if they rise to that level), experiencing them like the currents and eddies of a river. We can examine the current and channel it to good effect or ill effect, but, finally, these ideas move on through history, as we certainly do not. If an idea is nothing more than the aggrandizement of the leader herself, it will die along with her. If the cause is broader, but still sterile, it may endure a generation or two, but will eventually wither on its own accord or with the resulting weakness of its host social organism.

The direction of our lives depends upon which ideas push us through, and, for leaders, which ideas they choose to promote, re-channel or, on rare occasion, create. The direction of history depends on which ideas carry along the most consequential leaders and their followers and is finally determined by the outcome of battles that get joined and won.

Individually or collectively, we can embrace fertile ideas, such as democracy and markets, or succumb to sterile ones, such as racism and totalitarianism. One path leads to a prosperous, progressive and hopeful future. The other leads toward servitude, regression and despair. Fertile ideas are gifts that keep on giving the freedom to create more ideas. Sterile ones, while seductive for a few and often a source of comfort to a broader group, ultimately suffocate innovation, cut off dialogue and lead to failure.

My ambition for this chapter is simple: attune leaders to embrace the fertile and disable the sterile. This objective is part value judgement and part practical advice. A leader can follow a sterile vision just as readily as a fertile one, and she might even encounter more near term success with the former. However, over the span of time and people, the fertility of a leader’s cause influences the staying power of the effort, particularly among

followers. Staying power, in turn, is a crucial factor in success. A leader can overcome any number of ups and downs if her cause is profound and her ideal inspirational. Vain ambitions and dead end causes will wither quickly when fortune looks the other way. Bearing, courage, decisiveness, dependability, endurance, enthusiasm -- in short, many of the personal character traits that define a leader -- are sustained from the wellspring of the cause.

Markets are a fertile idea because they match a constantly changing set of participants and interests in a competitive environment based upon the central notion of exchange. Reputation is the key to functioning markets and a companion ideal. Teaching a man to fish is a fertile ideal. Giving a man a fish (in exchange for nothing) is a sterile ideal. Pretty axiomatic. One would think.

But isn't it natural to want to "simplify" things and bring "order" to a seemingly chaotic circumstances in life? When do you cross the line from helpful simplification and efficiency to totalitarianism? One quick hint: if proponents feel compelled to murder people that are unpersuaded by their cause, it is likely a sterile one. If they say: "It's a free country. I wish it weren't" they are on the wrong side of the line.

Similarly, anti-miscegenation, segregation, and other Jim Crow laws were promoted by governments that just wanted things "to stay the way they were naturally meant to be". A related hint: if proponents are appealing to science or nature in the cause of continuity, it is certain they have no appreciation for either the scientific method or the dynamism of nature and are pushing a sterile ideal.

As the fishing aphorism implies, involuntary redistribution is also a sterile idea. Demand invariably exceeds supply in this kind of arrangement, and any notion of a market breaks down, nullifying exchange signals, communication, and expectation in a society. It is simply too tempting for the politically ambitious to promise to others more of the pie than can willingly be produced by those who must bake it. Confusion, inaction, servitude and despair necessarily follow from forced redistribution schemes.

By contrast, voluntary generosity can be anticipated, encouraged and applauded with a positive impact on society. Reputation theory has a lot to say about how to match the generous with the truly needy -- those incapable

of meaningful exchange as the result of time, circumstances, unfortunate planning or disabilities. Our social order has an interest in encouraging generosity and altruism, but we must be vigilant of the organizations focused on the impetus. Another hint: In all the variations of Robin Hood, do you ever recall seeing him actually give to the poor? You see him take from the rich. You see a rivalry with the Sheriff of Nottingham. You see the party in Sherwood Forest with Maid Marian, Friar Tuck et al. But give to the poor? Perhaps that was marketing hype. It is a myth after all, and myths generally make for good drama, but bad outcomes.

Markets of all types (including altruistic ones) require policing for fraud; however government regulation as currently practiced has devolved into a graveyard of quixotic attempts to modify behavior and slow down the evolutionary process. Eminently well-intentioned and conscientious at their origin, these thickets of rules empower those deciphering them, but weaken more consequential actors, particularly leaders. Increasingly, dead letter rules simply provide cover for unprincipled or self-serving outcomes, sterile endeavors, and the free-riders among us.

Modern regulations also provide false assurances to leaders, who believe they've done something to bring order or progress by simply adding to the verbal thicket. However, for the broader society upon whom the leader depends, they prevent efficient matching of interests as circumstances change, which of course they do. Worse still, many other institutions and leaders outside of government have followed suit, pursuing rule-making strategies that serve as obstacles rather than tools.

In the coming century, leaders need to fashion a dramatically new organizational paradigm if they wish to find success and finish on the right side of history. The good news is that for an increasingly self-empowered and connected world, pre-ordained beliefs are giving way to more choice, and choice is the prime currency of progressive leadership throughout the human evolutionary path.

This freedom, which presents itself in degrees, gives an opportunity for leaders across all divides to embrace ideas that have worked throughout history (such as markets), defeat arcane ideas (such as the caste system), and draw from a wide range of new positive ideas (such as reputation theory) that can untangle the Gordian Knot of our current regulatory paradigm. Choice has always been a major determiner of the human fate.

So far, I have used very simplistic dichotomies to illustrate my point. In daily life, distinguishing the fertile from the sterile is not easy and remains a constant challenge for a leader. That challenge comes in many shapes and sizes.

Misappropriation.

The resurrection of Christ is a miraculously fertile allegory of joy and hope, which was initially spread far and wide by another fertile invention, the Greek lingua franca used extensively by Mediterranean traders. This powerful allegory at the heart of Christianity spawned J.S. Bach's 10th movement (Jesu, Joy ... or his "wedding song"), the tale of Aslan in the literature of C.S. Lewis and thousands, if not millions, of other inspirational moments (that any in turn have spawned their own moments).

And yet many claims on "Christianity" -- from the Inquisition and Divine Monarchies (on the right) to Liberation Theology (on the left) to pure hate groups such as the Ku Klux Klan -- are hopelessly totalitarian and sterile.

"Progressives" were allied at their outset with the idea of progress. Hence, the name. Early forays by the government into policing commercial, financial and labor markets were earnestly anticipated to promote progress in fields that had stagnated due to monopolies, corruption, slavery, and illiteracy. In certain cases, progress was achieved through successes such as trust-busting laws, land conservation, and universal education.

However, progressives veered off course early on by embracing eugenics and other quack science notions of progress. Today, progressives remain adrift. They do not understand the limitations of the government as an organized body and they fall prey to the mistaken notion that science introduces certainty, when in fact it represents the antithesis. Markets provide resolution and progress. Science is and should be about exploration and discovery -- perpetually. Likewise, technology is not the holy grail of progress. It is a tool that can just as easily fall in to regressive hands as legitimately progressive ones.

Unsurprisingly, today's progressives can be among the most reactionary elements in the public debate when presented with paths that challenge an *idee fixe*, such as public unions and single payer healthcare, with more

convincing alternatives, such as educational choice and consumer-centric care. Modern progressives have become as transfixed on illusory, yet comforting, “solutions” in a manner that recalls the cargo cults of Melanesia or other similar dead end organizing principles where false hopes hold sway.

Similarly observations could be made about terms such as diversity and sustainability. These terms can have fertile implications and accordingly broad appeal, but they have often been co-opted by the forces of reaction, sterility, and stasis who get attached to them as ends, rather than the means which they represent.

Diversity -- in ideas, genetic pool, practices, ecology, etc. -- is essential to the human condition. We can never be certain about the next source of inspiration and progress (or just plain survival), so keeping options open is a fertile objective. And yet the mantra of diversity has unfortunately served as window dressing for a more regressive agenda of hampering successful individuals and groups. As with all evolutionary processes, emulation is a far more constructive and meaningful response to success than sabotage.

Sustainability is a similarly innately positive idea. Nicholas Wade argues in his book “The Faith Instinct” that from the earliest of human times rituals and supernatural beliefs, while appearing irrational, created group cohesion. This cohesion enforced, in turn, altruistic norms that were adaptive by fostering ecological sustainability (among other norms). In other words, we have an instinct for altruism-driven sustainability that is linked to our survival.

However, as often as not, leaders have taken these norms and cohesive dynamics in the wrong direction. Wade explores the example of the Xhosa of Southern Africa and the Aztecs of Central America, whose leaders took religious sacrificial logic to such extremes and to such twisted purposes it ultimately destroyed their societies. Potlaches and Kula exchanges were examples of fertile, exchanged-based ideas that organized societies for mutual benefit and progress. Cargo Cults, on the other hand, were sterile mutations of these sustainable exchange traditions, based upon illusory counter-parties that had no chance of appearing.

In short, labels can be -- and often are -- misappropriated. The risk that language might mislead or misrepresent is discussed in the next chapter. Leaders cannot master the situation without mastering the language, and

they certainly cannot have it master them. Language, like markets, are a good servant and a poor master.

Duality.

Misappropriation can be distinguished from duality.

Duality involves an ironic concept -- the simultaneous contemplation of opposites. These dualities are not ideals or first principles, but they are important in the world of ideas and leadership and need to be considered and understood by leaders. Their lives and the lives of those around them are often experienced in a set of dualities.

As Shakespeare understood, the experience of drama hinges on sex and death, comedy and tragedy. One is, of course, fertile, the other sterile. Both live simultaneously within drama, which is a key element of the motivational toolkit of idea entrepreneurs. Similarly, in political life, freedom bears within it the notion of responsibility. In relationships, including that between a leader and those looking to that leadership, distance and self definition is essential for healthy togetherness and engagement. Verification is needed to solidify trust. Individual rights are protected by a social contract.

War is perhaps the ultimate duality that leaders face. Purposeful killing of others is a sterile precept and yet if war is truly the only means to achieve liberation from a totalitarian or other sterile force (and prevent further suffering thereunder), the promise of a liberated future may demand warlike actions.

The most challenging initiatives and decisions leaders face often reside within these dualities.

Adaptation and Evolution.

Successful leaders embrace refinements that can turn a fertile concept into an even healthier one. Good enough can be the enemy of better in a competitive environment.

Profit in a business endeavor is a fertile principle and, not surprisingly, the key metric by which business leaders are judged. Profit can be used to

reinvest in other promising company undertakings or it can be distributed to shareholders, who can take risks to sponsor new, innovative ideas. In any event, profit promises to spawn innovation, progress, and employment through reinvestment. Profit is the archetype of fertility, because without it, your business disappears. With it, the business can thrive and sustain itself. The more you have, the more you can reinvest. You can debate whether any particular subsequent use of profit is more productive than another, but clearly the absence of profit makes the entire discussion moot.

That being said, profit as a guiding principle can and should be improved upon. McKinsey & Company, one of the world's leading management consulting firms, focuses managers not on profit, but rather return on invested capital (ROIC). Capital flows to the highest probability weighted return. Business managers should always be focused not just on the "bottom line", but on where else their capital could be deployed and what weighted risks are involved in generating that profit. Economists refer to this as opportunity cost. Many companies, such as Koch Industries, make opportunity cost, not profit or market share, the guideposts for managerial excellence. If your ROIC is not measuring up in your particular market, you should be focusing energies and resources elsewhere and sending the profit off to other uses.

Conversely, if you are experiencing yields that seem too good to be true for a competitive market, you should re-examine your risk adjustment factor and outcome probabilities. They are probably wrong, and your gambit unsustainable as a result. Over a trillion dollars of mortgage-backed securities were labeled AAA or "risk-free", but they promised rates in excess of then current risk free yields and did not have any underlying characteristics that one might view as risk free.

This should have been a clue that something was amiss in that particular economic gambit.

Repackaging.

The threat from failed ideas reintroduced under new management or a new brand or both is very real. Sterile ideas, persuasively packaged, can serve the near term ambitions of an idea entrepreneur and his cohorts, who are all too human and temporal in their needs. These ideas are not misappropriated, as with the a KKK chapter that might operate under the guise of Christianity.

They are simply resold to the public in sexed up terms after the memories of previous failures have worn off.

Mao Tse Tung promoted a bundle of positive-sounding ideas -- the revolutionary vanguard, agrarian reform, the great leap forward, cultural revolution. Most of these were simply repackaged notions already proven to be exceedingly sterile (if not simply murderous) in practice. However, they served to put him at the pinnacle of power of the most populous nation on the planet until the end of his natural life.

This posture brought many temporal rewards in the form of access to valued resources and dominance (and humans remain hierarchical beings), which is a temptation too seductive for most to pass up.

Cognitive Appeal.

Beyond the alluring packaging and the dubious motives of self-interested leaders, sterile ideas can also be innately appealing. They provide not only a means to acquire power, but deep cognitive allure for adherents.

In this book, I contrast a comprehensive (or totalitarian) organization with a contractual (or limited) one. While those who found the time and inclination to read this far are unlikely to dive headlong in to a one-stop state anymore than they would buy fresh seafood at Best Buy, the idea of getting everything from your healthcare to your job to your school to your commuter transport to your spirituality from one provider does appeal to some. It is also appealing to look to one leader, one personality to guide the outcome, reassure your identity and shoulder the responsibility.

Our lives are increasingly complex. Who knew a year ago that you might well have to become familiar with the esoterica of credit default swaps and bond ratings agencies to make an informed judgment on whom to vote for in an election?

Simplicity, particularly given our consumerist values, is achingly seductive.

Consider how many advertisers reach out to you with promises to reduce the complexity of your lives, to deliver a simpler, less stressful life. For over a decade of our formative years, we are hard wired to extract a broad range of benefits from one pair of people -- our parents -- and the transfer of that

desire to a virtual parent in state form is so cognitively appealing, one wonders how we've avoided the totalitarian scenario as well as we have.

Unsurprisingly, the rule has been the invitation to royal privilege and its totalitarian demands.

The exception, including the American exception, has been the contractual state. By some freak accident of providence, our founding fathers designed a system entirely set out to impede the psychological proclivity toward totalitarianism. The Federal / State system, the three branches of government, the negative definition of state authority in the Bill of Rights. All of this had an express purpose to impede inherent human tendencies to toward *in loco parentis*.

Another very appealing cognitive notion is privacy. What could be more natural than the psychic pleasure of having secrets and feeling uniquely in control of your identity and your self-assessment? And yet, immunity from criticism is one of the surest paths to failure in almost any aspect of life. In addition to promoting personal failure, immunity from criticism has a dismal record in politics, economics and science.

In a mutually transparent world, identity data and aggregated, abstracted personal data can also be of tremendous value to economic entrepreneurs matching up desires with efforts to meet those desires. And how will you get the things you didn't even know you wanted until that entrepreneur finds you.

In certain circumstances, personal privacy and freedom of conscience does have an absolute value. For example, the secret ballot is an essential trust mechanism to avoid retribution and coercion in democratic elections. Privacy and physical security from others and the government -- along the lines envisioned by the 4th amendment -- is essential. It goes without saying that identity theft, credit fraud and password theft (hacking) are zero tolerance affairs that cross well over the line of permissible, even healthy, invasions of privacy.

Reputation theory has a lot to say about privacy. If, when and how you release personal data in to the market place is an essential element of keeping a transparent, market-based system vibrant and effective for matching personal choices.

Bad Plumbing.

No system has ever produced the quality and quantity of beneficial effects as free market capitalism -- a system founded upon and defined by competition, exchange and the sanctity of investment contracts.

However, similar to ignoring the claustrophobia of critical immunity in protecting privacy, wishing away the fragility of effective markets is not going to win the day for ideas that are important to our future. Thoughtless support for ideas, however salutary, is tantamount to no support at all.

It is comforting to believe that no matter what chaff is thrown in to the air of a vibrant market, the invisible hand will guide a positive and efficient outcome. Yet, as powerful a heuristic device as the efficient market hypothesis (EMH) might be, the EMH with its proto-religious imagery is still a tautology that does not itself ensure a valid outcome in any particular market. Markets are fine servant, but a poor master, as Benjamin Franklin noted. As with any system, the garbage in, garbage out rule applies, and the rules of the game need to be respected and enforced to maintain the reputation and efficacy of the market as a pricing and settlement mechanism.

To make matters even more dynamic, serious cognitive fallacies, and outright delusions, often animate individuals that might seek to regulate markets or supply key components, such as a stable monetary currency and protection from fraud.

For all their good intentions, government bureaucracies bias aesthetics over function, uniformity over diversity, process over outcome, doctrine over dissent, continuity over finality, and righteousness over humility. These virtues can mean that public parks are beautiful and neat, red lights always mean stop, trials are deliberate, consensus wins a period of grace, institutional knowledge is sustained, and communitarian values are ensured a voice.

But these virtues rarely serve the vital and dynamic nature of markets. Worse yet, the temptation for government entities to enter the market as participants has a long history of failure and misallocation.

For this reason, we need a new market-centric paradigm that can be understood and championed by a broad set of leaders throughout society. This market ethos and knowledge needs to permeate the society at every level in order to ensure it finds capable voices at those critical times and places.

The ultimate value of learning political and economic history is, of course, that we learn skills to spot the sterile ideas well in advance, before too many consequential adherents push it in to a meaningful flow of history. It is no accident that the fecundity of our ideas and related physical well-being is closely correlated to the invention and promulgation of writing and other communication technologies that allow us to pass along our experiences with successful and failed ideas, alike.

Yes, while it often feels like whack-a-mole with bad ideas, the broad evolution of human development has successfully rid us of many monstrous ideas -- feudalism, slavery, Nazism, apartheid, etc. The arc of history is long, but it bends toward justice.

Many others have scouted the general geography of fertility and sterility.

In the current era, Virginia Postrel explores the dichotomy between dynamists, or those who embrace change, challenge and competition, and stasists, whose instinct for the comfortable and familiar is paramount. Novelist David Brin, a transparency advocate, highlights the need for vibrant criticism and mutuality in successful decision making. Yale anthropologist James C. Scott uncovers the humble diversity and dynamism of metis, or adaptable local knowledge, in contrast to the aesthetic certainty, comforting dominion, and inevitable failure of central authority planning schemes.

Creative destruction is not just endemic to capitalism as Joseph Schumpeter theorized. It is a hallmark of all forms of human advancement.

The late Edwin Friedman, a leadership theorist, contrasts the anxious spirit of regression with the adventurous spirit that invites risk and hence possibility and progress. The Dark Ages were overcome not by a random desire to be enlightened, but by the Age of Exploration and the unavoidable truths unlocked by seafaring experimenters.

Friedman takes his heuristic 500 billion years deep in to evolutionary biology. He identifies a distinction between prokaryote cells (clone-based) and eukaryotes cells (nucleus, mitochondria-bearing). This revolution appeared about two thirds of the way into the existence of cellular life and made possible diversity, infinite variety, and the creation of evolutionary life as we know it. Prokaryote life is persistent, but unchanging. Invulnerability is its priority as cloning presents little risk of mutation. Eukaryotes life is dynamic and evolutionary, biasing toward strength and advancement precisely through mutation, the essence of individuation.

Generations recent and long gone have drawn analogous battle lines.

In the 19th century, advocates of the social compact theory of limited government battled the progressives, who bristled at limitations on state authority in view of the long litany of wrongs that needed to be set right. Only the state had the “power” to force the necessary advances in society they reasoned. The populace acting without that force was simply too unenlightened or self-interested to be the driving party to progressive solutions.

Unfortunately, for each step forward that a state might make, hubris has led it to take two steps backwards by engaging tasks ill-suited to its organizational form. Because of its innately defense / regressive posture, the government has never been a good agent for adaptation and change -- notwithstanding longings to the contrary. By definition, it advances by force of arms. It holds power first and foremost in a defensive and regressive posture and only progresses as an accident or afterthought.

In the 20th century, Hayek and Hazlitt took on the Keynesian notion that governments could forever manufacture a steady and prosperous “boom” through expert currency and fiscal manipulation -- irrespective of real life dynamic cycles of innovation, resource realignment, shifts in values and desires, and the perception of opportunity.

One of hallmark of sterile ideas is the production of false hopes. Included within a litany of false hopes is the notion that life can be free from criticism, competition, change and uncertainty. It cannot.

All of these thinkers would provide a Venn diagram overlap with the fertility/sterility duality discussed here. The fertility-sterility heuristic

applies across the spectrum of idea-centric activity: literature, music, spirituality, business, innovation, strategy or science, but this book is most concerned with non-military organizational leadership -- ideas with consequence as to how organizations, particularly state and state-regulated entities, are run, and how they interact with financial and commercial markets.

Military leadership and strategy is a subject from which many powerful lessons can be drawn for non-military leaders. However, the life and death stakes involved in the battlefield provide such clear direction and obvious consequences that there is a limit to the lessons that can be adapted to a non-military organization. While individual military leaders are often a tremendous source of admiration, respect and knowledge, the traditional military hierarchy also presents challenges when translated to an information-centric, market-based leadership paradigm.

I hope that the approach outlined in this book could be put to some use in the context of modern warfare, where the enemy is more often an idea, or multiple allied ideas, than a uniformed corps of opposing combatants. Accordingly, the need to plan for diverse fields of engagement under a unified strategy in order to vanquish an intangible foe(s) is essential for the success of the modern war endeavor.

A study of leadership in the sports arena or in business also provides great tools for leaders. But winning a ball game and pushing for profits present such clear goalposts that the leadership challenges are more tactical and clear cut. Instead, by tackling arenas where the shifting sands of first principles make it all the more challenging for those who might wish to claim a leadership role, I hope to introduce a dynamism to leadership studies that has not heretofore been explored.

Therefore, an essential touchstone for this book is the role of idea entrepreneurship and leadership in the context of a dynamic idea market. In business, this contest is often fought in the realm of product definition and marketing. In politics, the contest is reflected in the democratic process. Campaigns put forth most obviously the persuasive capabilities of the candidates. Often the bombast of the event media production obscures the underlying notions these idea entrepreneurs are peddling. And yet the ideas are always present, even if they are only by default a cult of personality associated with the candidate.

In the arena of public leadership, sifting through the verbiage to find the good ideas and discard the bad ones is a constant dilemma. Business leaders (very) often forget the golden rule of ROIC and falter in their leadership skills; but there are plenty of mechanisms in place to put them back on track -- stock price declines, takeovers, dissolution and bankruptcy for example.

Self-corrective mechanisms are less common in the public arena. How does an observer sort out what kind of ideas a prospective leader is pitching to them? Why might a sterile idea actually be preferred over a fertile one given the stakes? Certainly, no one ever admits to touting a dead end path. While seduction and solution may be as distinct as packaging and product, in the land of ideas it can be extremely difficult to separate the two.

Moreover, the reality is new fish enter the river of ideas every single day. The passage of knowledge from generation to generation -- through education and learning -- is unpredictable and imperfect, as is the trial and error nature of idea promulgation and implementation. We are all familiar with time worn cliché that those who do not study history are destined to repeat it (or at least forget that it rhymes). And many bad ideas are just too devilishly useful to a handful to ever wash away entirely.

The Achilles heal of any society, therefore, is its ability, or inability, to educate its new arrivals to think critically. That sentence is essential to the worldview of his book. Teaching critical and fertile thinking without sterile inculcation is a tight rope requiring constant vigilance. Like medicine, arts, or politics, teaching requires enormous and fragile “metis” or adaptable local knowledge. The temptation to indoctrinate, in particular, is too strong for many societies to resist in any particular time frame. This is the “what to think” (sterile) not “how to think” (fertile) bias.

Indoctrination ultimately leads to the failure of a society that insulates itself from criticism. While a reboot is always possible, many lives are derailed in the interim. That is the tragedy of history, as such lives lost cannot be recovered. These are the forgotten. The lost souls of history. It is the obligation of every leader to leave as few of these behind as humanly possible.

The balm of certitude and stasis slows the dynamism and fertility brought forth by skepticism, empiricism and the trial and error nature of knowledge

and human innovation. Accordingly faith, as opposed to reason, has a valuable role in the human condition. The need to fill in the fathomless gaps in our empirical knowledge is too great, and the comfort brought forth by faith, not to mention faith's uncanny allegorical relevance, is too important to our survival and the historical flow of ideas. A leader's faith must maintain its modesty, lest it turn to pride and certitude and envelop fields where empiricism and the jostling of elbows might serve society better.

In addition to the temptations of indoctrination, the passage of ideas is hampered by major epistemological challenges. As explored persuasively by such writers as Nassim Nicholas Taleb, several cognitive challenges limit our ability to ascertain cause and effect in markets and hamper our predictive capabilities.

Despite all of the effort put towards understanding price signals, events inevitably belie any successful predictions in the population of markets, including the market of ideas. Determining the relationship between a certain call in the marketplace of ideas and the resulting practical consequences is not an easy or exact science. As anyone who has ever tried to beat the stock market knows, modesty and humility are about the only certain adaptive traits.

This book attempts to work around these limitations by counter-posing idea archetypes that have been seductive through the ages. In some cases, moderate and pragmatic pressures are called for. In other instances, we discuss battles where surrender is not an option. Some battles, such as the battle over language (think Orwell's Newspeak), have a foot in both camps. Near term pragmatic accommodation may be necessary, but only as a means to survive until the next battle can be joined.

Often, sterile ideas produce practical results that apparently trump the more fertile approach, but that seduction cannot hide an underlying life or death struggle. So yes, Mussolini's state fascism made the trains run on time in Italy, but anyone having watched the movie "Life is Beautiful" would gladly be late to that appointment and read the paper a little longer in exchange for erasing that period from human history.

Whether politics is a continuation of war by other means (Foucault) or we accept the original Clausewitz formulation, ideas are at the heart of the matter and represent very serious business. Because of their ethereal nature, it is

very rare for ideas, even sterile ones, to disappear entirely. If they are seductive, like the promise of unchecked power, they have a way of trickling along until someone from succeeding generation unearths what is better left buried.

Bilbo's magic ring from *The Lord of Rings* is an allegory that captures the essence of my point. The ring resurfaces each generation, alluring new bearers and leaving destruction in its wake as it finds its next adherents, servants and seekers.

The ring is finally destroyed in the fires of Mount Doom, but not before Frodo discovered that it is a mortal challenge to dispose of those really bad, but really seductive, ideas.

The Toolkit

Language is the most important tool of leadership, because it is irreplaceable in the contest of ideas and essential to the art of persuasion. Leaders must repeatedly win a contest of ideas in order to proceed to the details of leading and protect the desired outcome. Clear language is also a foundational trust mechanism, because it allows people to communicate with mutual understanding. Hence, it is the most essential building block of any social group a leader intends to lead.

Photography, visual arts, and music generate meaning, mood and sentiment. Math and scientific method promise repeatable outcomes (after many false starts). Money stores value and enables market pricing and settlement. Topology (charts and graphs) is math that is illustrative, persuasive and increasingly useful in our visually-connected world. Non-verbal communication -- "bearing" as the Marine leadership guide calls it -- is certainly important in immediate settings, such as board rooms, debate forums, in front of TV cameras, in presentation halls, and on battlefields.

But nothing matches the vital currency and breadth of impact of language.

Imagine the 2010 health care national discussion without "death panels" or "reconciliation", the 2008 election without "hope" and "change", or the 1992 election without "read my lips". And what about the whimsical "Tea Party" that encapsulates such a broad protest sentiment in an apparently harmless mixture of aromatic leaves and warm water?

Unless you have an orientation in the use of language and its roots, you will quickly be lost in the political forest.

No matter how bright and hard working you might be, how attractive your imaging and demeanor, how clever your graphs and images, ceding linguistic terrain will leave you adrift in idea river without a paddle. Scott Brown in Massachusetts was an attractive candidate -- pickup truck and all -- but when he picked up a journalist's reference to the "Kennedy seat" and corrected it to the "People's seat" his campaign really took off.

From a public policy standpoint, the idea of plain English -- or the ability to agree upon and use common definitions -- is an important trust mechanism and essential to the marketplace of ideas. It is no accident that the foundation of Google is semantic query and not the sterile taxonomies of knowledge prevalent in the 19th century (think the Dewey Decimal System). If you start thinking taxonomy, just remember taxidermy -- all those stuffed, lifeless animals on the wall.

If you cannot agree that the numeral "3" signifies a triple set, then it is obviously a challenge to document and communicate financial value and create any form of market. Similarly, if you cannot master the significance of words, it is next to impossible to build a framework for selecting amongst competitive political ideas. In 1946, George Orwell published "Politics and the English Language", which perhaps as a result of its brevity remains one of the most widely cited essays on the misuse of language in political discourse. "Political language," Orwell states, "is designed to make lies sound truthful and murder respectable and to give an appearance of solidity to pure wind."

Orwell and other modern critics of language and politics from S.I. Hayakawa to Noam Chomsky follow an ancient line of contest that dates to Plato's dissection of the Sophists. At that fork in the road, philosophy, or the use of language to seek a shared truth, parted ways from rhetoric, or the use of language to attain advantage and power, be it personal or partisan.

Of course, that distinction is itself a rhetorical device. But it reminds us that the intention is not to disarm unilaterally or to devote oneself solely to the language of loftier truths and elucidation. That is the job of monks.

Leaders must enmesh themselves in the political process and persuade. Hence, they must avail themselves of all the tools out there as long as they do not set off on a path of misrepresentation, false comparisons, and sterility.

At the heart of the linguistic conundrum is what semanticist Alfred Korzybski phrased as “the map is not the territory” premise, or what Juliet mused in Shakespeare’s *Romeo and Juliet*: “That which we call a rose by any other name would smell as sweet”. As with other communication medium, a word is an abstraction, not the thing itself. And only the dictionary, the ethics of the speaker and the general limits of credulity by the linguistic community bind a word to the meaning a speaker wishes to ascribe to it at any given moment in history.

Hegel set out that meaning is nothing if not temporal.

[Semantic Web – Keyword - Search Google Section -- avoiding definitions, systematizing the social context of language - temporal meaning]

The temporal nature of meaning is apparent in the theatre of politics, where the immediate emotive value of language (or its heat) consistently outweighs its clinical, longer-term utility (or its light). In this very temporal linguistic terrain, a word or phrase that conveys effectively during one campaign or for one audience may not persuade at another moment in time.

This state of affairs may be distressing to philosophers and scientists, but leaders necessarily traffic in emotion. Etymologically, the word “motive” means to move or to act. In politics, for example, you seek to move people here and now from their comfortable seat to knock on a stranger’s door, donate money, influence their neighbor, and, of course, pull the voting lever for you. Action, not contemplation, is at the heart of rhetoric. Successful ideas always contain an emotive component, as do powerful words.

More importantly for our purposes, emotion is as important as insight in leadership.

You cannot win a contest of ideas without first winning the battle of language. An opening in the seam of your linguistic armor can begin to erode your position and your cause. If you intend to surrender on language, you might as well not show up at the contest.

Winning requires both offensive and defensive maneuvers.

You must choose words that support the idea for which you are battling and broaden its field of co-adherents, while circumscribing the reach of the language of a rival. We can speak as well about the language of alliance, but for now, there is enough just to deal with contested viewpoints.

In linguistics, words are deemed to denote (or mark) something specific, yet connote (or relate to) a much broader array of words that provide the meaning to the communication. An analogy with the world of math helps: standing alone, the number 2 denotes twin elements, yet $2x$ denotes twice a variable value, and the equation $2 + 3$ signifies 5. Hence, while “2” is a clear value indicator, the context of its usage connotes a broad array of values, or meanings in the case of language. The aggregate web of those connotations establishes context and subtext for any specific mark.

Of course, words are not the same as numbers. While a word is weighted down by prior usage, it does not hold any of the certainty and consistency of a number. For example, the term “liberal” once identified proponents of unimpeded commercial exchange, and now it identifies with social goals, such as gay marriage. “Progressives” included some good government reformers taking on Tammany Hall and culture of patronage, but now promote the idea of the government as a redistributive agent. Similar observations can be made about any number of descriptors, with many of these terms being literally flipped on their heads from prior iterations.

Linguists refer to the phenomenon of meaning shift as semantic change. This change can be a simple supplement, such as the use of the term “mouse” to denote a computer input device, as well as a furry rodent. Or it can be as complex as the flux of associations surrounding the polemic term “black” -- once used as a simple color descriptor now used in political discourse for individuals of sub-Saharan African ancestry.

An interesting element of semantic shift is that linguistic changes do not happen overnight. Each of the examples above has an interesting and detailed lineage that can be traced with enough time and effort. The word “black” as used to refer to people of sub-Saharan African ancestry replaced the word “colored” with the rise of the radical, socialist “Black Power” movement of the 1960s, which sought to use that specific identifier as a political recruitment tool.

Not surprisingly, academics preferred the more accurate term African American, and you will see this term in less polemical settings.

Mutation of word meaning is impeded by the contextual and sub-textual links that tie it down like Gulliver among the Lilliputians. With words, context is king. The word “context” is itself derived from the act of weaving textiles -- an apt metaphor for the creation of a meaningful tapestry from many single strands of text.

Good idea entrepreneurs pay attention to the text, context, and the subtext of any communication. Use a word or phrase that is too clinical, and while a ray of light may shine, your potential adherents might be easily distracted by more enticing tones and lose motivation to act on that word. Getting carried away by broad, passionate turns of phrase may produce affection and longing, but will result in adherents akin to unguided projectiles, certain only of disappointment once action, not words, are called for.

If your usage pattern is too stale, you may fail to satisfy the desire for novelty inherent in entrepreneurial promise and contain that element of the unexpected that will catch their attention. However, if you are too far out ahead of the usage curve -- meaning too creative and reaching in your use of language -- the only action you might evoke is head scratching.

Semantic change is a dual edged sword for idea entrepreneurs. They should be highly attuned to semantic change and be prepared to deftly parry parties pressing for change (often by using their own word usage against them), yet the more fixed the meaning you present on your own accord, the less susceptible it will be to being upended.

Orwell and other critics of communication often use the term “concrete” to describe effective language choice. This is an interesting turn of phrase, which I take to mean that the sign and the idea or thing are locked together, as if transfixed by concrete.

Your college writing instructor undoubtedly spoke of using lively visual imagery – choosing words that immediately bring to mind a specific, unshakeable mental image. Again, all of this points to language that is minimally susceptible to semantic change and provides a strong foundation for communication.

Numbers are about as concrete as it gets, and every parent has learned the effectiveness of the “countdown” in motivating children to act. On occasion, I’ve just started counting without even providing instruction and my kids will go on the high alert to figure out what righteous thing they should be doing.

Evocative imagery and clinical precision is a fine tool for philosophy, literature, science and kid management, but the language of moving adult audiences to action has some additional, often conflicting, demands.ⁱ For example, identification for adult audiences is an essential rhetorical device, and the broader, more mutable, the semantic context, the greater the ability for your audience to self-identify. Creating the self-indulgence of self-righteousness has strong cognitive pull, and politicians often seek to define a broad “us” and a narrow “them” upon which to base indignation.

But “Us” versus “them” is a seductive, shallow grave for the forces of reason. Indignation is notoriously effective for creating heat, while reducing the amount of light on the topic. Masters of self-righteousness surround us. From Rush Limbaugh to the Huffington Post, we are often being sold a very polished sense of superiority and certitude. You need to use the tools of rhetoric, without abandoning a foundation of reason. This is not easy, but it is essential for leaders hoping change minds and gain adherents in the marketplace of ideas.

If you cannot draw on the force of rhetoric, you cannot win the argument. If you cannot win the argument, your ideas will never carry the day. If your ideas do not carry the day, they might just vanish into the past.

Fortunately, you can use a concrete term that also carries emotive currency.

You can use an evocative and visual word that elicits broad allegiance. And, perhaps more significantly, you can replace a word that courts advantage for the opposing side with one that is fair in its description, but does not carry their water. The French term “le mot juste” to describe that perfect word for the moment. In addition to a notion of accuracy, the term “juste” in French alludes to fairness, ethical correctness, and moral justification, which brings us back full circle to Kant and the intrinsic need for ethics in linguistic expression.

So leaders must pick words that are clear, accurate, ethical AND pay homage to the rhetorical arts.

Likewise, leaders cannot countenance an opponent's misuse of language. If your rival employs broad and vague language, such as "hope" or "change" to gain adherents, press them on specifics: "hope in what?" "change in what direction?". Any reply is likely to narrow their field of appeal, even if they experience the immediate satisfaction of an answer. Make sure to move quickly along as though you got the answer you were looking for (even if it is not). The more you narrow the field on them, the broader your potential field will be.

If they want to call red green and green red, do not let pass by the opportunity to accuse them of doublespeak. If they call a 5% budget increase instead of a 10% budget increase a "cut" in spending, do the math from the old budget to the new one, and question what "new math" they are employing to use the word "cut". Even if it does not appear to score an immediate point, it will sow self-doubt and cause them to put some semantic processing to work establishing a credible lexicon.

If they resort to euphemism by claiming money you perceive to be wastefully spent is an "investment", then invoke the strong connotation there'll be no "return" on that investment. If they rely on the technique of obviousness in stating a problem ("Our bridges should be safe") propose to them an obvious solution ("Let's make sure toll fees are used first to assess and fix bridges before being spent elsewhere") that comports with your ideals.

They have the choice of what words they use, but you have the power to wrap that incident of text in the context and subtext of your choosing. Remember the meaning of a word is as much about the web of its connotations, as about what it denotes. You have more power over the latter than the former. They can say 2, but you can say $2+3=5$, thus creating the web of meaning you wish to attribute to the other side.

On the other side of the ball, the more concrete your terminology (or the more fixed its semantic meaning free of connotation) the less susceptible it is to meaning shift imposed by your opponent. As an example, in the previous Presidential election John McCain was able to simply co-opt the term "change" (he could have done it more immediacy and success than he

did) from Barack Obama, whereas McCain's campaign tag line "Country First" was so concrete and presented a prioritization that it elicited little more than some grumbling from the other side. Arguably, McCain traded off rhetorical breadth for precision in that instance, as evidenced by his later desire to reach out for new themes.

Similarly, there is no reason to abandon logic or lexical reasoning in your quest for rhetorical advantage. Logical incoherence and non-sequiturs often drive the reasoned mind haywire, but they need not and should not. Emotion has its place. Illogic has its uses. But do not succumb to it. Recognize the power that poetic turns of phrase have and do not under any circumstances let it get under your skin. One of the tried and true rhetorical tactics is precisely to throw logical sand in the water. The earnest amongst us often stammer and halt our thought mid-stream when faced with non-sequiturs and stretched metaphors.

If you want to win the battle ideas, relish the other side's illogic.

Illogic may be red meat for true believers, and may influence the pre-disposed, but it rarely sways undecideds. When faced with an illogical flourish, you can only lose when you lose your cool. Tactics in these instances are essential. You have three choices: fight fire with fire, launching a senseless counter-salvo that just might equally confuse your adversary and embolden your adherents. Fight fire with water, trying to put the flame out with cool reason and explanatory afterthought. Or, use a personal favorite: applying a rhetorical accelerant that reverses the narrative or hoisting them by their own petard.

Each response has a time and a place to work for maximum effectiveness, although if the opposing narrative you are battling is particularly sticky, the ONLY alternative you may enjoy is to work with the tools on the table provide a counter-narrative that navigates to a conclusion that is favorable to your cause.

Take the example of the rhetorical fuss over President Obama's association with the university set, prep school radical, Bill Ayers. This association raised concerns about his judgment in choice of acquaintances and had implications for his philosophical grounding. Perhaps Tony Rezko was perhaps more problematic on that score for Obama; but Ayers, having sought

out the limelight decades earlier as a bomb-setting, angry child of privilege, was better copy than Rezko, a garden variety influence peddler.

When Hillary Clinton first raised the Ayers association in the primary campaign, Barack Obama replied with his trademark rhetorical magic that it was not appropriate to evaluate him based on his association with a person who “committed despicable acts when I was only 8 years old”. This response was illogical in the sense that it was his association and judgment at 40, when he knew Bill Ayers, not 8, when he did not know him, that was at issue.

However, President Obama’s counter-parry was effective rhetoric, as jostling the ordered chess board pieces with a non-sequitur is certainly an alternative in a challenging turn. The phrase was all the more clever, as it combined an emotional appeal to the innocence of youth, a measure of indignation for acts so bad they were apparently unmentionable, and an implication (due to the time reference) that the obscure criminal in question had reformed or otherwise paid his debt to society -- which in this case was not true.

However, illogic also draws attention. It harbors enigma, raises curiosity and invites questions. It can be effective if you want to draw attention to a matter, but ill-advised when you do not. Under other circumstances, that might have been problematic for Barack Obama; however, enough sympathizers populated the reporting classes that any inconvenient and over-extended efforts to sort the logic from the illogic were initially muted, until ...

When Senator McCain chose (with some help from the New York Times) to follow up where Senator Clinton had left off on the topic, he commissioned his running mate, Sarah Palin, to open door number one -- the fighting fire with fire approach.

In an equally illogical rhetorical flourish, she accused Barack Obama of “paling around with terrorists”. Already no stranger to getting attention, Palin’s challenge engendered a firestorm around the once obscure debating point. The questions raised were significant. Who is the terrorist? What were the acts in question? Does he really fit within the definition of a terrorist, particularly with its vast array of us/them cultural connotations? How do you “pal” around with a terrorist? In a cave? In a café? In a brownstone? In a graduate seminar? And certainly, whatever one might do

with a terrorist, it is not piling. The statement made made no sense, and that was the point. It was an attention-getter for a struggling campaign.

But attention-getting can be a distraction if you actually have a point to make. Was it a cheap choice of words? Yes, “Terrorist” has a decently precise semantic cognate: an aggressor whose objective to “terrify” – particularly non-combatants -- rises above other legitimately realizable objectives. Bill Ayers might fit that bill, but the word is burdened with far too many connotations to be used with any precision, and Ayers activities were not even referred to by that term at the time he was doing them. It is a rhetorical grenade in an arena of sniper bullets. And “pal”, while eliciting an ironic smile among adherents, lacks credibility to sway the unconvinced. As an attention-getter, it was effective. In a world where a swath of the reporting classes was motivated to fill the logical gaps, it might even have been a successful tactic, but this was not the world of 2008.

An effective leader would have proposed alternative two (cooling water) or three (narrative accelerant). The cooling water of reason would have simply referenced the New York Times article on Bill Ayers that opened the door to the topic a few days earlier, and asked for an explanation of why the affiliation does not reflect poor judgment. Certainly, this is not someone you or I would choose to associate with at 40 years old unless new facts come to light about this person. “Please explain those new facts for us” would have been a more tactful path.

This would have been dry and effective, though not particularly dramatic. Perhaps, it would have generated attention and elicited a response. Perhaps it would have fallen on deaf ears and the issue would have receded quickly from view. Perhaps sensing points had been scored nevertheless, Obama threw even more sand in the water related to the topic during the final debate when he provided more details on his work with the unrepentant criminal, including the fact the board they served on together had some Republicans on it – that is, he must have been redeemed. [ENDNOTE 3]

Alternative three, the accelerant, may have been the more effective. Working with the original illogical, but effective, Dickensian narrative of the 8 year old and outlaw (Recall the “convict” from Great Expectations), Obama’s opponents might have tried: “I’m sure that when my opponent was 8 he was an innocent kid, but at 40 years old, after 20 years in the bowels of Chicago politics, I doubt innocence explains his association with his

unrepentant acquaintance. Perhaps there is a more believable explanation out there. And does he know why Mr. Ayers has never even apologized to his victims?” This is fighting subtext with subtext and winning. The logic is incontrovertible, but the rhetorical approach is dramatic, enigmatic and properly begs the question of guilt and innocence, which as we know from the plethora of TV dramas is a successful dramatic orchard to harvest.

Never go in to the battle of ideas without a flexible and sizable toolkit of the trade: words, logic and rhetoric. A very helpful online tool is a visual thesaurus, which along with Dictionary.com, Wikipedia.org and the traditional web search (Google, Bing, Ask, etc.) can provide a surprisingly effective foundation in semantic meaning both in terms of denotation and connotation.

Of course, speaking and writing are significantly different acts, and when you are in an conversational medium, you need to either have some anticipatory answers ready to go, or be awfully quick on your feet. Most opportunities to counter-salvo are fleeting and the chances of you hitting the sweet spot low without practice.

The best foundation for using both rhetorical and clinical turns of phrase is built upon the substance of the ideas that motivate your perspective.

Not unlike winning any battle, the justice of your cause relates to the longevity of your effort and likelihood of success.

The Paradigm

Markets -- whether commercial, financial, or political (e.g. for leadership roles) -- give us two essential elements of exchange: price and settlement. A functioning market also provides a forum for a contest among ideas, the outcome of which promises progress. This progress comes not only from the presence of competing alternatives, some of which are invariably better than others, but in the urgency to act and move along to the next decision point.

Markets are all about action. They entice our emotions to act because of the drama of dueling hypotheses and the catharsis of resolution. However, their inevitable consequences can also challenge us to the point of withdrawal. If possibility is the fuel, consequence is the throttle. The twin tyrants of Wall

Street -- greed and fear -- reach very deep into the fight or flight fulcrum in our psychology.

Keynes alternately praised and disparaged the “animal spirits” that enlivened markets. In his near-Victorian environment, it was difficult for Keynes to see rationality in emotion. Reflexively, he sought refuge in the calm of a wood paneled study and the symmetric corridors of a bureaucracy. However, for all the outward symmetry and order of a bureaucracy, a final resolution is often the last think it wants to produce, particularly if resolution threatens the very existence of the organization and its actors. Very often, a bureaucracy’s instinct for self-preservation (and other flaws) create anything but rational outcomes -- as Franz Kafka craftily explored.

Buy contrast, a market’s emotional barometer points to an essential (and rational) purpose: it creates a moment to moment accounting of the health of any hypotheses: the price of gold against the dollar will rise, the Kindle will outsell the Nook, the share price of Microsoft will fall, the price of a ten year bond will rise. An exchange based upon an hypothesis points toward progress by concluding the decision process and beginning the proof of concept. Everyone has an opinion. A market’s role is to (eventually) reward those whose viewpoint proves correct and punish those whose direction proves wrong. Animal spirits get us off the couch and in to the arena to see who is talking smack and who can really deliver.

A healthy commercial market in mobile operating systems tells us via sales figures how Android is faring against Palm and which one should gain our favor. A well functioning financial market tells us via share price whether we should believe more in the future of Microsoft or Apple and which leadership team should get access to our investment dollars on more favorable terms. This challenges other market participants to step up their game or retire from it.

Similarly, free and fair election contests set the direction of our public policy and allow us to evaluate performance against promises for the next review cycle (much more on the free and fair part later). Pressure to act resolves contradictory viewpoints, and that is essential for societal progress. Not surprisingly, this is the stock and trade of leaders.

The coincidence of time and value in a market provides price discovery and settlement. As with any dramatic high point, acting under time constraints

and consequences impacts decision-making. An inconvenient visitor? Quick. Duck under the couch? Or behind the door? Any decent dramatist understands, the power of drawing observers into your character by sharing the choices they need to make when the clock ticking.

Given the centrality of markets in building human civilization and the rewards for successfully navigating them, it is not surprising that we are adept at calculating possible outcomes in real time and making pretty good decisions in the aggregate. Notwithstanding the fascination some behavioral economists might have with decision anomalies, there is a general consensus that our subconscious is surprisingly adept at accurately calculating possible outcomes in real time when something vital is at stake. Francis Fukuyama goes with the eighty-twenty rule, which seems as good an approximation as any -- at least enough weighted toward a positive outcome to dissuade those inclined to throw traditional economics overboard out of frustration. Instead, they should instead put in the hard work to fine-tune the variables and hone the output. One should never let perfect be the enemy of good.

We should be more confident in this gift, which can produce surprisingly efficient collective judgements. For those content with the judgement of the ages, perhaps this confidence comes naturally. For the rest of us, the repercussions of being proven wrong are always a tough social nut to chew. The psychological hesitation to enter the market fray -- more specifically, to face its possibly negative judgment -- is a key driver for many who seek an alternative catharsis in "regulation".

Derived from the notion of ordered, sequential repetition (e.g. at regular intervals like marks on a ruler), regulation does not seek resolution or finality. It is inherently process for process sake. It comforts as a heartbeat comforts. And it ends as involuntarily as a heartbeat does. It may measure, but mostly for the government to take stock, not for individuals to exchange stock, compare possible outcomes, and move forward. Given a choice, regulation is a time piece, not a stop watch. Is regulation more "rational"? Perhaps in process, but not in outcome. Reasoning is not the same as decision-making. And all the reasoning and rules in the world do not move the pieces on a chess board or decide the next tournament pairing. Only action makes that happen.

This is not to say rules of the road are unwelcome. Markets are inherently competitive situations, and we are hard wired do just about anything to win a

competition - no matter how superfluous the reward might be and how dastardly the tactics we employ. We are hierarchical beings by nature and being on top provides its perks. While the social allure for healthy, well-functioning and fair markets is powerful, and a strong sense of social belonging does provide motivation, the individual instinct to cheat in order to come out ahead has an equal, if not greater, pull, particularly in the atomized society we have constructed.

This is where reputation theory -- and trust mechanisms, in particular -- are essential to delivering valid outcomes.

If a market has too many disreputable elements, it will fail to produce a valid outcome. Without valid outcomes, participants leave and any broader benefits from the markets are diminished, if not extinguished. Moreover, one or two bad apple can spoil the bunch when it comes to a market. Once a market's reputation is gone, it is a challenge to revive. Usually, an entirely new market must emerge. While new, more productive markets invariably arise in time, those interim periods can prove long and painful for people seeking an exchange. As mentioned, exchange and proof of concept also supplies progress, and so progress is naturally diminished in those periods of failed markets.

Frozen commercial and product markets slow consumer spending and delay product innovations aimed at early adopters and others that move the bar. Frozen financial markets mean capital gets "stuck" in existing investments and is not recycled and relied upon to fund new opportunities with a higher potential for return. Frozen political markets stymie obvious and necessary public policy course corrections. Eventually risk taking and innovation stall and the detriment falls on current and future generations. These consequences are not lost on the social side of our nature, which pines to make a lasting difference in face of the reality of our own mortality -- in the end every winner finds themselves at the same place on the finish line.

Therefore, rules are required. But rules need their own rules and that is where this section makes the heart of its case.

While rules are needed in order to validate outcomes, rules and outcomes are distinguishable. Once rules (and certainly rulers) seek to determine outcomes, they overstep their bounds. Like a referee with an eye toward one side or the other in a sporting match, players and spectators are ultimately

demoralized and turn away -- even when one side is temporarily pleased by a particular outcome.

So realizing that rules about rules are important what type should we look to? How do we keep from creating rules and rulers that overstep their bounds, thereby limiting, if not eliminating the benefits, of functioning markets and arresting human progress? This is the most important -- and least asked -- question among policy makers, and it is the reason I took the time to write this book.

Keeping with the sports analogy: contests are most successful when the rules are simple, easy to discern, and readily verifiable by officials and spectators alike. Complex behavioral directives that require expert interpretation often create as much drama off the playing field as on. No one would deny the athleticism of ballroom dancing and figure skating, but the resolution of these expert judging contests is invariably fraught with more controversy and drama than say ice hockey or pole vaulting, where the guidelines are simple and easy to verify.

Similar rules apply in the marketplace: quarterly, product sales figures are easy to translate to a stock price variance. Lengthy court proceedings are a challenge to price. FDA or other approval? Pure option value.

Dramatic suspense might be good to retain spectators, but it is bad for market participants, who are best served by a swift resolution of competing proposals. Therein rests one source of tension in the system. As markets become open to public scrutiny (generally a good thing), the interests of spectators begin to weigh more heavily on the process, and the possibility of drama overtaking resolution increases.

There is no easy solution in this instance, but rule makers do have to be sensitive that the self-interest of spectators not outweigh the objectives of the participants. Organized contests, such as sporting leagues, that are funded by and intended for the spectators themselves present a useful comparative case study. Leagues painstakingly seek to even the playing field in order to increase the dramatic appeal of the event and draw in spectators. No one wants to watch one team clobber consistently another.

Of course, leagues also cannot be perceived as rigging the contest, because the entire allure of the moment comes from some very real uncertainty around the outcome and the catharsis of a resolution of the tournament.

So why does the urge toward regulation persist in the face of much simpler alternatives? Like the allure of open markets, the explanation rests deep within our psychological make up.

Process, regularity, repetition can be just as much a mental drug as the thrill of the possible and the catharsis of a clear outcome. If free marketeers lose their bearings through hyperactivity or as outcomes produce puzzlement in a “free” market gone askew, statist fall for the opiate of regulation -- however ineffective, counter-productive, or illusory that promise of predictability and hope of the illusory might finally prove to be.

Behavioral economists often stumble in to this trap. After uncovering all manner of oddball evidence pointing to an inability to safeguard our own own economic self-interest in a market environments, many behavioral economists then turn and run headlong into the arms of rule makers (particularly government-empowered ones) with scant analysis of what cognitive fallacies and deeper interests might delude or belie these efforts.

Between life tenure, sovereign immunity and a monopoly on the legitimate use of force, state rule makers in particular have a near limitless capacity for self-delusion. In addition, they inherently favor processes that might delay or impede clear outcomes, accountability or other threats to their tenure. Idi Amin, Stalin, Saddam Hussein, Mao Tse-Tung, Kim Jong Il and other id-driven psychopaths are more historical norm, than exception, given the structural biases of state organizations. And, of course, at the lower echelons you find numerous examples of functionaries “going postal” when any threat to their station or (often delusional) expectations are frustrated.

In a market-based, transactional world with contractual sanctity, a fool and his money (or power) soon part ways. This is simply not the case in a realm where consequences are removed from actions, which is the case with most state-sponsored regulatory endeavors. Our government has managed to build impressive edifices that skillfully evade any notion the public might have of enforcing accountability.

Not surprisingly, it can take its own form of madness and immunity from criticism to confront tyrants, small and large, who often have long tenures as a consequence of inaction. Thomas Jefferson referred to a class of citizens who might prefer the calm of despotism to the tempestuous sea of liberty. Call this the person in Chicago living under a man by the name of Daley for the last [50] years. Of course, being resigned to one's fate with a despotism focused on potholes, parking tickets and parades is a lot different than throwing in your lot with a despot responsible for the national economic well-being and security when financial printing presses and nuclear weapons are involved. Not fighting city hall may be an option, whereas surrendering your country is simply not.

Predictable, time insensitive, repetitious, unresolved. Virginia Postrel refers to these sentiments as stasist in contrast to dynamist. But this is not just a matter of ideology - conscious or unconscious. The cognitive allure of regularity is powerful -- both for those in power with no interest in being unseated or those otherwise perfectly content with their lot in life and little interest to see challenge or change. Inaction and immunity from criticism are precisely what markets and their political analogue, elections, were conceived to replace. Not surprisingly, the advancement of human civilization has been closely tied with the development of both.

The genius of democracy and fountainhead of its fertility, is not that it consistently chooses the finest in its leaders with great deliberation. Trial by ordeal (or perhaps the first hundred people in the Boston phone book as W.F. Buckley quipped) may serve that purpose better for all we know. Democracy occasionally produces remarkable people by chance, but, more importantly, it can be counted on to replace choices that have veered so far off track that an apparently cost-free action (voting) is finally understood to have punitive consequences. Of course, with such distant consequences, it is questionable how much rationality is ever engaged and whether politicians are perceived as anything more than discretionary luxury items, which present their own challenges to market theorists.

Given democracy's essential benefit, it has not been lost on good government types that term limits are an example of a trust mechanism that should be put in place. Without such limits and other trust mechanisms, it is simply too easy to rig the system, once you gain control of the levers of power. As one Islamist in Turkey stated recently: democracy is like a trolley car: you stay on board until it is your stop.

And terms limits may not be enough. As gerrymandering in the State of California has proven, you can ensure incumbency re-election rates are in the 98%+ territory with tax dollars recycled through public unions in large amounts to fund objectives that are about anything except accountability and consequences. Similarly, the genius of capitalism is not that it produces the most exquisite products (medieval indentured court artisans might well have done that), it is its ability to reject really bad value propositions, such as the Pontiac Vibe.

The larger question today is: why does American Idol -- a tournament for random singers of sappy cover numbers that has produced a string of hit makers -- work more effectively than the more consequential American political system or the multi-trillion dollar world capital markets and their insurance brethren ?

Why have good markets gone so bad? And how do we fix them ? In simple terms, as economist Raghuram Rajan has noted: plumbing matters.

By most measures, broad swaths of the financial markets are in deep dysfunction. With the advances in communications technology and electronic trading, we should expect that public markets would be increasingly open to smaller companies that foster innovation, offer attractive risk reward characteristics, and have historically outperformed their larger brethren over decades. One would also assume that democratization of the markets would have a full head of steam with an army of investing Davids swarming over bureaucratic goliaths, such as Fidelity and Merrill Lynch.

And yet, the opposite has proven true.

Companies under a \$1B market capitalization traded on public equity markets have seen declining trading and interest in their shares. Over one third of the stocks on the over-the-counter exchange are trading below the amount of cash they have in the bank – even though many are producing positive cash flow.

These companies are -- in the eyes of the market -- worthless, despite their absence of leverage and the ability to produce above average returns for investors. Moreover, the price-to-earnings-to-growth ratios of a broad group

of growth stocks are a fraction of the integer taught in every finance course. These markets are dysfunctional because fear breeds fear. Buyers stay away because they are fearful there is no one to sell to. Sellers remain on a hairpin trigger, because they fear the exit doors will close at any moment. There is no trust. No one of sufficient reputation to provide a counter-party.

Certainly, many retain a long term view and are content with their overall position and prospects if their entry point was low, but this is not how public investors are traditionally benchmarked. The peer pressure instinct and the rise of the exchange traded funds (ETF) has produced a remarkable correlation between the movement of individual stocks and the movement of the overall market. In July of 2010, this sat at over 80 percent -- a stunning figure that has made the public marketplace all but irrelevant as a pricing mechanism for individual stocks. Without a reliable counter-party on the other side a transaction, it is impossible to have a properly functioning market.

The dysfunction of the public equity markets is matched by a variety of disconnects in the vast private markets in equity, debt and derivatives. In September 2008, a deep fault line between the face of risk represented by the nationally-recognized statistical rating organizations (NRSROs) and the calculation of risk offered by the private credit default swap (CDS) market set in motion an unprecedented challenge to the solvency and credibility of the entire worldwide financial system, including many state-run banks.

At a critical moment, the short term credit markets emitted high decibel signals that a broad international network of financial counter-parties were not to be trusted. Their reputations had been torn to shreds, and with that failure of confidence, the broader financial markets rapidly sought to re-price expectations.

A variety of attempts have emerged to explain the financial meltdown of September 2008. As the pertinent facts slowly emerge, we need to consider the elements of the crisis and understand how they might impact marketplace theory. The first misguided narrative was that the meltdown was the result of “market failure” and “deregulation” where Wall Street operated with reckless abandon. Others point to the Community Reinvestment Act (CRA) and a series of government actions over the last several decades that put increasing pressure on lenders to reduce credit standards, while the Federal Reserve was simultaneously pursuing a low rate

environment and the environment encouraged more creative financial instruments.

Considering that the heart of the crisis rested with highly regulated or government-sponsored entities (AIGs, NRSROs, GSEs), this latter version is perhaps closest to the truth; however, both narratives are fragmentary and fail to point to any direction for the future.

There were several markets in question, but the proximate culprit (the market for inter-bank loans where risk premiums soared and inter-bank credit froze) worked as one would expect to the extent it predicted the probability of default on securities that had not been adequately reserved for -- thus impairing and implicating the solvency of entire financial institutions as counter parties.

Many of these counter-parties were, in fact, tightly regulated or government-sponsored entities that were deemed safe and yet market indicators told us otherwise. They were headed off a cliff -- at least one constructed by accountants. The question follows: why were defaults inadequately reserved for? What was the source of the over-leveraging of the financial system? Were illiquid instruments properly accounted for given their most probable cash flows to maturity.

Was this binge truly a market failure and an outgrowth of unchecked capitalism, as some have breathlessly proclaimed. Or was it the product of the moral hazard represented by a handful of "too big to fail" institutions trafficking in securities made "risk-free" in no small part by a sclerotic, government-mandated oligopoly, government market makers, and well-protected political fiefdoms?

Further, how do you assess "market failure" in the market for sub-prime mortgage securities when a critical counter-party was the government itself? Is the government ever an unvarnished market participant so long as it enjoys sovereign immunity and pursues non-market policy objectives as it did by participating in the sub-prime market? These, and other, questions about raise important questions about fostering effective markets.

The benefits of functioning markets as pricing and settlement mechanisms are generally obvious. One only has to look at websites like Intrade and other sui generis efforts to create a market dynamic to see how brilliantly

markets can get up and running in moments and offer an approximate value of anything from pork bellies to the likelihood of an election outcome.

Nonetheless, the term “free” applied to markets is a misnomer in many ways. As Milton Friedman loved to point out: there is no free lunch. While it is good to imagine a world of wide-open, unimpeded interchange, effective markets require many elements that have a cost -- in time or money -- that must be paid by someone, somewhere along the line. Negotiating and settling on an effective cost-allocation arrangement is a crucial foundation for any market exchange institution - be it formal or ad hoc. Equally as crucial is retaining the ability to modify the arrangement as technology and regulatory externalities shift the often delicate negotiated balance previously established.

The first unavoidable cost is recruiting, vetting and training participants in the market. I am not referring to observers who have more stake in the drama than the outcome, but participants who win or lose on a daily basis based upon the outcome. This might not be a high hurdle with American Idol, where the ability to have an opinion on a singer of an existing popular song (and text in your two cents for literally two cents on your mobile phone) is not a high hurdle.

But let's move to the next level in the same commercial arena: judging new musicians and new songs that have not yet had wide distribution and are looking for a hundred thousand dollar investment in the form of a record deal. Malcolm Gladwell explores in some measure the cost and consequences of getting a trained ear in music, and he counter poses the casual listener with the expert listener. Presumably, before a song is popular, it takes some additional training to pick the next superstar or hit song out of unknown line up. This training takes time and adds costs to an effective marketplace for new singers.

In some manner those talent scouts (known as A&R reps) need to be identified and supported in order for the production of new music to be a functioning business. Arguably, the success of certain sub-genres of music, such as American country music, is built on a foundation of talented market makers and participants that get accordingly compensated somewhere along the line. The streets and alleyways of Nashville teem with aspiring songwriters and musicians offering up their best in the artistic equivalent of a jousting tournament. Other genres may not have successfully built this

ecosystem and the market may not produce results. [research country music business]

Now take this up several notches to the analysis and selection of securities that are in the trillion dollar stock market -- particularly predictive modeling of financial results which forms the basis of pricing analysis and results in large investment allocations by institutions and individuals. In addition to understanding the basics of accounting, business, and financial transactions, a market participant might need to be a vertical industry expert and have an opinion on whether or not indium phosphide or lithium niobate is going to be the substrate of choice for the next generation of tunable lasers used in telecom network applications.

How many people do you think can fit that bill? Not many. And how much money does it take to train and put that person in place? A Boatload. And that is before you even count the cost of licensing, certification, monitoring, continuing education and access to otherwise sensitive and valuable information flow.

As a result, in an effective market there is invariably a tension between openness to, and indeed a need for, new participants and the wisdom of the crowds versus a requirement of clubbiness -- or the need for a reputation infrastructure that excludes disreputable, uninformed or illusory counter-parties.

This market requirement for effectiveness is very distinct from the arcane regulatory rule by experts embraced by progressives, Keynesians, and other adherents of the church of 20th century "progressivism". The market dynamic this book envisions is more akin to a gladiatorial contest among those with something valuable at stake, which encourages them to be informed -- again, nothing parts ways quicker than a fool and his or her money. As we saw with the recent financial crisis, hyper-leveraging, insurance providers of questionable solvency, and dissolute and wayward sovereigns are examples of illusory counter-parties that can despoil markets.

Resolving this tension and right-sizing participant vetting for the quality of the opportunities the market represents is one of the arts of making an effective and solvent market.

Certainly, you can count on a healthy dollop of self-interest to motivate learning in market participants -- particularly in financial and commercial ones -- but discouraging transactional apathy through transparency, accountability and the freedom from misrepresentation is a key element in creating an effective transactional infrastructure.

Once again, plumbing (and plumbers) matter.

Markets are like any other business: they must manage the allocation of resources and provide an effective service at a price above cost. This is an art that must constantly be fine-tuned in light of a number of ever changing factors. As with any such area, regulatory regimes or licensing schemes that are heavy on static behavioral rules and byzantium gotcha clauses are far less effective than a simple set of transparency and disclosure rules based upon trust mechanisms and reputation theory.

In the case stock analysts this is accomplished by requiring disclosure of personal holdings and mandating attestations on research reports. In the music industry this might be disclosures related to payola at radio stations and other practices that might deliver us from noxious tunes, and with political journalists this would suggest disclosure of their voting history and paid promotional efforts in the political arena, so as to deliver us from skewed agendas.

The need to sustain clubbiness should not be viewed as a repudiation of the Army of Davids concept, in which the plummeting cost of collecting, organizing and distributing information promises to make everyone a citizen journalist (or music critic or stock picker). But even the most ardent flat world believer, recognizes the need for paid professionals, who can devote time and effort to ferreting out complex truths. The tension between openness and clubbiness simply implies a moving baseline as technology alters the landscape and dramatically reducing the costs of recruiting, informing and policing market participants, while, in theory, empowering paid market participants to do a better job under increasing outside scrutiny.

In fact, if you do not see the costs in a market rationalizing (following a cost curve downward as compared to the value of the market), the likelihood is that something is amiss elsewhere in that market. Layers and layers of cost built up on a market is an indication of mis-regulation, rather than a cry for more regulation.

And this, of course, is where we find ourselves in the stock market after a decade of mis-regulation by Washington in the guise of “reform.” Spitzer, Sarbanes, Oxley, Frank, and Dodd. All well-intentioned. All on a mission to change human behavior for the better. All ignorant of the underlying power, necessity and fragility of markets and the simple tools necessary to make them work effectively. Moreover, they are sadly and strangely unconcerned with the actual impact and unintended consequences of governmental actions.

On the other hand, many free marketeers harbor an implicit illusion that markets are free. Markets have many cost that must be borne somewhere along the way. As effective as technology can be at reducing costs -- and as promising as transparency might be at providing raw data -- neither will eliminate the need for professional market participants (that cost something) to create priorities, match participants, bend the bid and the ask together, and sustain the vibrancy of the market.

In addition to the cost to establish and designate counter-parties in an effect market place, “free” markets are rarely efficient in a practical sense because they are readily susceptible to manipulation and fraud.ⁱⁱ Yes, markets are efficient in tautology, i.e. markets efficiently reflect all the information available to the market, so the efficient market hypothesis (EMH) is extremely useful and certainly foundational from a heuristic standpoint.

Policing markets, however, is another matter. Plumbers can be expensive and so can the police. Here we have yet another cost of the marketplace – policing. Any effective market must solve the question of who pays the cost of policing and how to police the police. Quite apart from the cost question, effective markets, and certainly truly efficient ones, are far more difficult to achieve in practice than we generally perceive because it is difficult to ascertain and allocate the market actor costs.

Unquestioned acceptance of the EMH does a disservice to market theory, as it has taken a fair working hypothesis and turned it in to an article of faith. This leads to a false dichotomy between “defenders” of the EMH that fail to recognize the cost and fragility of a market and “detractors” of the EMH that feel the answer is to regulate markets as if they are bi-polar individuals in need of medication. I propose instead the constant care and feeding of reputation watchdogs and the empowered of actors at many levels that are

focused first and foremost on disreputable elements entering a marketplace -- misrepresenters, illusory counter-parties, and market makers interested in the outcome.

In the former, there is a hesitancy to correct what is obviously broken (also known as *laissez faire*), whereas the latter creates an instinct is to keep pouring more and more regulatory calming medication in to the patient, not realizing it is fools errand and just killing her. In the final count, *laissez faire* will win out over hyper-medication, as the animal spirits, left on their own, will reanimate a moribund and collapsed market.

However, there is certainly no reason NOT to fix the simple things that ail markets that have veered off track.

An academic debate swirls around the EMH, its offspring, its application, its popularization, its profit generating ability, and its detractors. Forays into behavioral economics have built a convincing edifice in two respects: testable cognitive fallacies demonstrate that in certain instances market actors act inconsistently with their own rational self interest. And yet effective markets can correct because of their capacity for criticism, and even behavioralists credit the EMH as a portfolio management theory (in connection with diversification), because market participants have the benefit of mis-pricings caused by fallacies and fraud in both the up and the down direction.

The markets that matter the most to us are neither innately effective, as the EMH has been misconstrued by some, nor problem children in need of medication, as the behavioralists often portray. The allocation of market costs simply need to be renegotiated when circumstances change. The temptation to get careless or have a sense of entitlement to a working market is real, and it is painful to extract one's self from a market once that market becomes dysfunctional. Why?

Behavioralists would do well to study the cognitive fallacies of market regulators (both private and state) and institutional inertia generally. I suspect they would find confirmation fallacies, group think, and other defensive psychological methods make people reluctant to accept that a once good market has gone bad. But circumstances do change. Technology is introduced. Side negotiations have unintended consequences for other cost allocations. Bad actors undermine reputation systems. All of these

eventualities need to be built into effective markets. Leaders, in turn, need to be trained to assess the health of the many markets that surround them and find remedies when

Of course, the state certainly plays a role in ultimately sanctioning truly criminal activity, but if you ask the head of any stock market from Singapore to London to Chicago what makes their market special, what makes it work on a day to day basis, you invariably land on a consistent point: reputation.

This is a very real life answer, with very real life consequences. If a market loses its reputation, it loses its vital life force. For decades, a combination of factors led to the markets in the United States having the best reputations and drawing the most capital from around the world to participate in them. Unfortunately, that reputation has been badly damaged and it will take significant innovation in the markets to regain that reputation. Leaders need to be finely attuned to reputation and adept at navigating its alleyways.

At its most basic level, reputation is an exchange partner selection mechanism based not upon direct experience and knowledge, but upon (relatively immediate) perceptions about reliability, veracity and intentions. Without reputation, markets grind to a halt because it is simply too burdensome to complete thorough due diligence on a potential partner and their offering within the price and settlement constraints of a functioning market.

The scalability and speed of reputation-based decision-making accelerates actionable knowledge within a community to a significant degree and dramatically enhances efficiency. Hence, reputation is a very adaptive and useful social and economic mechanism because markets -- the main institution of human progress -- rely upon it.

Look no further than the search function on your computer: reputation is at the core of Google's PageRank algorithm, which makes semantic web search lightning fast and relevant (and made Larry Page and Sergey Brin billionaires). Google operates markets at several levels. At its foundation, Google retrieves pertinent information from a sea of possibilities. This is a market in the sense that a multitude of pages on the internet are vying to get found by Google's web bots. The bid is the keyword, the ask is the web page to be found, and the trade occurs within the displayed ranking system.

This free service might appear to be a public good in traditional economics parlance, but the result is no less of a market. Remember, Google is trying to engage in a very meaningful trade with you ... they are engaged in a brutal competition for your time, attention and focus and provide you something in exchange. Of course, Google also makes money by operating a more traditional bid/ask market alongside this organic information retrieval service. Sponsored listings are the subject of an active keyword bidding system where real money changes hands. But the crown jewel of Google is the organic marketplace, where keywords find their page mates via a reputation-based system. Not surprisingly, an entire industry has arisen around advising companies on how to play well in the Google search ecosystem.

Markets with good reputations, i.e. trusted connections, entice new entrants, which in turn enhances the value of the networks by a matter of exponents following Metcalf's heuristic law. So trusted network nodes are the building blocks of an effective market. Tellingly, in practice, Google is as much a security company as an information retrieval company. Google engineers spend more time protecting their PageRank asset from fraud and manipulation, than they do enhancing the underlying algorithm itself. EBay is another example of a successful marketplace built upon a participatory reputation system, and it has a similar armada of anti-fraud mechanisms that protect buyers in the marketplace. [additional details of extent of anti-fraud expenses and activities of Google and EBay]

The need for constant vigilance is an under-appreciated cost of the "free" market equation. Since fraud is deviance, we associate it with rarity. Perhaps this could be called the wishful thinking fallacy. But studies have shown that the temptation for fraud is omnipresent, particularly with impersonal relations. Only when the broad consequences of perpetrating fraud outweigh the benefits does the risk of fraud abate.

There are a number of ways of controlling fraud. Reputation networks are the essential first line of defense, but they also present an organizational paradox. Therefore, leaders need to both master their potential and understand their limitations.

Reputation networks are powerfully adaptive because they meaningfully decrease transaction costs by: (i) reducing the need to individually due diligence and calculate the full range of outcomes, (ii) eliminating the

burden to negotiate and reduce to writing every single contingency (and its enforcement and compliance mechanism), and (iii) bridging the “you first” trade timing quandary. The resulting ease of exchange enables broader specialization and division of labor within the organization because of the confidence that reciprocity will eventually be forthcoming. This, in turn, creates more effectiveness, prosperity and desirable outcomes.

However, reputation networks by their very nature represent potential targets for those intent on engaging in fraud. Trust mechanisms to prevent fraud come in all shapes and sizes. In the traditional family-based and social world, obloquy and ostracism borrowed heavily from religious belief, shared sacrifice and ancestral affiliation (real or mythologized) to create a web of social sanctions. The risk of getting excommunicated from the tribe remains a powerful trust mechanism when group expulsion could mean the difference between life and death or pro-creation and no creation. But this mechanism faces limitations in modern society, which promises tremendous independence from those bonds, even to those who attain that independence simply by beating the system.

Bernard Madoff was only the latest in a long history of fraudsters that abused traditional ethnic and religious affinities and the sanctions that underlay these kinds of traditional trust mechanisms. Assumptions about the trustworthiness among Jews, or Japanese or Mormons have frequently been grist for swindlers. Whatever the spiritual or other rewards of group membership may bring, as trust mechanisms they have had to evolve in order to survive.

Trust mechanisms are no different than any other adaptive social innovation that has mirrored the advancement of human civilization. Early religious rituals often involved bodily mutilation and human sacrifice. Nicholas Wade theorizes that these intense rites of initiation (or high costs of entry) were driven by the demands of early collective warfare and the need to be able to trust the commitment of your fellow co-warriors. Whatever their genesis, the more egregious practices have evolved over time to less gruesome forms. Shared sacrifices have evolved to be at least as instructive and helpful as punitive. Tithing, lay ministry and other measures of sacrifice have replaced those early religious shock treatments. Meanwhile, positive bonding rituals such as song, dance and trance have remained both in religious practice and within secular society.

This evolution has been mirrored in core mythological elements of religion. Thus, within Judaism, Abraham proves his fealty to God by offering to sacrifice his son Isaac, but God deems the offer alone sufficient proof. The offer versus the actual sacrifice had now become a sufficient trust mechanism ... creating a far more adaptive religion from the old tribal tyranny. Christianity goes a step further and offers up a singular sacrifice in the story of Jesus. Adherents need not even take the risky step of offering a sacrifice, but need only believe in the one man who went so far as to offer himself in sacrifice for all. The sacrifice to end all sacrifices.

Religion along with ties of kinship, language and shared ancestry have been powerful and essential trust mechanisms for millennia. Not surprisingly, huge trading networks were given birth by cohesive groups within groups: Greek-fluent merchants in the early Mediterranean, Jews in the diamond business through the last century, Arab- and Anglo-centric seafaring networks.

However, the last century has witnessed an exponential growth in the needs for heterogenous and diverse reputational networks that cannot rely upon traditional social exclusionary mechanisms such as religion, language and kinship. Several forces of hurricane proportion under the rubric of globalization have swept across the economic globe during that period, and only the ability to rapidly produce new trust mechanisms has enabled society to maintain a semblance of order. And semblance is the operative term. Time and time again during this period, we have witnessed a breakdown in markets and the reputation systems that underlay them. It has never been easy to get either markets or reputation correct, but the need for an entirely new order of trust mechanisms has made the challenge increasingly daunting.

On the positive side, the last century has witnessed a notable expansion of enforceable legal and regulatory frameworks throughout the globe. Accounting conventions have been increasingly standardized around traditional double entry book-keeping practices, Western balance sheet conventions, and global accounting house franchises. Linguistic barriers have been diminished through the use of the English lingua franca in business. Despite these positive developments for the prospects of exchange and trade, neither legal action, nor regulatory frameworks, are in and of themselves trust mechanisms. In fact, they are the opposite, as their outcomes are too uncertain in terms of length of process and end result to be

market adaptive. Recall that markets are all about the coincidence of price and time for purposes of settlement. While market prices may not be predictable at any given point, the market process is. Legal and regulatory processes are unpredictable and uncertain by design.

While the implied threat of legal action and the risk of being outside the law (expelled from the group) enhances the trustworthiness of market participants, the law's effectiveness as a trust mechanism is limited to its impact on the immediate assessment of that consequence by those participants. The assessment can vary by individual risk tolerance and numerous other factors, however, unsurprisingly, certainty of consequences leads to more compliance than the severity of those consequences.

Particularly in the context of understanding market environments, the legal system should be assessed by leaders in light of its ability to impact behavior and enforce reputation. Legal processes need to be understood by leaders, of course, but they are not the daily grist of leadership. Trust mechanisms operate for market purposes by creating the trust necessary to trade, not as a result of the process of enforcing sanctions when trust is breached. The two are inter-related, of course, but critically distinguishable. In practical terms, the resort to legal process is an indicator of a market failure -- be it in commercial, financial or political markets. Somewhere along the line, the counter-parties were unreliable and/or the rules of the road were unclear. A key priority of leadership is to avoid both outcomes.

In order to be effective, modern trust mechanisms involve four core elements: mutual transparency, simplicity, integrity and actionability. The primary pathogen in any market is misrepresentation and each of these elements need to be tuned in specific instances to eliminate this threat. Not surprisingly, the job of market regulators is first and foremost to maintain and police the transparency and effectiveness of the markets and immunize the market from misrepresentation.

Misrepresentation is at the crossroads of market plumbing and market theory, as viewed by traditional economists. Securities lawyers are familiar with the Fraud on the Market (FOTM) theory, which is at the foundation of securities laws, and is derived directly from the efficient market hypothesis (EMH). A traditional fraud claim requires a plaintiff to prove they knew of the specific misrepresentation causing the harm and reasonably relied upon it. FOTM requires only evidence of a loss and evidence that

misrepresentation was being made “on the market” at the time of the purchase. Proximate cause is implied by the simple presence of fraud in the market system and reliance is implied by participation in the market. In legal parlance, the act of participating in the market creates the necessary privity for a fraud claim.

In practice, the burden of truth in the FOTM rests upon the company, presumably due to the deterrent effect over the entity that has the most control over material, non-public information impacting the exchange of shares. This premise is not without its critics. With respect to secondary market trading for every investor who lost, another has gained by the misrepresentation. Furthermore, hindsight has a way of shifting our perspective on what might have been “reasonable” to represent at the time. Nevertheless, the FOTM underlines just how important honesty is to the good functioning of a marketplace and should be have its boundaries extended. For a market to be effective, misrepresentation needs to be extirpated not just from the subject of the trade, but also among buyers and sellers in the market and their representatives.

Among the flaws of the Global Settlement and Rule 2711 -- and the reason they have largely worked more harm than good -- is that only companies and their banking representatives were considered threats to the integrity of the role of research analysts. This premise is naive at best. Analysts get “thanked” via commissions all the time for making calls in the direction of one of their institutional investing accounts. They often get tips and information from those same investors. Is this threat from the buy side sinister? Not necessarily. What is problematic is simply if a research analyst misrepresents material facts about a company or its marketplace in his or her communications.

If you come away with only one thing from this book, it is that misrepresentation matters, and that rule applies to all the actors in the marketplace. What Shakespearian drama is not set in motion by duplicity? Drama might be good in the theatre, but it is destructive in the marketplace. Unsurprisingly, much of the dysfunction of markets in the broader sense can be traced to the government stepping in as an actor in the marketplace. Government is not particularly good at transparency (for itself), simplicity, or actionability.

With respect to integrity, the doctrine of sovereign immunity, which remains a foundation of our legal system, prevents the prosecution of the government itself for fraud. Not surprisingly, we witness that government actors have even less incentive than the rest of us to represent the truth when it does not serve their immediate interests. Private actors caught lying face harsh sanctions. The same simply cannot be said for government mendicants. An interesting example of this was when the CEO of Caterpillar was in the embarrassing situation of contradicting the President after a public announcement regarding lay-offs that may or may not occur with the passage of the 2008 stimulus package. The CEO was subject to criminal sanctions for misrepresentation, so he had to tell the truth. The President? His only jury would be the public and too many variables enter the equation for that to be an effective enforcement mechanism.

Interestingly, some of the biggest detractors of EMH, Warren Buffet and George Soros, invest in areas that are closely tied to government action: insurance and currencies, respectively. If sleight of tongue is at the heart of gains due to market inefficiencies, hanging around the government is a good place to get actionable leads. Simply put, government can lie through its teeth with consequences that are indirect at best. If you know when they are lying (or telling the truth when people presume they are lying), then you can make a lot of money.

So what is the catch? Shouldn't it be easy to require and enforce veracity in the market? Couldn't we simply have draconian laws aimed at misrepresentation and deceit and apply these to all actors?

It is not that simple, because counterpoised with the need for veracity in a market environment is the need for information. Truth is not relative, but it is selective. Any testimonial or text has a pretext, context and subtext, all of which can be dispositive for a market actor. Laws that are too plaintiff friendly can place a chilling effect on the free (and often iterative) flow of information. If there are lies, damned lies and statistics, and one wants to focus firepower on the damned lies.

So I am not arguing here for opening the floodgates of lawsuits against public figures that do not tell the truth. I am just saying that the public should be broadly aware of this critical wrinkle in the law, and observers should further sharpen public critique of those who stray from honest representation. Moreover, radical transparency in government is a long time

overdue and the only truly effective way to handle the issues long term. Trust, but verify, was the way former President Reagan used to say it.

Another factor in ensuring information flows in a marketplace is cost. While the internet has significantly lowered the cost of delivering relevant information, it has only made differentiated viewpoints that much more difficult to obtain. The well-intentioned Regulation FD (for Full Disclosure) and Sarbanes Oxley, were meant to provide higher quality information to a broader set of actors, yet we have witnessed the evaporation of information from the public equity markets. Rule 2711, which prevents research analysts from gaining compensation from primary securities issuances, has created a death valley of information flow in the marketplace from broadly available sources. Not surprisingly, the public equity markets in the United States, once the most thriving in the world, have withered on the vine.

The advent of the journalist model for equity research, web tools, expert networks and other serving specifically buy side accounts have compensated to some extent on the buy side, however companies have been unilaterally disarmed in their quest to get information in the marketplace, making it an initial feast for buyers, but little reciprocal confidence for sellers. The Hotel California model, where investors can get in, but they can't get out, is not a long-term effective market model. Furthermore the Cramer model of stock analysis has its limitations.

The market for political ideas has witnesses an ever more rapid deterioration of an effective market. We desperately need a transparency act to revive that market, as we did for the stock market in the 1930s. Institutional biases toward the fraudulent flow of information, such as sovereign immunity, pollute the market and reduce the reputation and value of a connection of actors.

Defamation laws in the United States, particularly the application of the "actual malice" test for public figures, has created a publish-first, fact check later culture among the major media stakeholders. Given well-documented partisan and ideological bias at many of these institutions, it is not surprising that false and misleading information has reached epic proportions in our national dialogue. The marketplace for ideas has suffered as a consequence.

Markets are successful and effective when incentives are in place to encourage the publication and dissemination of as much accurate and

truthful information as is obtainable. It is essential that the marketplace for ideas remains fertile, and that people are well armed to defend the best ideas and vanquish the worst.

In the realm of politics, the analogy to these examples is the cost of making the citizenry fluent not only in the language of politics, but in the key ideas and principles that animate the political process. As a democracy, you should not only have a pretty good plan to ensure that your citizens can participate in a trustworthy manner, but that they are prepared to do so in an informed and productive manner.

The more efficiently you develop an informed and skeptical citizenry and provide them trustworthy mechanisms to participate, the better your collective decisions will be, and the more effective and prosperous your society will become (all other things being equal).

A related and highly relevant topic in the marketplace of ideas as it relates to politics is the question of recruiting, training and policing (for honesty) of political journalists. These professionals, who are remunerated and have significant access to the political idea entrepreneurs, are similar to the A&R rep or the stock analyst. They need to be compensated and vetted to participate in an effective market for political ideas.

The Focus

The most common source of failure in any institution, particularly those dealing in public goals, comes from a lack of rigor in defining objectives in the context of the alternatives. This failure is compounded by an unwillingness to end efforts that have either reached achievable objectives and are no longer needed or will never reach any desirable outcome. Above all, the task of leaders is to bring organizational focus within this light. They must communicate principles, choose personnel, identify priorities and ultimately implement policies with a view toward successfully reaching the objective they set forth.

One of the flaws in the treatment of government reform and policy thinking is laziness in defining the spheres that constitute government, both as a funded corporate body and as a sphere of influence through regulations, court action and public rhetoric. This means that many of the existing efforts and arguments, both anti-government screeds and good government

pabulum, conflate essential issues and muddle through false starts. Unsurprisingly, public leaders schooled in traditional government reform studies charge off in the wrong direction more often than not, as leadership is too often equated with immodesty and personal ambition. Successful public leadership is modest in its objectives (because it understands the limits of the form), but uncompromising in its desire to deliver and account for results.

Dashed expectations born of unrealistic expectations are exacerbated by an industry built up to shift blame for the failure to identify and account for achievable objectives. Leaders who don't define and defend their choices will be tempted to join that destructive exercise. If you add on top of the unhealthy blame game the various cognitive fallacies of planners, regulators, and public interest organizers, you have a witch's brew of ineffectiveness. Leaders cannot be drawn in to this reactive mode and expect to be successful.

While this perspective leads naturally to a philosophy of limited government, it is not anti-government. There are activities that government must do, activities that government can do but might choose not to do, and activities that government simply should not do -- no matter how tempting it might be to promise the moon and the stars. In the first two instances, a well-grounded set of ideals can help to dramatically improve governance and the prospects for peace, prosperity and opportunity for any society.

In the third instance, one is reminded of the William F. Buckley quip that a conservative is a person standing athwart history yelling: Stop. Invariably, it starts innocently with the best intentions. A small program to help first time home buyers turns in to a full scale middle-class entitlement in Frankenstein form that cracks the foundations of the world financial system. A medical safety net for senior citizens and the indigent metastasizes until it overwhelms the entire medical system and threatens over a century of astonishing progress in battling disease and understanding human physiology.

The government is first and foremost an entity which claims a monopoly on the legitimate use of physical force. This definition, first offered by Max Weber, has never been the subject of much dispute. Whatever you might think of the proper government role in society, it is commonly understood to be founded on the potential for authorized violence against its own citizens

and others and the appropriation of wealth through taxation. This is more than just a tautology, it is an essential fact that informs all the organizational dynamics of the government.

On occasion, state violence seems reasonable, such as when police are called to the scene of a convenience store robbery or a country is defending its borders from incursion. But when laying the groundwork for government action -- whether for security or social services -- leaders must always remember: we are talking about the entity with the guns and the presumptive right to use them as it sees fit. Whatever progressive planners might ultimately envision for the use of state power, public leaders need to be aware that the government is, at its core, a regressive organizational form. It was formed to provide defense through violence -- hardly the DNA for hope, opportunity, dynamism and fertility regardless of the best intentions.

The power to use compelling force creates at least one obvious systemic risk: immunity from criticism. Organizations that are impervious to criticism are not places to deposit a lot of unbridled authority. Furthermore, because of the availability of force at the behest of the taxing authorities, the government also has comparatively unlimited resources for legal processes to silence and render inactive people that oppose its efforts.

Again, this is a core reality to keep in mind when thinking about resolving problems of a public nature. Some may wish it were otherwise, or wish to conceive of a state where criticism is openly accepted, elections for leadership dynamic and thoughtful, and functionaries flexible and broad-minded, but by pure act of definition this wish will never come true. In designing a constitutional form of government built on limited powers and internal checks and balances, our Founding Fathers understood this reality ... and so must the new generation of leaders if we are to have any hope of continuing to be successful as a nation.

Because the government holds a monopoly on authorized violence against other people, it is also tempting to default to a view of the government in its simple corporate form -- a direct delivery vehicle for services paid for by tax receipts of one form or another. Both sides of the statist / libertarian divide make this common mistake and accordingly often talk past a plethora of applicable solutions to desirable outcomes.

Nowhere is this fallacy more prevalent than in the realm of government studies and public policy faculties, where practitioners are cocooned in their narrow specialty and see non-corporate government solutions as a threat. Leaders need to be aware of this institutional instinct and look at actions and outcomes in the broadest context of society's overall efforts to address a problem. The corporate model of government is increasingly joined by a much broader array of unfunded regimes that government action fosters and influences through tax policy, regulation, enforcement priorities, guarantees, insurance schemes, and central banking functions. For leaders, this state of affairs presents an ominously complex set of choices and priorities. It has also spawned a multitude of leaderless institutions and practices that can ultimately subvert the best intentions and efforts of those leaders.

Awareness of these non-corporate effects are essential for public leadership. State direct ownership may be less important than the extent and character of the rules and regulations, which create a captive set of actors that form a symbiotic relationship with the state. Whether they are formally government sponsored entities, such as Fannie Mae and Freddie Mac, or in areas such as securities, banking and healthcare that are so extensively regulated and/or subsidized that only a few large players with extensive government relationships can survive in the marketplace, the result is the same.

Moreover, no action that a leader takes on behalf of a public entity exists in a vacuum.

As we witness a significant increase in non-profit and for profit efforts devoted to areas of social welfare, health policy, the environment, economic revitalization, self-certification and other altruistic-minded endeavors, it is essential to factor these efforts in to any leader proposing like-minded solutions, if only to avoid unnecessary duplication or unintended consequences. Social altruism is innate to human nature. Successful leaders know how to encourage, foster and promote this instinct, particularly to accomplish public objectives. Once again, generally speaking, the state is a very poor vehicle to carry out an altruistic agenda. By its very design, it limits social entrepreneurs and risks redirecting efforts to a broader political calculus.

Under some governing principles, public leaders are not even allowed to directly provide a service if a non-government actor is already in place. This potential for "crowding out", which is well-recognized in economic

theory, has broad applicability to public goals generally. More to the point, altruistic efforts have their own processes, accountability, and ideal lifespan and need to be conceived of differently than through a political lens.

A public leader acts within two distinct realms: one of “corporate action” and one what I term “regime action”. Corporate action in its purest form involves taking money in through taxation, fees, etc. and dispensing it out in the form of purchases of goods and services. Leadership in this realm should be similar in scope and focus to any corporate body that is hoping to achieve more with less resources. Efficiency is a central guiding principle, because the elements are so readily measurable. Regime action involves an assessment by leaders of the ancillary impacts of tax policy, regulatory approaches, insurance schemes, currency policy, guarantees and enforcement actions that seek to significantly influence otherwise “ungoverned” activities. Here the goal is not efficiency as much as neutrality. It is essential that leaders understand markets and reputation, because fostering the health of both is critical to their overall ability to succeed.

The line between corporate and regime action can be blurry. In many areas, from social services to healthcare to environmental protection to security to central banking, leaders might operate in both a corporate manner and as influencers. Their corporate activity might significantly influence the policies, practices and economics of third parties, such as non-profits or businesses, even if no formal regime is in place. A regime could be as simple as granting tax exempt status to a community food bank operating as a non-profit or as complex as the securities and banking laws and regulations. As a general rule for leaders to aspire to: the more concrete and parsimonious the guiding texts, the greater the transparency and accountability, and the more effective the fraud prevention elements, the better the regime.

Corporate action by government is readily identified. Taxpayers remit funds to one fisc or another. The tax dollars get sorted out among the tiers of national, state and local entities (and often leveraged with debt), and these funds eventually find their way, by example, into the paycheck of a teacher, soldier, and administrator or contractor. This is Government 1.0. There is significant improvement to be made in the transparency and accountability of Government 1.0, but the mechanism is readily understood.

Government 2.0 is centered principally on regimes. Regime action is far more pervasive and much less understandable than corporate action. This mystery is unfortunate, because regime action is inevitable, often unrecognized, and rapidly growing. In the best light, regime action can accomplish social objectives without resort to the taxpayer's pocket. Of course, indirect costs and inefficiencies, specifically regulatory burdens, are often not appropriately calculated. Furthermore, regulatory immodesty, obscurantism, and an allergic reaction to transparency and accountability are endemic to state actors, whether we are discussing a corporate or a regime action; so leaders need to factor all of this in making decisions.

In any event, leaders should be focused on the resolution of a consensus priority, take full account of all the actors (particularly non-government) focused on that problem and all the tools available to each one of them, and be scored, disclosed and dynamically evaluated in a comprehensive manner aimed at the highest benefit for the lowest fiscal and indirect cost.

A pivotal aspect with both corporate and regime activity is the law of unintended consequences. Flexibility and adaption are therefore essential to any effective regime or corporate action by government. The dichotomy I present should help identify the root cause of such consequences and aid in the search for a remedy.

Above all, a leader must resist the siren song of the totalitarian -- the real Frodo's Ring of temptation. Of course, today's political discourse has generally avoided the term totalitarian. Like the word "fascist", it has become a catch-all bucket of negative connotations with fleeting semantic meaning. This is not unsurprising, considering the the history of its more enthusiastic proponents:

"Everything in the State, nothing outside the State, nothing against the State." - Mussolini

By the term totalitarian, I am referring simply to the instinct that leaders can face to merge organizational efforts that are better served by remaining distinct. So why use such a charged term? More pernicious than the mere instinct to merge organizational efforts are the philosophical underpinnings of such effort. Invariably, this discipline leads to a desire to have all efforts housed under the same roof and directed by the state. I apply the term in this book because I want to emphasis that partial actions in the totalitarian vein

represent a slippery slope down to a state where few nations have recovered without revolutionary violence. Leaders cannot afford to drift unawares into such a realm.

One of the most recognized articulations of totalitarianism comes from Thomas Hobbes, whose social contract theory drives human beings together out of sheer necessity to avoid the brutish travails of existence involving a constant war of one on one. This vision of the individual is antithetical to human freedom and idea fertility. In Hobbes' view, individual self-interested motivation is a malevolent force to be reined in by a greater authority. Society, or rather the overarching violence of the state, is meant to save us from ourselves in essence. Hence, all of our rights and our duties come from the social compact, or the state, without which we would have not peace.

Not surprisingly, this philosophical foundation led Hobbes to a unified theory of state, where commercial, religious and political authority was to be centralized to minimize the "strife" inherent in individual autonomy. But few concepts have proven more sterile than the one articulated by Hobbes and his ideological kinfolk, from Karl Marx to Noam Chomsky.

Hobbes was in some ways a straw man. In real life, he was bested by his contemporary Locke. The founding fathers of the American revolution delivered the most most exceptional nation on earth based upon the primacy of the individual right to self-determination. While the intellectual currency of Hobbes has been significantly devalued in the economically progressive, labor-divided world, it is surprising how the core temptation at the root of Hobbes' worldview rears its head in each historical epoch.

The separation of the ecclesiastical and the political has been a hallmark of advancing civilization since Pontius Pilate stumbled into an ecumenical dispute some 2000 years ago. Every once and while, however, society regresses. Secular Nazi Germany and Soviet Communism sought dominance over (and the elimination of) a variety of religious communities. Radical Islam makes no secret of its efforts to create subservient state machinery in Afghanistan and everywhere else for that matter. Liberation theology operates to enable and justify corruption in poor communities.

The merging of the spiritual and the political is a prevalent example of totalitarianism, and it is not surprising given the cross-currents of temptation

and the shared sacrifice and political / social foundations of religion. Some clearly find it enticing to usurp the state's monopoly on force to win over religious adherents who might otherwise remain unconvinced. Others promoting unappealing political arrangements might enlist religion as a means of buttressing support. One example of this is the doctrine of the divine right of kings prevalent in the middle ages.

Similarly, we can look to all manner of examples of the state entering the commercial arena with vigor or the commercial and the spiritual merging with abandon. The former produced the Yugo, and the latter produced the sale of indulgences. Each resulted in sterility and subsequent revolution in its own right.

When you enter the realms of scientific inquiry (and by relation education), the interplay with politics, commerce and religion may be more subtle, but evidence of foul plays is not hard to come by. Spirituality and religion are by definition belief systems, centered on connecting dots where empirical evidence does not exist, but where human yearning to grasp the unknowable does. Scientific inquiry quite to the contrary is grounded in the principal that you only go as far as the evidence might take you. There can be leaps of faith in science, but they are technically hypotheses. If the evidence does not quickly catch up to them, the premise must be abandoned by serious scientific practitioners. The holdouts have simply turned normal scientific inquiry into scientism, or a belief system that is all the more dangerous because of its scientific veneer.

The entrance of politics, religion and commerce into the scientific realm has produced all manner of abominations to the truth matched only by the certainty of conviction at the time. From Nazi eugenics to snake oil cures befitting a Mark Twain character these combination rarely prove advantageous to society. As a stream of ideas, scientific inquiry survives by and large despite, rather than because, of those influences.

Notwithstanding a raft of what could only be described as bad experiences in its regard, the ecosystem for totalitarian thinking remains surprisingly resistant to disinfectant. We see flirtations with totalitarian thinking every single day.

The majority of these flirtations are inconsequential, if not benign. Toby Keith can sing a satiric song about the "War on Christmas" with the tongue

in cheek totalitarian line that “Uncle Sam and Santa Clause are one and the same” and just in case you were wondering, he has no shame suggesting extremely prejudicial forms of violence to expunge those individuals that might think otherwise. For the record, Toby Keith is one of the most remarkable and tenacious talents in music, and he has written many rousing popular tunes. Still, the further irony of Toby Keith’s song in the context of my discussion is made only stronger by the usurpation of the religious significance of Christmas by the rampant commercialization of the holiday via a secular Santa Claus with almost no relationship to the birth of Christ other than nomenclature. Keith’s song offers up an amusing cultural totalitarian trifecta of the political, religious and commercial.

Often, however, current flirtations with totalitarianism are more consequential than a satiric country song. While no serious thinker today thinks the government should make automobiles (witness the Yugo), the business of certainly politically connected car makers General Motors, Chrysler and Ford, which have asked for government loans and loan guarantees based principally on nostalgia. Ten car companies manufacture cars in the United States. The more successful ones tend to focus on making good cars, rather than lobbying Washington.

Likewise, no one should entrust a substantial portion of their net worth with a basically unaudited hedge fund because of religious identification, and yet we witnessed the debacle of Madoff, who preyed significantly on Jewish goodwill. “He’s a mensch,” so my money must be safe.

You only make that mistake once. Or so it would seem.

The resilience of totalitarian thinking is a mystery, given the evidence of its general ineffectiveness in achieving even stated goals, much less actually desirable ones. Whence this moth to the flame impulse? It may come from innate cognitive reductionism or some other adaptive phenomenon from early tribal existence, where monomania had a hand in our sheer survival. We overindulge in simple carbohydrates to our detriment because of a once adaptive proclivity, so why not simple ideas?

At one point, chief of the hunting party, head shaman, tribal elder and general big man on the savannah may have been critically adaptive. It is hard to argue that is the case today. Or it may be the irrepressible temptation to use the government cudgel and violence generally to advance commercial

or religious interests and affinities is unavoidable. It could also be rooted deeply within our linguistic traditions and our ability to cognate language: notice the affinity of words such as goods (commercial) and God (religious) and govern (political).

In any event, totalitarian thinking persists, it is problematic in most every instance, and the battle against it must be won. So far, I am simplifying the argument against totalitarianism – perhaps to its adversaries’ detriment.

From the traditional conservative right, you can hear that many political theories have their roots in religious ideology and the nation, if not the state, merits a spiritual identifier. Modern states have successfully persisted with an overarching religious affiliation, such as Catholicism in France, the Anglican Church in England and the various strains of Judaism in Israel. The deist phrase “In God We Trust” on the US Currency has hardly slowed the progress of American capitalism. The Ten Commandments are nothing if not a seminal legal code that merits state enforcement in their own right.

At least one early North American colony was founded expressly as a city on a hill, as a nation that made a covenant with God, in explicit reference to a spiritual text, Jesus’ Sermon on the Mount. The quote in its full is deeply evocative and supremely motivational having been borrowed by both Democrats (John F. Kennedy) and Republicans (Ronald Reagan) alike to refer to both American exceptionalism and the weight of responsibility that falls upon leaders generally.

All of this is true.

But the original “City on the Hill” reference with respect to the United States came via John Winthrop, a contemporary of Hobbes, who was no fan of democracy and whose Puritan effort was a transparently a totalitarian effort combining church and state. Fortunately, these earlier ambitions failed miserably; and they were subsequently rejected by other colonists, the American revolutionaries and the Founding Fathers.

John Winthrop’s rhetorical flourish is proper currency for those looking to emphasize the same point that “all eyes are watching us, so behave wisely”; but his lifetime efforts serve as a reminder of the narrow gap between flirtation with, and implementation of, totalitarian ideas.

More relevant to our current state of affairs, doctrinaire Islam makes no secret of its demand for state action both in the legal realm (Sharia law) and in military tactics (the life and times of Mohammed). Most would consider these approaches -- the early Puritan efforts and radical Islam -- a step backwards from the lessons of history and efforts doomed to eventual failure from internal inconsistencies or external efforts.

From the traditional left, you are likely to hear some form of Marxist reductionism, where economic imperatives drive all phenomena no matter how seemingly diverse. Religion is directed toward the masses as an opiate, used to reduce the pain, and distract from the injustice, of the extraction of their surplus labor.

Liberation theology builds on this metaphor, offering up religion as a hallucinogenic, promising to use the state of epiphany to return that surplus labor back to adherents through the state mechanism. Science, education, ethnic identity and more are to be subsumed to the State.

But for the inconvenient truths that transaction costs are significant, governments cannot plausibly identify whence the surplus labor came from and should be returned to, investment resources have meaningful risk / reward demands, and human beings are not invariably beasts of burden, Marx would have had a valid suggestion.

None of this being the case, the economy, and labor markets in particular, are simply too complex and unruly to implement the vision of the liberation theologians and other Marxists, who envision either the elimination, or disturbingly the co-option of religion, as neo-Marxists such as Hugo Chavez and Adnanijead, and others have done, for state purposes.

From the technocratic center, you will likely hear that government has successfully funded any number of basic science and exploration efforts, from the space program to the internet to the study of ocean currents. Most consider public education to be a successful government program, at least compared to the alternative of no education.

Likewise, central banking and the centralization of currency and depositary insurance schemes, backed by the implied balance sheet of the taxing authorities, has arguably helped give policy makers tools to counter balance manias and panics in capital markets. No less an economic liberal than

Adam Smith argued for a role of the government in building basic infrastructure. Many also argue that the tax- exempt status of philanthropic efforts, including religious ones, is a form of state subsidy – and a simple an effective one at that. Again, all true.

All of these observations raise a host of legitimate questions. When can a leader know when they are facing a real totalitarian threat? When is a perceived threat benign and better ignored? When does the combination of separate efforts (that might otherwise seem best disparate) have merit and appear worth the risk of engagement?

Clearly, guidance is in order.

First, any benign combination of efforts in this vein respects the important distinction between the motivational, inspirational, metaphorical and allegorical on one hand -- which every speech act might comport -- and the practical intertwining of the realms that is more pernicious.

The Ten Commandments posted in a City Hall rotunda as an article of historical, artistic or even religious inspiration is not the same as writing these statements in to the laws being enforced in that same building. The failure to acknowledge such difference is sterile formalism – a condition that afflicts much of the current civil liberties debate in the United States. Similar observations would apply to religious invocations at state events, where much ado is often made about an ecclesiastical reference.

Similarly, there is a line between seeking divine assistance and guidance, on the one hand, and claiming divine authority or justification, on the other. Such proximity argues that no matter how scrupulous the language usage, it is best to keep religious discourse out of the state realm. Perhaps.

However, strict rules in that regard might well result in a form of secular totalitarianism, particular if, as I argue, belief-based suppositions are inevitable, irrespective of their wrappings. Discriminating against religious discourse might arguably have the effect of encouraging the substitution of other less overtly allegorical forms of belief – such as pseudo-science or politically convenient morality. In practice, these issues have been relatively well resolved by overarching cultural norms in the United States that limit most of these instances to general deisms.

Second, state action should not be evaluating in the light of morality akin to religious judgments, profits or returns more suited to the commercial realm, or findings best left to the uncertainty and empiricism of the scientific process.

One of the biggest red flags for anti-totalitarians is when a state action is being undertaken on the basis of a claim to moral superiority.

When the language of morality is in play in state action (or business for that matter for leaders following the logic); you can be almost certain, some of the actors are dissembling and the outcome lacks logical authority and a well defined sense of purpose.

A nation (or business) might arguably have a good or bad origins and actors' motivations can certainly be well- or ill-intentioned, but when the state acts, it is not being bad or good, it is merely carrying out a policy either that reflects a total or partial consensus, or does not. Similarly, a business either makes decisions that maximize the returns that conform to expectations of investors or it falls short of that goal.

It is seeking a goal, which it achieves or it does not. It is expending resources efficiently toward an objective, or it is not. Examples of moralizing by state actors are as ubiquitous as they are fraught with a record of failure. As one pundit wrote, those leaders who dwell on the cosmos to often forsake the concrete.

This is not to say that our fundamental common laws and their derivative statutes do not have a profoundly moral basis, be it ecclesiastical or a utilitarian. Murder, theft, fraud, and other crimes, ultimately draw from deep issues of morality. And the morality short-circuit absolutely has a place and time. Leaders need to have awareness of these foundations. Feel them under their feet, not imagine them in the stars.

What I am referring to is moralizing about essential managerial decisions around the implementation of consensus government.

When President Bush described our efforts against militant Islam following the attacks of 9/11 as a crusade, not only did he chose language with inopportune historical connotations and an inappropriate subtext of religious authority, he raised major concerns for those leery of the Leviathan.

Perhaps, to him, as a person, the challenges presented something akin to a personal crusade, a strong personal source of strength akin to the deep well from which leaders as diverse as Martin Luther King, Jr. and Abraham Lincoln have drawn. But a state actor's task is not to bear a cross, but rather to identify an achievable objective, and measure the success toward that end. That cross has already been borne, less we forget.

It does not matter how "good" our actions might have been. We were either achieved success toward an identified end or we did not. Simple moralizing leads down a sterile path, because it short-circuits the feedback loop need to maintain fertile and dynamic progress toward consensus goals. Or put another way, the road to hell is paved with good intentions. Once you lose sight of your objectives, then all the moralizing in the world will not recover efforts for their better purposes.

On the left, we never hear of the effectiveness (or lack thereof) of progressive income taxation, but about the good in and of itself achieved by "the rich" paying their "fair share" of income taxes. This morality play immediately short-circuits a broad range of essential questions and analyses that can and should take place. What is the impact of progressive income taxation on work effort, entrepreneurship and productivity of individuals? What is the revenue impact of progressive taxation? Is there a better way to move funds into state coffers?

If progressive taxation is presented as a good in and of itself as it often is – a "moral" imperative -- then these questions never get asked and never get answered. Also lost in this sterile state of affairs, are the objectives to be paid for, the priorities assigned to those objectives and hence the actual need for any resources. The morality presupposes that any such objectives have been adequately explained and defended, which we know is often not the case.

On the right, one often finds a similar moral imperative around the absence of taxation, as in taxes were innately evil. Given my views around the Leviathan proclivities of the state and its generally insatiable appetite to take on efforts it best not, I certainly sympathize with this political morality play deriving from an Old Testament allegory.

While the instinct to starve the beast might be appealing, it is not useful for anti-totalitarians. The state does need to accomplish some tasks, however limited one might view those tasks, and it needs appropriate resources to do so. Hence, taxation in some form or another is inevitable. Admitting that reality in a forthright manner is more productive than invoking a religious morality play. To those on the right that might object, I would point out that the Left -- founded in Marx -- will develop plenty of hair-brained schemes that deserve complete scorn.

However, attacking taxation as innately evil does not advance the ideas that deserve advancement.

Centrists generally eschew moralizing. They can point with some logic to successful efforts to merge government and commercial or scientific (and educational) efforts. But which ones of these efforts really work? And which ones are on balance totalitarian and ineffective in nature and should be avoided? The need for guidelines built around a set of concentric circles of effectiveness seems apparent.

Let's revisit the initial premise of the state as the entity with a monopoly on the legitimate use of force. Starting from the centermost of a concentric set of circle, it is clear that a public leader's primary role is to enhance the defensive posture and effectiveness of the police and military -- with the later being important for the preservation of the state and the former for the preservation of individuals and their rights. Not surprisingly, the most influential and positive contributions made to the private economic sphere by the government (the internet, jet-powered flight, satellite and other wireless communications, such as CDMA technology, atomic power, etc.) were commercial derivatives of military investments.

Even effective infrastructure expenditures, such as the interstate highways, ports and railway, are partially justified on the basis of policing and military exigencies, including general safety concerns. All of this leads to the more complex arena of expenditure controls and transfer pricing, but for now it is important to recognize the potential for success in this arena for the cross over from the government realm to the commercial realm.

The next circle is in the realm of exploration, both topographical and knowledge-centric. Here again, we have witnessed a record of success from Lewis and Clark to the Apollo program to pioneering efforts in information

technology and life sciences and genome research, which are funded and encouraged by a number of government basic science initiatives. Significant commercialization has followed a number of these explorations, which were aimed, not surprisingly, at extensions of state power. To be clear, I am not arguing here that sovereign territorial expansion is a good thing or a space exploration budget should see no limits, just that the commercial overflow from these efforts, has witnessed some legitimately positive results.

Perhaps it is the nakedly totalitarian-like nature of a state's military and police activities and territorial expansion that allows for distinctions and clarity in these realms. There is no debate that the state must engage in these core functions, just that civilian, rather than military, authority must ultimately prevail at the helm of the efforts. And as with every "found good" deriving from the nation state's efforts (such as the acquisition of natural resources such as oil, etc.), the state has a legitimate and critical role in sorting out the resultant commercial benefits – arguably in a transparent, accountable manner that provides maximum benefit for the populace.

However, as we move away from native functions of the state (use of force, exploration and expansion), we begin to witness increasingly problematic misuses and abuses of science by the state. Pseudo-scientific eugenics in Nazi Germany would, of course, be one obvious extreme driven by purported "public health" concerns; however, even before we meet such extremes, cross-purposes between science and governance are almost immediately in play. Science by definition is an iterative, empirical exercise where even settled concepts are subject to debate and challenge from new evidence. That debate rightfully should be allowed to continue within the scientific community and concerned outsiders to sustain any kind of vibrancy.

However, once commercial or, yet worse, state interests get invested in a certain scientific outcome, history has witnessed all manner of resistance to thought fertility. From Copernicus to Galileo to Danish scientist Bjorn Lomborg, who recently penned a critique of anthropogenic global warming (AWG) published by Cambridge University Press, we have witnessed attempts to silence debate by scientific rivals running to the state for sanction. I am not opposed to a carbon tax a priori, but one would be foolish not to realize that a government that has instituted a carbon tax based upon a theory of AWG will have a severe conflict supporting research that disproves AWG. This conflict is undeniable, and it could only induce sterility.

Conflicts can certainly be managed, but only if they are acknowledged. This takes leaders of character, humility, discipline, knowledge and foresight – a pretty big roll of the dice to bet on those types being readily available when needed.

Dwight D. Eisenhower’s prescient warnings against the military industrial complex prior to the Vietnam War -- where it was arguably a factor in how, if not if, we waged that war -- were part of broader skepticism toward the state’s involvement in any research, development and production. In his farewell address to the nation, he warned: “Today, the solitary inventor, tinkering in his shop, has been overshadowed by task forces of scientists in laboratories and testing fields. In the same fashion, the free university, historically the fountainhead of free ideas and scientific discovery, has experienced a revolution in the conduct of research. Partly because of the huge costs involved, a government contract becomes virtually a substitute for intellectual curiosity. For every old blackboard there are now hundreds of new electronic computers. The prospect of domination of the nation's scholars by Federal employment, project allocations, and the power of money is ever present – and is gravely to be regarded.”

In quick summary: parsing out the benefits derived from native state efforts in the use of force, exploration and expansion might be called totalitarianism 101. We know well the devil we are dealing with in these instances. Further extension of efforts into the frontiers of science and knowledge can generate benefits, but history is fraught with examples of the misuse and abuse of science by states.

If one should be on guard for corruption, patronage and cronyism in the first instance, in the second instance, anti-totalitarians need to be skeptical of scientific inquiry directly supported by the state. This becomes increasingly true the further we move away from the speculative frontiers of knowledge and exploration -- with fewer entrenched interests -- to either commercialization or implications for the expansion of government where a conflict rests.

Publicly funded education faces a parallel path as scientific inquiry. The more we are opening frontiers for children and giving them basic tools to explore the knowledge universe, the less susceptible we are to encountering conflicts. The closer an educational path approaches current state funding activities, the more tenuous the claim to objectivity. It also seems a quite

valid, if not essential, experience, to have public education focus significant efforts on rendering clear and present the mechanics of civic life, if not the status of current debates (which again cut too close to the conflict edge).

The third circle out from the center is in the area of natural monopolies, specifically in the areas of infrastructure, such as roads, rail lines, ports, utility grids and so forth. The concept of natural monopolies (or more precisely practical monopolies) is attributed to John Stuart Mills, who set out to complete the work of his teacher Adam Smith.

Mills was stunningly right about a lot of things – from his vigorous opposition to slavery, to his rejection of racial theories of intelligence, to his support of universal suffrage. These were all positions that were not nearly as current at the time as they would seem now. So his record certainly merits out attention. He was a quintessential dynamist to borrow a concept from Virginia Postrel. Fortunately, there is a tremendous body of work on the topic of natural monopolies and the state’s rightful role in regulating and investing in them.

Generally speaking, there are two broad trends of note in the last several decades: first, due in large part to the pressure from Freidrich Hayek and other economists of the Austrian School, significant scrutiny began to be paid toward how many truly “natural” monopolies might exist. The early net was cast quite broadly (by governments naturally), and everything from trucking, to airlines, to phone service, to waste removal were inappropriately deemed to be natural monopolies. Remember, we are not talking here about network effects, where advantages might accrue from ephemeral, but mutable connections, but instances where monopoly rents were deemed inevitable due to the physical limitations of the desired resource (land to build roads or lay water mains for instance).

As Hayek and his brethren outlined, the theory of natural monopolies depended on costs associated with production and the dynamic of competition, which can change quite dramatically with technological innovation. Fortunately, we have seen operating regulations and guidelines modified significantly in these instances and refocus.

Second, there has been significant experimentation in the manner and means of regulating and financing such natural monopolies. These experiments have taken place on a worldwide basis with some of the most innovative

solutions being found in unexpected places, such as Chile or Singapore. Fascinating and frequently productive innovations have come about to introduce the tonic of competition, reduce the footprint of the regulator and increase policing effectiveness for misdeeds. In many ways, the sphere of natural monopolies is, like the first one, a devil that we know. Perhaps it belongs closer to the first one, than the second one, which requires such a fine balancing act. Nevertheless, here the state can and has been successful, particularly in regime-style activities.

The circle beyond the sphere of natural monopolies flirts significantly with confusion and failure (if not disaster), particularly when we are speaking about corporate government action rather than regime action. In this circle, I put health services, most social and welfare services, the arts, public interest broadcasting, home ownership, business promotion, and many other more recent activities of the government. Of course, these are often tremendously laudable objectives in their own right. Precisely because they are so support-worthy, governments tend to check their analytical skills at the door. Success here has certainly been known to happen here, but a few guidelines are essential.

First, these are areas that are almost always best delivered, if at all, by regime, in lieu of corporate, action. Anyone who has actually experienced state run and managed healthcare or state media is painfully aware of the failings these efforts present.

Ideally, state support for these and other laudable efforts should be limited to a tax shield for givers and for the entities. If the result of a tax shield is insufficient to meet the objectives set forth by the consensus of community, then the next step toward the deep end of the pool would be one of the various flavors of private/public partnerships that have a demonstrated some success. Generally speaking, the more localized, adaptive, time-limited and dynamically scored these efforts are the better. In addition, presuming that adequate performance incentives (and failure penalties) are in place, insurance and guarantee schemes tend to perform better than direct funding models. Most successful state healthcare schemes for example follow this model, for example.

But serious perils abound in ANY move from a simple tax shield to a more elaborate guarantee program by the government and beyond. The disaster of Fannie Mae and Freddie Mac is a testament to good intentions (and some

bad ones) gone terribly awry. In the beginning, the US government supported home ownership with a very straightforward and simple tax shield on mortgage interest. The idea was that home ownership led to all sorts of positive societal benefits, including reduced crime, independent wealth creation, community stability, etc. But policy makers could not leave well enough alone. A variety of government agencies – most notably Fannie Mae and Freddie Mac – stepped up the loan guarantor role under the theory that this could lower the effective interest rate, creating an additional economic incentive to home ownership. The ground was getting a little more tenuous, but the system held together for some period time.

Unfortunately, as with any other government entitlements, the pressure to expand the field of participants proves irresistible (with the class of voters being its only limitation). The only way to expand these programs was to significantly lower the underwriting standards, substantially decrease the market interest rate to provide for affordability, and significantly increase the risk profile for lenders. By 2005, Fannie Mae and Freddie Mac and its handmaidens on Wall Street had migrated from an insurance scheme that not only sought to lower interest rates for already qualified buyers, but qualify otherwise unqualified homebuyers. At the height of its activities in this arena, Fannie Mae and Freddie Mac were purchasing over half the sub-prime mortgage originations in the country. This made companies like Countrywide Mortgage and Golden State Financial very profitable intermediaries in the short term, because these companies were guaranteed a ready buyer for securities that would have otherwise been considered unmarketable. Of course, we now know this business was unsustainable, and we know that the policy-makers behind the scenes expressed a minimal grasp of the breadth of the problems created by having trillions of dollars of fraudulently labeled securities in the market.

The foundational error of this government program was compounded by a number of other factors, which eventually led to the meltdown of the US and world debt and capital markets. While I generally favor regime action over corporate action, it invites the law of unintended consequences like few other activities. Perhaps more precisely, I favor bringing regime action to light, as I believe that the government is engaged in significantly more regime action that it (or the citizenry) is aware of or becomes accountable for.

Turning to Fannie Mae and Freddie Mac, the first compounding factor was the dishonesty of the government relationship these government sponsored entities (GSEs). The GSEs represented an off-balance sheet liability for the United States government. Off-balance sheet obligations are not intrinsically negative, however, when they are undisclosed, as was the case with Fannie Mae and Freddie Mac (and Enron for that matter), serious problems inevitably ensue. The implied guarantee of the US Treasury for Fannie Mae and Freddie Mac undoubtedly inflated credit ratings and spawned a three-fold malevolent phenomena in the private sector – an expansion of previously suspect sub-prime and Alt-A loans under the “cover” of government action (if Uncle Sam’s doing it, it can’t be all bad), a crowding out effect, where the private industry took on increasing marginal loans as the government entered the market and received a priority to the less riskier tranches, and a floor-becomes-the-ceiling phenomena, where the statutory capital ratios applied to private sector were corrupted by a reliance on failed ratings agencies, that in no way reflected the real risk that lenders were undertaking. So what seemed like safe capital ratios were anything but safe.

Had the thesis of this book been followed earlier, it may have been more apparent that these programs were would be a disaster. Why?

First, the GSE efforts involved activity (improving home ownership), which was a laudable, but non-core capability of the state. In constitutional legal jargon, such an effort should be subject to strict scrutiny. Or in my words, you better have a damn good reason that you are doing it and it cannot currently be accomplished without a state role. At a bare minimum, the home ownership imperative should have had a specific, identified driver attached to goals that were realistically achievable and limited in their aims. In hindsight, there was little, if any, reason to move beyond mortgage interest tax deductibility, which is already a massive subsidy to the home-ownership effort.

The original idea behind the mortgage guarantees for certain loans (known as conforming loans) was that first time home-buyers might face unreasonably high interest rates due to a lack of credit history. But the broad expansion of consumer credit in the United States since the 1970s essentially eliminated this concern. The credit scoring industry has a pretty good idea of the credit-worthiness of almost every 25 year old in the country. Once the inadequate credit rationale for first time homebuyers had

become an anachronism, the federal guarantee industry should have died a natural death. But as with so many other well-meaning government efforts that have lost their original *raison d'être*, they continue on either as lifeless shells or, more problematically, with expanded or unrelated mandates.

This is where we found ourselves when the federal mortgage guarantor agencies decided that the anachronistic mission -- of helping first-time homebuyers of unknown credit risk lower their interest rates -- needed a facelift. Hence, a modestly defensible tax deduction scheme turned into a marginally defensible guarantee / insurance scheme, which turned in to an indefensible and (unsurprisingly) hidden government direct lending and wealth transfer scheme to otherwise unlikely borrowers.

Left to its own devices, the mortgage industry would have undoubtedly developed securitization, credit default swaps, and other financial instruments that have been on the whole successful means of managing and allocating risk. However, without the government as a policy-based buyer of uneconomic loans, it is doubtful that sub-prime loans would have morphed en masse in to the AAA-rated securitized bonds that infiltrated the financial system like a virus and destroyed a good portion of the credit infrastructure. The profit motive has surprising limits when an illusion loses its sponsoring magician. Once the credit infrastructure tumbled and savvy investors could buy (real) AAA mortgage bonds with 18% cash pay coupons, the allure of other instruments, particularly equity, became negligible. The corresponding collapse in equities further exacerbated the downward cycle.

Any discussion of the GSEs and the financial crisis raises a few additional questions.

First, the idea of a central bank and a single currency has been a subject of debate going back to the founding fathers. Hamilton and Jefferson weighed in on opposite sides of the topic, with Hamilton eventually getting the upper hand and helping found the first central bank. That central banking effort died a few deaths in the ensuing period, before being resurrected in its current form about a century ago. Properly composed, a central bank, tacitly supported by a government (or perhaps by several governments like the European Central Bank), can be an effective means to maintain the price and currency stability desired by merchants and producers of goods and services. As with any activities in the realm of economic welfare, the more active the

role that the state plays in determining the policies, personnel and procedures of the efforts, the more troubled the history of the endeavor. Ideally, the state role is limited to granting an anti-trust exemptions and using the bank as its own bank on commercially customary terms. This is the formal status of the Federal Reserve, or US central bank, although arguably the inability of the Federal Reserve to avoid the spotlight has put pressures on it to do much more than its native capabilities.

Of course, any time the state acknowledges a monopoly and becomes a key customer, it needs to be conscious of pricing power both in borrowing and in lending. Ironically, the problems have mostly arisen not when the state is limiting the Fed profits, which revert to the US Treasury, but rather when they succumb to the temptation of losing money (by mis-pricing risk) to curry favor with a current administration. We saw such pressure clearly in operation with the GSEs.

Additionally, the US government has a perverse incentive with respect to any crisis that might generate a “flight to quality”, as this tends to lower its overall borrowing costs, thus encouraging more government borrowing and influence over the economy. This skewed incentive ultimately confuses cause and effect and overstates the ability of the government to “adjust for” the native ebb and flow of consumer and business confidence without causing more harm than good. Nonetheless, among totalitarians, there is a tremendous faith that the government should (and can) compensate for technology, business and capital cycles. In most every instance, this faith is misplaced, if not counter-productive.

Currencies are unique among commodities in that the supply (and on occasion demand) is determined directly by government fiat, not by concrete reference points such as proven reserves and actual or projected demand. A government’s taxing ability, repayment track record, and interest rate offer bears on the value of the currency as a mechanism for acknowledging public indebtedness, but ultimately the government’s power over the value of this “commodity” is constrained only by default parameters.

This moves us in to the government role in the debt and equity securities market. Historically, the US Government had not been an active participant in the equities market, which was one reason for the success of those markets. They have, however, been significantly involved in the debt capital markets, both as a bank regulator, and more problematically through the

GSEs as a dealer and issuer of debt. This has created a serious problem, as their participation in the debt markets as an active principal led them astray from their objective role as a regulator and enforcer of anti-fraud and market manipulation rules. Just at the time when they should have turned their attention from fraudulent equity research, toward the potential systemic problem of fraudulent debt ratings, they took a flying pass – because this would have deeply implicated their own failings in policing the trillions of dollars of issuances coming from the GSEs.

The Leviathan is real. It is a constant temptation. And it is an idea that must be battled and defeated, if we are to retain the economic and ideological freedom necessary to fight future battles. Leaders have no higher calling.

The Sunlight

Transparency is a uniquely modern challenge for today's leaders.

The digital information economy has generated an unprecedented amount of data. The ability to record, store and retrieve that data in an increasingly organized and relevant fashion has resulted in new organizational models across disciplines and geography -- empowering amazing efficiencies with deep troves to plumb for analysis and decision support.

However, leaders are now challenged by a situation that has been demonstrated repeatedly in the last decade: with a simple thumb drive or internet file transfer, entire organizations with their people and their history can be laid bare to the world. Effective leaders must now anticipate such sabotage; and in the electronic age it can be more consequential than ever. Reputation, the ability to exchange, and progress hang in the balance.

Putting aside the technical challenges of securing data, every leader must also make the critical decision of who gets what data when within an organization. In fact, these information access rules now define the very organizational form itself, and the first job of a leader is to know who they are leading, to what purpose, and with what tools.

Notwithstanding this obvious state of affairs, leaders and organizations apply comparatively little thought to this dynamic. What thinking that does get employed around transparency and information access is usually done by the legal department in a reactive mode -- focused not on the potential for

innovation and accomplishment, but the possibility of misuse, from the information. The failure to incorporate a pro-active, market centric approach to data access represents a missed opportunity to better define an organization's mission and core competency. In addition, by failing to anticipate and diffuse the impact of broader access to information (planned or inadvertent), a leader's failure is practically guaranteed.

Organizational definition for businesses and not-for-profits have several layers of complexity tied to the core value proposition offered by that business. While some basic rules apply across the range of choices, policies accordingly vary broadly.

In the management of public bodies, however, the objective is more straightforward. With few exception, the more transparency, the better. This is the people's business as is often repeated. It has been nearly a century since Louis Brandeis wrote: "Sunlight is the best of disinfectants", and the weight of American jurisprudence and regulatory effort has leaned against the inertia of secrecy. In 2007, conservative Republican Tom Coburn joined forces with then junior Illinois Senator Barack Obama to sign the [transparency act], which provides for transparency down to entry-level accounting be posted on the Internet.

Clearly, this effort and similar ones at the state and local level, represent essential and invaluable progress toward open public operations and eventual accountability. Because our competitive options are limited in dealing with the government, we require transparency and accountability more than in any other organization.

Despite this reality -- or perhaps because of it -- opaqueness remains the rule in the government sphere. For all its sunshine laws, freedom of information acts, and fervor to open up the books of private enterprises -- the government is often reluctant to embrace simple transparency technologies and are adept at avoiding significant scrutiny. This is particularly the case where its own decision-making processes might fall under scrutiny and their organizational survival, growth and influence might be challenged. As surprising as it may seem, completely open financial statements, replete with check registrars and entry-level accounting for government agencies and government concessionaire of one form or another are extremely rare.

Extensive and byzantine rules govern many aspects of the government procurement, for example, yet little effort has been put in to straight forward winners like reverse bidding, entry-level financial disclosure, and audited financial statements. The government has promulgated a sea of regulations around campaign finance, yet seems incapable of enacting basic pay-to-play prohibitions for contractors, lobbyists, corporations, and unions seeking government spoils or provide basic auditing and control functions for campaigns.

The government grants significant concessions and favors to many areas of non-profit efforts, while demanding less disclosure, even to donors, than one might find relative to the ingredients on a box of cereal.

Without transparency, accountability is elusive. Without accountability, it is impossible to determine if a government action, be it corporate or regime-based, is actually successful and deserves to be continued (or should be ended). Would you invest your savings in a fund that never provided you a financial statement? If the Madoff incident accomplished anything, it was to disabuse everyone of the notion they can blindly trust others with their money without transparency or accountability.

A leader implementing a transparency policy will face three valid challenges: physical security, personal privacy and commercial advantage (related to market incentives). The first challenge (physical security) can generally be met with reasonable safeguards. Personal privacy has a time and place, such as restrictions on the sharing of personal financial statements or healthcare records, with the public (or within the organization) if they are required for submission. However, the extension of privacy protections to limit the ability to judge the performance of employees, particularly public employees has generally nefarious implications.

In this age of ubiquitous information and cyber-tipsters, distribution of valued information is practically free. Yet, this has not created a frictionless marketplace. The main barriers to the marketplace of ideas are access to media, particularly interactive new media, prioritizing the flood of information, through traditional editorial selection or social media, and the ensuring the knowledge and absorption of the recipients (i.e. an educated citizenry), none of which are trivial tasks or free of charge. While there is much to be said and written about with regard to radical transparency in

business and society, my focus remains on the government and political life of a democracy, because I believe that is where transparency is so essential.

As a baseline, there is no reason for the government and the political process to be anything other than an open book from start to finish. This means all committees, all proceedings, all drafting sessions, all mark ups, all budgets, all expenditures, all accounting down to entry level, all benchmarks -- in short everything should be accessible on the Internet in real time by anyone who wants the information. While corporate activity and government processes have long been an area of activity for transparency advocates, I would argue that broad-based accountability, benchmarking and ratings can only happen when transparency is extended significantly through the system to include regime action (and beyond).

On the commercial side, we have witnessed that since the 1930s when the securities laws opened the doors for transparency to companies selling shares to the public. While the growth in ancillary rules and regulations have now begun to hamper the effectiveness of the public markets and driven quite a few companies back underground, the core sunshine principal remains a reliable guide. Importantly, even the analysts involved are required to disclose personal holdings and interests, in order to provide an independent assessment of the writers' potential conflicts.

A deep push for transparency would extend disclosure and transparency out even further -- to all sorts of additional realms of government concession, including the non-profit sector (putting aside religious organizations for first amendment reasons or other disclosures that might violate personal privacy), recipients of research and development dollars, where complete and full disclosure of methods and results should be required if the recipient involves government dollars, political parties and other recipients of government largess, franchise and concession.

While a number of private organizations monitor to some extent the efficiency and effectiveness of these non-government agencies, it is essential to have a consistent level of transparency across the spectrum of publicly-focused action, so that an apples to apples comparison of effectiveness can be made. In some instances, government corporate action may indeed prove to more efficient for a given objective than regime action, but we do not know that without the viral effect of disclosure laws.

Another crucial area for transparency would require that professional journalists, those that are paid by the state directly (such as NPR) or by concessionaires or government contractors, such as radio, broadcast and cable journalist should be required to disclose their voting records.

While a web or print exclusion might well be in order, because they are not subject to the same government concession advantage, if the owners hold sports franchises, which benefit from tax subsidies and anti-trust exemptions, then they would be subject to the disclosure rules. This type of transparency would hardly be unprecedented, as it parallels the requirements equity research analysts face in disclosing their personal stock holdings. This would represent a healthy ray of sunshine on the political process, which is perceived by many to be rigged by political journalists with statist agendas given the importance that access to state actors has to their careers.

I believe radical transparency in government would go a long, long way to keeping the Leviathan at bay, because secrecy is so essential to maintenance of power by the state.

The traditional objection to a radical transparency rule would be in the area of national security and policing operation, specifically instances where the ill intentioned might seek to gain a distinct advantage over the forces protecting the physical safety of citizens. While this is a valid objection that deserves scrutiny and proper enforcement, many security classifications are of dubious value. Weighed against a more open system, one wonders if a if greater intelligence and better security as a result of broad feedback loops.

Already, our security agencies risk being left far behind the flow of information from webizens, be they professional or amateur. As an example, in coverage of the Iraq war the work of Michael Yon, a web journalist, was anywhere from 6 to 12 months ahead of the curve from the mainstream media and one has to wonder if it was not superior to the flow of information (and certainly analysis) up through the chain of command to the White House. Michael was far out ahead of the traditional media in describing the impending civil war following the bombing of the Samarra Mosque by Al Queda in 2006, and he was also well ahead of the curve in declaring victory in the war during the Summer of 2008. This does not mean that war-planning sessions need to be web-cast, but it does argue for additional transparency with regard to decision-makers seeking to understand the status

of the conflict. Perhaps more to the point, the era of “Trust Us” government is certainly over.

This position would argue for particularly broad disclosure related to country and intelligence analysis, basic understanding of military programs and readiness. Some argue that we are at a tactical disadvantage by letting the other side know what we already know about them, and perhaps more critically, such a posture would expose our “sources and methods” of intelligence gathering. My articulation does not preclude an “unknown” quotient, where evidence is simply not sufficient to release toward any conclusion, nor would it encompass compromising sources and methods of gathering intelligence, which would clearly need to remain well guarded.

There would be impetus for agencies to put things in the unknown category when it might not wish to disclose its sources and methods, but considering the alternative, this might not be an insurmountable obstacle. Others argue that disclosure of compromising facts limits are ability to control certain sources with compromising information. One noted example of that was Yassir Arafat’s personal life, which apparently involved trysts with underage men and other scandalous behavior. One has to wonder what national interest it serves having men of this type, as vulnerable as they are, in our particular thrall.

Of course, where this is leading is that the intelligence failure that has been so widely reported in the lead up to the war in Iraq. While the extent of knowledge available to the American public and its representatives in the run up to the war is subject to some debate, there can be no disagreement that a continual, full disclosure of information leading up to the war, including the doubts, would have laid the premise that a certain amount we do not know and that any action must be taken within that light. This would have undoubtedly created a much broader net of support for the war effort, particularly

One additional conundrum is that many aspects of our governmental system (and particularly the political system) are viewed as adversarial, which means a high priority is placed on strategy and tactics versus consensual decision-making. Adversarial parties are very reluctant to open up caucuses and other processes that might put them at a tactical disadvantage. Notwithstanding George Washington’s admonitions about partisan rancor, it does not appear that traditional political parties will disappear anytime soon

or that we'll install a parliamentary system to accommodate additional parties. When the rights of private parties and rights of association are not implicated, the privacy privilege should be regarded as suspect. Radical transparency is certainly problematic for entrenched interests, including traditional political parties, but the objective is to improve the speed and quality of decision-making, not install one particular party or the other.

Publius #10 factionalism - a wide open party process. The initiatives of the Sunlight Foundation are one of the strongest non-partisan efforts to provide disclosure in the executive branch and legislative branch.

Election Fraud

Evidence-based decision-making

Mutual transparency -- new TSA screening process. David Brin.

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The current land of political discourse is a frustrating one for those of you have followed the some of the lines of reasoning – perhaps unconsciously before reading this book. The discourse appears to be split between the anti-intellectuals on one side and the pseudo-intellectuals on the other.

Anti-intellectuals have a visceral reaction – perhaps wisely – to abstract thought and language. They do not care to distinguish between the unfettered discourse of the sophists and the cold clinical language of the pedants. In many ways, they are not wrong. For the vast majority of our day to day decision, very concrete responses, to very concrete problems suffice perfectly.

The Leaders:

Scott Brown

Richard Branson

Magic Johnson

FDR

ⁱ Arthur Schopenhauer, “The Art of Being Right”. A short treatise on the arguments to use to win an argument, whether you deserve to o

ⁱⁱ Basic sets forth the theory of Fraud on the Market, which is the foundation of private actions in securities class action lawsuits. In essence it eliminates the requirement of reliance in fraud cases.